SUPERIOR COURT

CANADA
PROVINCE OF QUEBEC
DISTRICT OF MONTREAL

No: 500-05-001686-946

DATE: April 14, 2011

IN THE PRESENCE OF: THE HONOURABLE MARIE ST-PIERRE

The Estate of the late Peter N. Widdrington
Plaintiff
v.
Elliott C. Wightman and AL.
Defendants

JUDGMENT

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[1] Time has come to put an end to the longest running judicial saga in the legal history of Quebec and Canada.

[2] Time has come to decide the plaintiff's claim, one of many claims made before our Court by lenders and investors in Castor Holding Limited ("**CHL**" or "**Castor**") further to Castor's bankruptcy in 1992 and, in so doing, to communicate answers to various common issues that will be binding in all of these other files.

The Case in a nutshell

[3] The core issue of this case concerns professional responsibilities and whether the defendants, chartered accountants and partners of the accounting firm Coopers & Lybrand ("**C&L**" or "**Coopers**"), were negligent in the performance of their work and the issuance of their opinions for Castor and whether they should be held liable to indemnify Peter Widdrington's estate ("**Widdrington**") for its alleged loss of $2.7 million further to Castor's collapse and bankruptcy.

- Are under review, the work done for the 1988, 1989 and 1990 audits and the work performed in preparation of valuation letters of Castor's shares.

- Are under review the following opinions issued by Coopers: the 1988, 1989 and 1990 auditors' reports on the consolidated financial statements of Castor, the various valuation letters issued during that period and until November 1991 and the various certificates issued to support legal for life opinions signed by McCarthy Tétrault.

[4] Given the claims made in other files and the binding effect of the present judgment on all common issues, more than $1billion in claims is at stake for Coopers in case of an adverse decision on the negligence issue.

[5] The four fundamental questions - the first three being common issues and the fourth a specific issue to the Widdrington file - are[1]:

1. Were the audited consolidated financial statements of Castor for 1988, 1989 and 1990 materially misstated and misleading?

2. Did C&L commit a fault in the professional work that they performed in connection with the subject audits of Castor, the valuation opinions that they issued and the legal for life certificates?

3. Taking into account that Castor is incorporated under the New Brunswick Corporation Act, that Coopers performed its work in various worldwide locations under the responsibility of a Montreal engagement partner and always issued the consolidated financial statements and other opinions out of its Montreal offices, that Widdrington resided in Ontario while various other claimants live in different European countries, what is the governing law applicable: New Brunswick or Ontario common law, Quebec civil law or another law?

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[1] The parties have submitted numerous questions that the Court should consider in her deliberations - there are 176 questions on the final list of questions : see the Minutes of trial, conference call of May 19, 2010, annex G

4. Did Widdrington suffer damages and, if he did, is there a causal connection between a fault of C&L and those damages that render Coopers liable for same?

[6] Castor raised, borrowed and loaned money for real estate properties located in Canada and the United States until it collapsed and went bankrupt in 1992.

[7] Castor operated as an unregulated financial intermediary, a private company: Castor presented itself as a spread lender, placing deposits and loans from private and institutional investors and banks, many of which were Europeans, into high yield mortgage and equity loans.

[8] Castor operated internationally out of its head office in Montreal. It had various subsidiaries[2], namely in Curacao (Netherlands Antilles)[3], Zug (Switzerland)[4], Rotterdam (the Netherlands)[5], Cyprus[6] and Dublin (Ireland)[7].

[9] The accounting for the Canadian operations and the corporate consolidation was performed in Montreal at Castor's offices. The accounting records for a number of the subsidiaries were maintained in Zug (Switzerland) and Schaan (Lichtenstein) by companies called Aurea Treuhand and Global Management.

[10] Coopers & Lybrand were CHL's auditors from the company's inception[8] and Elliott Wightman ("**Wightman**") was, at all times, the engagement partner in charge of the Castor file.

[11] Under the responsibility of Wightman, two teams were involved to audit CHL and some of its subsidiaries: the Montreal team, who worked out of Castor's head office in Montreal and the overseas team, who performed its work in Zug and Schaan.

[12] Consolidation work, final wrap-up meetings with Wolfgang Stolzenberg ("**Stolzenberg**"), the mastermind behind Castor, and issuance of the consolidated audited financial statements always took place in Montreal.

[13] Other professional services in litigation rendered by C&L to Castor like the issuance of share valuation letters and the issuance of certificates in support of Legal for Life Opinions were also rendered out of the C&L Montreal office.

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[2] PW-16-3 and PW-2893-2
[3] CHIF – see PW-2400-18, PW-2400-20 and PW-2400-42 (bates 016638 and 016639)
[4] CFAG – see PW-2400-18, PW-2400-20 and PW-2400-42 (bates 016638 and 016639)
[5] CHINBV – see PW-2400-29 (bates 016301), PW-2400-34 (bates 016396)
[6] CHIO – see PW-2400-75 (bates 017084), PW-2400-98 (bates 017713 and 017714), PW-2400-101 (bates 017783) and PW-2400-102 (bates 017817)
[7] CHII – see PW-2400-75 (bates 017084), PW-2400-98 (bates 017713 and 017714), PW-2400-101 (bates 017783) and PW-2400-102 (bates 017817)
[8] PW-2400-14 (bates 016044), PW-2400-17 (bates 016112 and 016113), and PW-2400-20 (bates 016157)

[14] Widdrington invested in Castor in October 1988, December 1989 and October 1991. He became a member of its Board of directors on March 21, 1990.

[15] Widdrington claims that he relied upon the Consolidated Financial Statements of Castor audited by Coopers, the Auditors' Reports and the Valuation Letters also prepared by Coopers, as well as the Legal for Life Opinions, to invest in and to loan substantial sums of money to Castor and moreover, to approve as a Board director, the declaration and payment of a dividend for which he was sued further to Castor's bankruptcy.

[16] Widdrington claims that he would simply not have made investments in Castor absent the unqualified opinions of Coopers, one of the world's largest and most prestigious accounting firms.

[17] Widdrington alleges that such reliance was reasonable and that Coopers should be held liable for all damages he sustained further to his investments and to his decision on dividend.

[18] Other lenders and investors make similar allegations.

Plaintiff's position

[19] Plaintiff submits that:

- Overwhelming evidence shows that C&L failed to perform their professional services in accordance with the standards of the day and that such failures were blatant, pervasive and inexcusable faults.
- Castor's loans and revenue were overstated by hundreds of millions of dollars and the audited financial statements bore no relationship to the reality of Castor's true financial position.
- Quebec civil law applies - where C&L negligent acts and faults took place.
- Widdrington's reliance on Defendants' professional opinion was unquestionably reasonable in the circumstances.
- Widdrington suffered damages as a result of Defendant's numerous faults and should be indemnified.
- In the specific circumstances of the Castor file, same conclusions would ensue should the Court come to the conclusion that she has to apply the New Brunswick or the Ontario common law.

Defendants' position

[20] Defendants submit that:

- Castor's audited consolidated financial statements for 1988, 1989 and 1990 were not misstated and the results of Castor's operations and the carrying values of its loans were fairly presented in accordance with generally accepted accounting principles ("**GAAP**").

- Subsidiarily, if the Court concludes otherwise, Castor was one great «*theatre of misconception*» and the fraud was so pervasive that it prevented C&L from uncovering the true nature of the misstatements on the financial statements.

- The governing law is the New Brunswick common law, in light of the corporate legislation applicable to Castor ("lex societatis"). If the Court comes to the conclusion that the *lex societatis* does not apply :

    - Ontario common law applies to the Widdrington case, where Widdrington resided and where his prejudice occurred, if any; and,

    - Various other laws apply to the other cases, depending on the domicile of the plaintiffs and the location of their respective prejudice.

- None of the investments made by Widdrington can be attributed to his reliance upon the auditor's reports on the financial statements of Castor, the valuation letters signed by C&L or the Legal for Life Certificates issued to McCarthy Tétrault with respect to its Legal for Life Opinions. Overwhelming evidence clearly shows that the determinative factor that led to Widdrington's investments was his absolute faith and blind trust in Stolzenberg.

- Defendants are not and should not be held liable for Widdrington's alleged damages.

- In the specific circumstances of the Castor file, same conclusions would ensue should the Court come to the conclusion that she has to apply Quebec civil law.

The Judgment's content (road-map and features)

[21] Writing clear and complete but concise reasons represents a titanic challenge.

[22] Evidence focuses on hundreds of corporations, numerous individuals involved and quite a few real estate projects.

[23] Above and beyond the testimonies rendered *viva voce* by 30 witnesses[9] during over 260 days of hearing (between January 14, 2008 and May 2010), the evidence namely includes:

- More than 100 days of examination of twenty-five C&L staff members and partners[10] that took place in the 90s;
- Thousands of pages of thirteen rogatory commissions[11] that took place between 1998 and 2003;
- Thousands of pages of testimonies rendered on discovery or during the first trial which were introduced into the court record by notice under section 398.1 *C.p.c.*, by consent or further to judgments rendered by this Court during the second trial[12];

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[9] Lay witnesses: Harold James Blake, Harald Boberg, Mari Elizabeth Ford, Bernard Gourdeau, Barry MacKay, Norman Martin, Jean Guy Martin, Ingrid O'Connor, Walter Prychidny, Paul Quigley, Cynthia Rancourt, Ronald Smith, Kunjar M. Sharma, Manfred Simon, Ruth Tooke, Udo E.O. Riedel, Helmut Schreyer, Heinz Schoeffel, Elliot C. Wightman; Expert witnesses: John Campion, Earl Cherniak, Kenneth Froese, Russell Goodman, John Kingston, Alain Lajoie, Alain Lapointe, Phillip Levi, Lawrence S. Rosen, Donald Selman and Keith Vance

[10] Examinations of the following persons: Elliot C. Wightman, Michael Hayes, Michael Pollock, Mari Elizabeth Ford, Misti Jordan, Tarek Kassouf, Martine Picard, Martin Quesnel, François Quintal, Daniel Séguin, Jean Guy Martin, John Grezlak, Zymunt Marcinski, David Hunt, Linda Belliveau, Kenneth Mitchell, Penny Heselton, Stéphane Joron, Gary Hassard, Donald Higgins, Pierre Lajeunesse, Bruce Wilson, Janet Cameron, Allan Cunningham and John Bolton. (for the precise dates of those examinations – see the minutes of trial of January 7, 2008, annex C)

[11] Examinations of the following persons: Jurg Bänziger, Gaston Baudet, James G. Binch, William P. Cunningham, Lellos Demetriades, David T. Smith, Harold B. Finn, Ernst Gross, Antonios Hajiroussos, Clifford A. Johnson, James F. Moscowitz, Ira Strassberg and Michael Zampelas.

[12] Examinations on discovery of the following witnesses : Bernard Gourdeau, Ronald Smith, Michael Dennis, Elliott Wightman, Peter Widdrington and Heinz Prikopa (see minutes of trial of January 7, 2008, at pages 4 and 5 with attached annexes); Transcriptions from the first trial produced further to an agreement between the parties and with the consent Court: Christine Renaud, Soo Kim Lee, Leonard Alksnis, Peter Widdrington, Heinz Prikopa, George Taylor, Fitzsimmons, Jarislowsky, Lowenstein, Morrison and Lajoie (see the minutes of trial of January 7 and 8, 2008; the minutes of trial of March 3, 2008 and the minutes of trial of). Extracts of the transcriptions of the testimony rendered by David Whiting in the first trial (see the minutes of trial of December 8, 2009 , pages 5 and 6 and annexe A (pages 12 to 20) and the minutes of trial of December 10, 2009 and transcription of December 10, 2009 pp. 4-5); Extracts of various transcripts produced into the Court record further to judgments rendered (see namely Judgments rendered on January 27, 2009, April 3, 2009, April 6, 2009 and May 13, 2009)

- More than 5,000 exhibits representing several hundred thousand pages, of which experts' reports produced by the 14 expert witnesses[13] and relating to the following topics: generally accepted accounting principles, generally accepted auditing standards, fraud and the auditor, preparation of share valuation reports, principles of due diligence applicable to the purchase of shares in a private corporation, principles of common law relating to negligence and liability further to a misrepresentation and an alleged pure economic prejudice and Canadian and American economy in the late 80s and early 90s.

[24] Hoping to facilitate the reading and the understanding of the reasons that lead her to her conclusions, the Court introduces a road-map, and some features, of the present judgment.

Road-map

[25] The Court follows the following road-map:

- Description of some historical background of the trial.
- Enunciation of her main conclusions.
- Introduction of the main players and topics through a "who's who section".
- Description of the issues and of the task.
- Analysis of the negligence issue as it relates to the consolidated audited financial statements of 1988, 1989 and 1990.
- Analysis of the negligence issue as it relates to the valuation letters.
- Analysis of the negligence issue as it relates to the Legal for Life Certificates.
- Analysis of the reliance issue.
- Analysis of the liability issue, including the applicable law.
- Analysis of the damages issue.
- Analysis of the costs issue.
- The conclusions.

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[13] John Campion, Earl Cherniak, Kenneth Froese, Russell Goodman, Stephen A. Jarislowsky, John Paul Robert Kingston, Alain Lajoie, Alain Lapointe, Phillip Levi, Paul J. Lowenstein, Donald C. Morrison, Lawrence S. Rosen, Donald Selman and Keith Vance

Features

[26] An alphabetical list of names, abbreviations and main technical expressions is attached to the present judgment as a reading tool.[14]

[27] A detailed table of content is also attached to the present judgment.[15]

[28] Summarizing all evidence is impossible: therefore, the Court relates the relevant evidence, as she understands it, issue by issue, referencing through footnotes as much as possible.

[29] Early on in the judgment, the reader will find some general remarks on credibility and reliability of evidence. Additional remarks, with explanations and illustrations, are made under relevant and specific headings and subheadings of the judgment. General and additional remarks complement one another.

Historical background

[30] Further to Castor's bankruptcy in 1992, many lawsuits were instituted in the early 90s, all plaintiffs making similar allegations of professional negligence against Coopers.

[31] From the outset, a judge was designated to manage and coordinate all these cases[16].

[32] On February 20th, 1998, a ruling was made «*to ascertain that the issues raised in these actions be tried as efficiently, expeditiously and inexpensively as possible while never losing sight that our conception of justice is a delicate balance of right results, fair procedures and effectiveness*»[17] .

- One case was selected to proceed first: «the Widdrington case».
- All of the other Castor related cases were suspended pending the outcome of the Widdrington case.
- Plaintiffs in all the other Castor related cases were given status in the Widdrington trial, on the common issues.

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[14] Schedule 1 to the present judgment
[15] Schedule 2 to the present judgment
[16] In 1996, Justice Carrière took over from Justice Halperin who himself had taken over from Justice Gomery
[17] Ruling of Justice Paul Carrière of February 20, 1998

- On the common issues, such as Coopers' negligence and the relevant governing law, the judgment in the Widdrington case was binding on all the other Castor related cases.

[33] A first trial, that started in September 1998 and lasted no less than eight years, was aborted because of the judge's illness and his inability to resume its conduct.

[34] On September 7th, 2007, chief Justice François Rolland ordered a new trial and designated the undersigned to preside it. [18]

[35] The second trial commenced on January 14th, 2008 and ended on October 4th 2010 when the case was taken under advisement.

[36] On all the common issues, the present judgment has a binding effect on all the pending lawsuits brought before the Superior Court by creditors of Castor against Defendants. Those pending lawsuits are identified in Annex A of the trial minutes of March 12, 2008[19].

Court's main conclusions

[37] For the reasons set out in the present judgment, the Court has come to the following main conclusions:

- the audited consolidated financial statements of Castor for 1988 are materially misstated and misleading;
- the audited consolidated financial statements of Castor for 1989 are materially misstated and misleading;
- the audited consolidated financial statements of Castor for 1990 are materially misstated and misleading;
- C&L failed to perform their professional services as auditors for 1988 in accordance with the generally accepted auditing standards ("**GAAS**");
- C&L failed to perform their professional services as auditors for 1989 in accordance with GAAS;
- C&L failed to perform their professional services as auditors for 1990 in accordance with GAAS;

[18] *Widdrington c. Wightman*, 2007 QCCS 6881

[19] A copy of this is attached to the present judgment, as schedule 3, to form part hereof

- C&L issued various other faulty opinions relating to Castor's financial position during 1988 (valuation letters and certificate for Legal for Life Opinion);
- C&L issued various other faulty opinions relating to Castor's financial position during 1989 (valuation letters and certificate for Legal for Life Opinion);
- C&L issued various other faulty opinions relating to Castor's financial position during 1990 (valuation letters and certificate for Legal for Life Opinion) ;
- C&L issued various faulty opinions relating to Castor's financial position during 1991 (valuation letters and certificate for Legal for Life Opinion);
- The governing law is Quebec civil law;
- Widdrington's reliance on Defendants' professional opinion was reasonable;
- As a direct result of C&L's negligence, Widdrington did suffer some damages and shall be indemnified by C&L accordingly;
- The Court would have come to the same conclusions had she had to apply the New Brunswick or the Ontario Common law.

Who's who

[38] The objective of this "who's who" section is not to draw an exhaustive list of all entities involved but to introduce the main players and topics.

[39] The main players and topics are: Castor, Stolzenberg, Wost group of companies ("**Wost group**"), Ingrid O'Connor ("**O'Connor**"), Ronald Smith ("**Ron Smith**"), Manfred Simon ("**Simon**"), Barry MacKay ("**Mackay**"), George Dragonas ("**Dragonas**"), Socrates Goulakos ("**Goulakos**"), Edwin Bänziger ("**Bänziger**"), Ernst Gross ("**Gross**"), Marco Gambazzi ("**Gambazzi**"), the Cooper's audit teams, various partners of Cooper's firms located outside Canada, the York Hannover companies ("**YH Group**"), Karsten Von Wersebe ("**Wersebe**"), David Whiting ("**Whiting**"), Walter Prychidny ("**Prychidny**"), the DT Smith group of companies ("**DT Smith**"), David T. Smith ("**David Smith**"), James Moscowitz ("**Moscowitz**"), Ira Strassberg ("**Strassberg**"), McLean & Kerr and some real estate properties financed by Castor.

Castor

[40] Castor Holdings Inc. was founded in 1975 as a privately owned investment banking and finance organization by Stolzenberg and Wersebe.

[41] Castor Holding Limited ("**CHL**") was incorporated on December 29, 1977 by letters patent in the Province of New Brunswick[20].

[42] CHL purchased the net assets of the previous parent company, Castor Holdings Inc., effective January 1, 1978[21].

[43] The initial balance sheet of CHL, as at January 1, 1978, disclosed total assets of $3,969,726$[22].

[44] Wersebe was the chairman of CHL from 1977, date of its inception, until 1986 and was a director until 1987[23]. Stolzenberg was the president and the chief executive officer, a director, and succeeded Wersebe as chairman in 1986[24].

[45] Castor's subsidiaries included CH International Finance NV ("**CHIF**") located in Curacao (Netherlands Antilles)[25], Castor Finance AG ("**CFAG**") located in Zug (Switzerland)[26], CH International Netherlands BV ("**CHINBV**") located in Rotterdam (the Netherlands)[27], CH International Overseas Ltd. ("**CHIO**") located in Cyprus[28] and CH Ireland Inc. ("**CHII**") located in Dublin (Ireland)[29].

[46] The accounting for the Canadian operations and the corporate consolidation was performed in Montreal at Castor's offices. The accounting records for a number of the subsidiaries were maintained in Zug (Switzerland) and Schaan (Lichtenstein) by companies called Aurea Treuhand and Global Management.

[47] The company's assets grew from $643 million in 1986[30] to $1,871 billion in 1990[31]. Castor nearly tripled in size in those four years. Castor's growth was exceptional.

[48] The growth in Castor's loan portfolio consisted mainly of loan disbursements to fund construction costs, renovation costs, upgrading costs, holding costs and operating expenses and loan increases to enable borrowers to pay interest on their existing loans.

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[20] PW-2400-8 (bates 015926 to 015937)
[21] PW-2400-14 (bates 016045 and 016046)
[22] PW-1053-7, sequential pages 3 to 21
[23] PW-2400-13, PW-2400-74, PW-2400-79, PW-2400-84, PW-2400-85, PW-2400-92 (bates 017617), PW-2400-94, PW-2400-95, PW-2400-98
[24] PW-2400-13, PW-2400-74, PW-2400-79, PW-2400-84, PW-2400-85, PW-2400-86, PW-2400-91, PW-2400-92, PW-2400-98
[25] PW-2400-18, PW-2400-20 and PW-2400-42 (bates 016638 and 016639)
[26] PW-2400-18, PW-2400-20 and PW-2400-42 (bates 016638 and 016639)
[27] PW-2400-29 (bates 016301), PW-2400-34 (bates 016396)
[28] PW-2400-75 (bates 017084), PW-2400-98 (bates 017713 and 017714), PW-2400-101 (bates 017783) and PW-2400-102 (bates 017817)
[29] PW-2400-75 (bates 017084), PW-2400-98 (bates 017713 and 017714), PW-2400-101 (bates 017783) and PW-2400-102 (bates 017817)
[30] Consolidated audited financial statements for the year ending on December 31, 1986 : PW-5, tab 8
[31] Consolidated audited financial statements for the year ending on December 31, 1990 : PW-5, tab 12

[49] Castor's two main clients, the YH Group and the DT Smith Group, relied almost exclusively on Castor's willingness to annually capitalize interest on outstanding loans through the granting of new loans and increasing existing loans. The YH Group portfolio represented Castor's most significant portfolio of loans throughout the period. Castor essentially became the financing arm of the YH North American Group.

[50] On February 26, 1992, an Order was issued granting CHL court protection until June 26, 1992. On July 9, 1992, CHL was adjudicated bankrupt as of March 26, 1992 and Richter and Associates were appointed Trustee in Bankruptcy.

[51] Castor was like a coin – it had two sides: the appearances and the reality.

Appearances

[52] Castor held itself out to its investors and lenders as a spread lender who earned profits based on the difference between its cost of borrowing and the rates at which such funds could unfold by way of loans to its own borrowers.

[53] In corporate brochures, circulated during the period of 1987 to 1991, Castor described itself and its business as follows:

> **Since its inception**, Castor has **focused** on **short and medium term** loans in the North American mortgage market. These investments have been for its own account, as well as on behalf of a growing international clientele.
>
> Castor's preferred investments are **first and second mortgage interim loans** on income producing properties (i.e. office, commercial, hotels, industrial and apartment buildings), well located in major urban areas. Castor's primary investment activities include:
>
> - Purchase and placement of first and second mortgages for terms between six months and two years;
> - Interim financing for construction and development secured by mortgages and take-out commitments.
>
> (...)
>
> During 1987, the **Company placed mortgage loans** of about $250 million in Canada and the United States, which were refinanced in Europe and Canada. Castor **currently administers** directly or in trust for its clients, **mortgage loans in excess of $800 million**. **All proposed investments are reviewed and thoroughly evaluated** by Castor's experienced personnel, prior to commitment. **Underwriting standards are high** and, in addition, particular attention is given to the **Company's policy that loans are not to exceed 75% to 80% of the**

> **estimated market value**. Careful attention is also paid to **asset and liability matching and maturities** in order to provide funding stability"[32] (our emphasis)

[54] The audited consolidated financial statements of Castor disclosed that Castor's business was highly successful and profitable in that Castor could grow dramatically its asset base, revenues and earnings between 1978 and 1990.

Reality

[55] Very few loans made by Castor were short-term loans: at contractual maturity, Castor had no choice but to renew them, year after year.

[56] Castor made and renewed loans to borrowers when it was obvious that such borrowers would not be capable of meeting their financial obligations. Castor acted more as an equity partner than as a lender.

[57] Virtually, none of Castor's borrowers (save in those rare cases where a borrower was a true third party) respected its financial obligations or other loan covenants to Castor.

[58] In 1988, 1989 and 1990, new loans were rarely secured by real estate mortgage, they were mainly equity loans.

[59] In 1988, 1989 and 1990, loans clearly exceeded 75% to 80% of the estimated market value, the Castor's publicized loan to value ratio.

[60] At least 90% of the interest and fee income recorded during each of the three relevant years (1988, 1989 and 1990) in respect of the entire Castor loan portfolio was composed of capitalized interest and fee.

[61] The greater the failure of its borrowers to satisfy their loan obligations, the more revenue Castor could recognize.

[62] Castor had no choice but to raise ever increasing amounts of money from lenders and investors in order to satisfy its outstanding and exponentially increasing financial obligations as well as to support its borrowers' insatiable cash needs.

Stolzenberg, the Wost group and O'Connor

[63] At all relevant times, Stolzenberg was the president and chief executive officer of Castor.

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[32] PW-1057-1, at page 4 (to the same effect generally, except for the figures that are updated, see also PW-1057-2 (1988) and PW-1057-3 (1989)

[64] At all relevant times, Stolzenberg was also president and shareholder of Wost Holding Ltd[33].

[65] Stolzenberg was involved in a multitude of other corporations.

[66] O'Connor started as a bookkeeper for the Wost Group in 1977, when she moved to Montreal with her husband. She worked for the Wost group of companies[34] three days a week, and she was its sole employee until 1993. She speaks German, English and some French.

[67] Before she joined the Wost group, O'Connor had worked for approximately 9 and ½ years as a secretary to the president of Thorne Riddell in Toronto and had done some accounting work there, but without formal training in accounting.

[68] The companies she was handling included Wost Holdings Ltd.[35], Wost Development Corporation, 97872 Canada Inc. ("**97872**")[36], 612044 Ontario Ltd. ("**612044**")[37], 606752 Ontario Ltd. ("**606752**")[38], 166505 Canada Inc. ("**166505**")[39] and 687292 Ontario Ltd. ("**687292**")[40] .

[69] Her functions consisted namely in:

- Setting up the filing system and the accounting books and records, including their cash receipts, cash disbursements and general ledgers;
- Handling correspondence, invoices, payments and bank transfers and bank reconciliation;
- Preparing analysis and trial balances at year-end for the audits;
- Acting as an officer for corporations of the Wost group and, in that capacity, signing reports, resolutions and agreements[41].

[70] O'Connor performed tasks for Castor while an employee of the Wost group: she handled compilation of statistical information on a spreadsheet, and updated same on a

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[33] Compendium PW-340
[34] PW-292
[35] PW-317, PW-318 A, PW-318 B, PW-318 C, Pw-319, PW-320, PW-321, PW-322 and Compendium PW-340
[36] PW-292, PW-323, PW-324, PW-325, PW-338 and PW-339
[37] PW-292, PW-326, PW-327, PW-328, PW-338 and PW-339
[38] PW-292, PW-329, PW-330, PW-331, PW-338 and PW-339
[39] PW-292, PW-332, PW-333, PW-334, PW-338 and PW-339
[40] PW-292, PW-335, PW-336, PW-337, PW-338 and PW-339
[41] O'Connor, January 14, 2009, pages 35-36 (for more details see also cross examination, O'Connor, January 15, 2009, pages 55 to 71)

monthly basis, in the Roxy Petroleum file, an investment Castor had made in oil production in Western Canada.[42]

Ron Smith, Simon and MacKay

Ron Smith

[71] Ron Smith was employed by CHL from March 1980 to June 1992.

[72] In 1968, Ron Smith obtained a Bachelor of Science degree from Bishop's University, a Bachelor's degree in Business Administration in 1970 from same, and a Master's degree in Business Administration from Queens University in 1972[43].

[73] He started his employment history with Nesbitt Thompson Company and, after he graduated from Queens, he worked in their corporate finance department until 1974[44].

[74] In 1974, Ron Smith joined the Mercantile Bank of Canada[45] working in one of its branches as a person in charge of analyzing credit applications and proposals, getting them approved by the bank, negotiating documents with lawyers, closing and monitoring thereafter the transactions with the bank's credit department.

[75] In 1976, he was transferred to the credit supervision of the head office, as assistant vice-president. In charge of a large real estate portfolio and managing a team of people, and like other account officers in the bank, he had a dream: to join a real estate company[46].

[76] In 1978, he left the Mercantile Bank for Mondev International, a real estate development company based in Montreal that he joined as a financial and development officer.

[77] In 1979, he met with Wersebe, who was looking for a vice-president finance for YHDL. Stolzenberg was present at that meeting. Ron Smith did not get the position with YHDL. However, in March 1980, he was hired by CHL as manager of mortgage investments[47].

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[42] O'Connor, January 14, 2009, page 36 (for more details on circumstances, see also cross examination, O'Connor, January 15, 2009, pages 55 to 60)
[43] Smith, May 14, 2008 at pages 8 and 9
[44] Smith, May 14, 2008 at page 9
[45] Smith, May 14, 2008 at page 9
[46] Smith, May 14, 2008 at page 13
[47] Smith, May 14, 2008 at pages 14 to 16

[78] He was attributed various titles while working for Castor and over the years was promoted from manager to senior vice president.

Simon

[79] From July 1981 to April 1992, Simon worked at Castor.

[80] Simon obtained a Bachelor of Commerce from the University of Toronto in 1968 and an MBA from York University in Toronto in 1972[48].

[81] In 1968, he joined the Toronto-Dominion Bank in Toronto. Until 1974, he spent most of his time in the branch system as a loan officer or manager of a team of loan officers. At the end of 1974, and until 1980, Simon joined the international division of the bank and worked for that division, mainly in Frankfurt[49]. Simon speaks German.

[82] In 1980 and 1981, he worked for the TD Bank in Calgary in their national accounts' division servicing companies in the oil and housing industries in Western Canada.

[83] In 1981, Simon saw an ad. Head hunters out of Toronto were looking for someone who had an international banking background to join a growing company in the financial sector[50]. He answered this ad, met with Wersebe and Stolzenberg in YH offices in Toronto and ended up being hired by CHL, as a vice-president[51].

MacKay

[84] Mackay is a Certified General Accountant. He obtained his degree in 1976, from McGill University, through the evening program. [52]

[85] From 1973 to 1976, he worked for Trizec as manager, handling revenue producing properties such as Place Ville Marie, BCN building, 360 St-Jacques.

[86] From Trizec, he worked at Hercules Canada as a financial analyst for a year and thereafter at the Mercantile Bank, as a senior administration officer in charge of four departments: mortgage, payroll, reports and accounting[53].

[87] From 1980 to 1992, he worked for Castor as manager of administration, in charge of accounting and foreign exchange operations[54].

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[48] Simon, April 23, 2009, at page 81
[49] Simon, April 23, 2009, at pages 83 to 85
[50] Simon, April 23, 2009, at page 88
[51] Simon, April 23, 2009, at page 89
[52] MacKay, August 24, 2009, at page 64
[53] MacKay, August 24, 2009, at pages 64-65

[88] From 1988 to 1990, his official title at Castor was "*manager of administration, manager of special projects*"[55].

[89] Ruth Tooke, Cynthia Rancourt and Christa Karl reported to MacKay[56].

- Ruth Tooke ("**Tooke**") was responsible for general accounting[57]. She was hired in 1979 by Stolzenberg to work for Castor and her employment was terminated on March 13, 1992[58]. While reporting to Mackay, she also interacted with Ron Smith of the mortgage department. [59]

- From 1986 onwards, Cynthia Rancourt ("**Rancourt**") assisted Tooke in the general accounting[60]: she was responsible for posting cash receipts, cash disbursements and several other entries and had other responsibilities[61]. While reporting to Tooke and MacKay, Rancourt also interacted with Ron Smith.

- Christa Karl ("**Karl**") took care of the funding side of Castor's operations, i.e. the shareholders and the loans to Castor and the investments in Castor. While reporting to MacKay, Karl also interacted with Simon[62].

Dragonas and Goulakos

[90] Dragonas and Goulakos are chartered accountants, both former C&L employees, who exercised their profession together as partners.

[91] Dragonas and Goulakos performed accounting and consulting services for Castor: their services included administration services in respect of the Montreal Eaton Centre, "accounting assistance" on a monthly basis and "supplementary services"[63].

[92] Dragonas and Goulakos were also contacts for Coopers for the purpose of their audit of the consolidated financial statements of Castor.

[93] While they were performing accounting services for Castor, they also provided similar services for Stolzenberg and companies of the Wost group.

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[54] MacKay, August 24, 2009, at page 65
[55] MacKay, August 26, 2009, at pages 31-32
[56] MacKay, August 24, 2009, at page 66
[57] MacKay, August 24, 2009, at page 66; Tooke, February 28, 2008, at page 26
[58] Tooke, February 27, 2008 at page 53
[59] MacKay, August 24, 2008, at page 67
[60] Rancourt, February 29, 2008, at pages 150 and 151
[61] Tooke, February 27, 2008, at page 60; Rancourt, February 29, 2008, at pages 169 to 171; Rancourt, March 3, 2008 at pages 22 to 25
[62] MacKay, August 24, 2009, at page 67
[63] D-20 and D-21

Bänziger and Gross

[94] Bänziger provided accounting and administrative services for Castor and its subsidiaries through and on behalf of his company Global Management Limited ("**Global**"). He was particularly instrumental in the banking and wire transfers between Castor, its subsidiaries and their respective creditors and debtors.

[95] Bänziger was a Director of one of Castor's subsidiaries, C.H. (Ireland) Inc.

[96] Bänziger was a principal contact for Coopers, along with Stolzenberg, with respect to the audits of the financial statements of the subsidiaries of Castor. He also assisted in the preparation of the unaudited consolidated financial statements of Castor, including the June 30 statements.

[97] His son, Jurg Bänziger ("**Jurg Bänziger**"), worked with him and also provided accounting and administrative services for Castor.

[98] Gross worked in Zug (Switzerland) from 1985 to 1987. He worked exclusively for and was responsible for the foreign exchange and money market sections of Castor's overseas subsidiaries[64].

[99] At the end of 1987, Gross went to work in Schaan (Liechtenstein) because the work he had been doing previously in Zug was transferred to Global in Schaan[65].

[100] In March or April, 1990, Gross also took over responsibility for the loan files of Castor's overseas subsidiaries. From that point forward, he was in charge of the administration of the loan files, including documentation relating to the renewal or prolongation of loans, making pay outs, and applying incoming funds to the right loans.[66]

[101] Throughout his engagement for Global, Gross worked exclusively for Castor's overseas subsidiaries[67].

Gambazzi

[102] Gambazzi is a lawyer in Lugano (Switzerland) acting for several investors in Castor, individuals and corporations, who wanted to remain anonymous.

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[64] Gross, September 28, 1998, pages 14 to 17
[65] Gross, September 28, 1998, pages 18 to 20
[66] Gross, September 29, 1998, pages 270-271 and 347-348
[67] Gross, September 28, 1998, pages 38-39

[103] Gambazzi was a shareholder of Castor through companies he owned or controlled, and a Director and a Managing Director, with signing authority, of the offshore subsidiaries of Castor.

Coopers - Castor's audit teams and Coopers Partners in other jurisdictions

Castor's audit teams

[104] Coopers has acted as auditor for CHL since its inception and Wightman has always been the engagement partner in charge of the audit and of the Castor file in general.

[105] Members of Castor's audit teams, in Montreal and overseas, have come and gone over the years.

[106] Between 1986 and 1990, while Castor nearly tripled in size, the size of the teams remained about the same, as well as the time spent on audit work in the field, and the rollover of personnel was noticeable.

[107] John Grezlak was involved with the Montreal audits from 1982 to 1987, as audit manager, but he left Coopers in October 1988[68].

[108] Bruce Wilson was involved with Castor's overseas audit, as audit manager, from 1985 to 1987 inclusively, but he left Coopers in August of 1988[69].

[109] Even if he remained the partner responsible for the overseas audit until the end, Jean Guy Martin, who had personally been involved with the supervising on the site of the overseas audit work since 1982, ceased going to Europe after the 1988 audit.[70]

The 1988 audit teams

[110] In 1988, the Montreal audit team included Kenneth Mitchell (audit manager[71]), Martine Picard[72] (supervisor), Daniel Séguin[73] for a certain period of time (senior), Linda Belliveau (senior)[74], John Talbot (staff assistant) and Charles Soroka (staff assistant)[75].

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[68] Grezlak, January 4, 1996, pages 8 to 10
[69] Wilson, October 28, 1996, pages 6 to 9
[70] Martin, December 18, 1995, pages 7 to10: Martin, January 5, 2010, pages 71, 72, 76, 81 to 94
[71] Mitchell, April 22, 1996, pages 2 to 5
[72] Seguin, December 11, 1995, page 14; Picard, December 6, 1995, pages 7, 8, 18, 23, 79 and 93
[73] Seguin, December 11, 1995, pages 8 to 15
[74] Picard, December 6, 1995, pages 7, 8, 18, 23, 79 and 93
[75] Picard, December 6, 1995, pages 7, 8, 18, 23, 79 and 93

[111] In 1988, the overseas audit team included Jean-Guy Martin (partner), Mari Elizabeth Ford (audit manager) and Janet Cameron (audit manager).

The 1989 audit teams

[112] In 1989, the Montreal audit team included Kenneth Mitchell (audit manager), Penny Heselton (supervisor), Linda Belliveau (senior[76]), Stephane Joron (staff), Pierre Lajeunesse (junior, staff assistant) and Mitsy Jordan (junior, staff assistant).

[113] In 1989, the overseas audit team included Mari Elizabeth Ford (audit manager) and Tarek Kassouf (audit supervisor)[77].

The 1990 audit teams

[114] In 1990, the Montreal audit team included François Quintal (audit manager), David Hunt (supervisor), Robert Wagstaff for one week [78] (senior) and Martin Quesnel for one week[79] (senior), David Pascal (staff assistant[80]) and Michael Pollock (staff assistant[81]).[82]

[115] In 1990, the overseas audit team included Mari Elizabeth Ford (audit manager) and Tarek Kassouf (audit supervisor)[83].

Coopers' partners in other jurisdictions

William P. Cunningham

[116] William P. Cunningham ("**Cunningham**") was a partner in Coopers & Lybrand Ireland from 1987 to 1991[84]. He had joined Coopers & Lybrand Ireland in 1973 and qualified as a chartered accountant in 1976. Between 1976 and 1979, he worked in Coopers & Lybrand, Ireland; between 1979 and 1981 in Coopers & Lybrand, Germany; and from 1981 onwards, was back with Coopers &Lybrand Ireland[85].

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[76] Belliveau, April 1, 1996, page 21
[77] Kassouf, November 17, 1995, pages 7 and 14
[78] Hunt, March 28, 1996, page 24
[79] Hunt, March 28, 1996, pages 34 and 35
[80] Hunt, March 28, 1996, page 171
[81] Hunt, March 28, 1996, page 167
[82] Quintal, December 1, 1995, page 73
[83] Kassouf, November 17, 1995, page 14
[84] Cunningham, November 24, 1998, page 11
[85] Cunningham, November 26, 1998, pages 29-30

[117] He did the audit of CHI in 1989 and 1990 but the audit for 1991 was never completed[86].

[118] His role was to carry out the local statutory audit, which is what Coopers & Lybrand Ireland was appointed to do. Since C&L wanted to include the figures that related to CHI in the consolidated figures, C&L needed a certain amount of work done by Coopers & Lybrand Ireland on those figures. In that capacity, and during various periods of time, he interacted with C&L, namely with Mitchell[87].

Clifford Johnson

[119] Clifford Johnson ("**Johnson**") was a partner in Partner of Coopers & Lybrand Bahamas[88].

[120] As were two other partners in Coopers & Lybrand Bahamas, he was invited to act for companies incorporated at the behest of Wightman: Chur Investments Limited ("**Chur**"), Petra Investments Limited ("**Petra**") and Sloppin Investments Limited ("**Sloppin**"). He discharged the duties of a director, something with which he was familiar, and that he understood.

[121] Chur was a trust formed under the laws of the Cayman Islands that was dissolved in December 1985[89]. The shareholders that remained involved with Chur until it was dissolved invested in Petra.

[122] Petra was created under the laws of the Turks & Caicos Islands in 1983[90]. Its three directors were partners of Coopers & Lybrand Bahamas. Shareholders included Stolzenberg, Simon, Ron Smith, MacKay, CHIF and Wightman's wife, Ruth Wightman[91]. Petra raised funds, which were invested through Sloppin, its wholly-owned subsidiary and operating entity.

[123] Johnson's understanding of the Chur, Petra and Sloppin organization was to permit friends and business associates of Wightman to invest and obtain a better than average return and to convert investment income into capital income [92].

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[86] Cunningham, November 24, 1998, page 32
[87] Cunningham, November 24, 1998, pages 42 and 44
[88] Johnson, October 27, 1998, page 12
[89] Johnson, October 27, 1998, page 31
[90] Johnson, October 27, 1998, page 38 and PW-345 and PW-346
[91] Johnson, October 27, 1998, pages 39 to 52
[92] Johnson, October 27, 1998, page 63

Antonio Hajiroussos and Michael Zampelas

[124] During the period between 1987 and 1991, and until July 1998, Antonio Hajiroussos ("**Hajiroussos**") was a partner of Coopers & Lybrand, Cyprus. He was in charge of the department relating to the administration of the offshore companies which did not have their own offices in Cyprus[93]. Since Castor's Cyprus subsidiaries had their own offices in Cyprus, he was not involved with them as much as he was with other entities. However, he had banking signing authority and was receiving instructions from Bänziger and Stolzenberg. He met Stolzenberg a few times in Cyprus and once in Canada.

[125] Between 1987 and 1991, Michael Zampelas ("**Zampelas**") was also a partner of Coopers & Lybrand, Cyprus. In fact, he was the president and the managing partner of the firm.

[126] From their respective inception and until they ceased to operate, Coopers & Lybrand, Cyprus were the auditors for CH Cyprus, CHIO and Enar Middle East Limited, three subsidiaries of Castor[94] under the responsibility of Dinos Papadopoulos[95].

YH Group, Wersebe, Whiting and Prychidny

YH group

[127] The main corporations of the YH group to whom Castor loaned money are:

- York-Hannover Holdings Ltd. ("**YHHL**") and its successor KvWIL, after a reorganisation and a winding-up of YHHL in 1987;
- York-Hannover Leisure Properties Ltd. ("**YHLP**"), and its predecessor York-Hannover Amusement Ltd. ("**YHAL**");
- York- Hannover Developments Holdings Ltd. ("**YHDHL**");
- York-Hannover Hotels Holdings Ltd. ("**YHHHL**");
- Skyline Hotels (1980) Ltd. ("**Skyline 80**"), a wholly-owned subsidiary of YHHHL;
- York -Hannover Hotels Ltd. ("**YH Hotels**");

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[93] Hajiroussos, March 18, 1999, pages 75 and 76
[94] Zampelas, March 15, 1999, pages 2 and following
[95] Zampelas, March 17, 1999, pages 62-63

- York- Hannover Developments Ltd. ("**YHDL**").

Wersebe

[128] Wersebe was the president of Castor since its inception and until 1986, when Stolzenberg took over the position. Wersebe was also a shareholder (he owned 40% of the shares) until 1987, year in which Stolzenberg bought his 40% participation.

[129] At all times, Wersebe was also the directing mind of the York-Hannover group of corporations.

Whiting

[130] After graduating from the university in 1968 and writing the final exams in 1971, Whiting became a chartered accountant. He received the silver medal for second place standing in Ontario, and he stood in the top twenty (20) in Canada that year[96].

[131] He joined Clarkson Gordon (now Ernst &Young) in 1968 and left in 1985. During the years at Clarkson Gordon, in their Ontario or New Brunswick offices, Whiting occupied various positions in different departments and had numerous responsibilities, within the firm, the Chartered Accountant Institute or other professional associations.

[132] In 1985, he joined the YH group as Vice-President, position he occupied until the group dissolved.[97]

[133] Whiting assumed responsibility directly for YHDL's accounting and financial reporting and for corporations beneath the YHDL umbrella. His functions included direct income tax work and part of the functions of a Chief Financial Officer which include maintaining a relationship with some of the lenders such as Bank of Montreal ("**BMO**"), National Bank, Castor, occasionally the First Interstate Bank of Canada ("**FICAN**"), and with some of the partners such as Castor, the Confederation Life Insurance Company, and the group of companies called Camrost[98].

[134] He was Assistant-Secretary to all YH companies in North America, and Secretary of YHDL. He was a signing officer of all companies and had access to their corporate records and minute books. He dealt with lawyers who were acting on their behalf. He was involved in negotiating and executing documents[99].

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[96] Whiting, November 10, 1999, page 11 and PW-1135
[97] Whiting, November 10, 1999, page 13 and PW-1135
[98] Whiting, November 10, 1999, pages 13 to 20
[99] Whiting, November 10, 1999, pages 19 to 24

Prychidny

[135] Prychidny was a graduate of Toronto University in 1974 and obtained a Bachelor's degree in Commerce. He received his designation as a chartered accountant in 1976 and as a chartered business valuator ("**CBV**") in 1980. That very same year, he wrote CBV exams and received the highest marks in Canada.

[136] Between 1974 and 1983, Prychidny worked for two firms of chartered accountants, the first being Price Waterhouse and Crawford, and the second Smith and Swallow, at the beginning in audits but mainly in the business valuation field. He also worked for Walker Industries, a corporation where he acted as Chief financial officer ("**CFO**").

[137] In October 1983, when he started in the hotel business, and until June 1990, Prychidny was associated to the YH group:

- In 1983, Prychidny joined the YH group as CFO of YHAL in Niagara Falls, where he and his wife had grown up and where they were looking forward to moving back.
- In 1985, at the request of Wersebe, he left YHAL and joined YHHL as Executive Vice President. His mandate was to upgrade the Skyline chain of hotels and to look after the management of those hotels and of the Maple Leaf Village hotels[100].

DT Smith, David Smith, Moscowitz and Strassberg

DT Smith

[138] DT Smith was comprised of eight corporate entities and seven partnership entities. The general partner of the partnerships was a corporation whose stockholders were also the stockholders of each of the corporations. The entities were developers of single family homes and condominiums in California.

David Smith

[139] After many years in various business fields, including insurance and commercial real estate, David Smith started a new business as a builder and developer of residential homes in Southern California.

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[100] Prychidny, October 14, 2009 pages, 37 to 40 and October 16, 2009, pages 20, 30 to 38

[140] Prior to getting involved into this home building business, and acting as a broker David Smith had completed several transactions with Stolzenberg. To get financing, he went to Stolzenberg[101].

[141] His first project in California was known as Wood Ranch 1. It was located in the Simi Valley[102] and included approximately 120 single family homes. Other projects followed.

Moscowitz

[142] Moscowitz is a lawyer and an accountant who has a Master's degree in tax law.

[143] For approximately a year and a half, form 1973 to mid-1975, he practiced as a lawyer.

[144] He gained accounting experience between 1975 and 1985, and before he met David Smith, with the accounting firms Oppenheim, Pell Dixon & Company and Ernst & Young or Ernst & Whinney, in New York.

[145] His business relationship with David Smith started as a partnership in a company called David T. Smith Associates which was primarily a commercial real estate developer in Florida, carrying on its business in New York and New Jersey.

[146] In the mid 80s, Moscowitz moved to California and began working for the DT Smith group handling day-to-day operations related to construction projects in California as well as coordinating meetings with attorneys, accountants, and lenders and maintaining books and records of the corporations[103].

[147] Moscowitz was executive Vice President and member of the board of each of the DT Smith corporations, but he never was a shareholder or a partner in those projects.

Strassberg

[148] Strassberg is a Certified Public Accountant ("**CPA**") licensed in the State of New-York since 1980 and, since 1987, a stockholder in the firm Rogoff & Company ("**Rogoff**"), an accounting firm established since 1946[104].

[149] When he started at Rogoff, in 1980, he was involved on a part time basis in various real estate projects that Rogoff was auditing, like conversion of condominium properties and tax shelter projects. Then, Strassberg had also his solo practice as a

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[101] David Smith, March 13, 2000, pages 15 to 17 and Ron Smith, June 10, 2008, pages 8 and 9
[102] David Smith, March 13, 2000, page 9
[103] Moscowitz, December 13, 1999, pages 18 to 25
[104] Strassberg, November 1, 2000 at page 104

CPA. The business of Rogoff evolved. In 1984, Strassberg became a full time employee and remained with this firm ever since.

[150] Strassberg met David Smith and Moscowitz in 1982 or 1983, while David Smith and Moscowitz were associated with a company called Berg Harmon Enterprises doing investments and establishing partnerships for the purposes of generating tax shelter and investing in shopping centers. Their professional relationship began: Strassberg rendered audit services to various entities.

[151] In 1986 or 1987, further to an internal revenue reform, the tax benefits from the tax shelters were eliminated for subsequent years. David Smith and Moscowitz moved to California where they started the DT Smith group, a home building company. Rogoff became the auditor of the group and Strassberg became the engagement partner.

MC Lean & Kerr

[152] McLean & Kerr is a Toronto law firm which performed numerous services for Castor in the 80s and the early 90s.

[153] At the beginning, Harry Kerr was the partner in charge of Castor's account but Leonard Alksnis ("**Alksnis**") took over during the 80s, before the 1987 to 1990 period[105].

[154] At the end of 1990 and thereafter, at the request of Alksnis, other lawyers of the firm were involved in the incorporation of various corporations and preparation of documents relating thereto: Harold James Blake ("**Blake**"), Christine Renaud ("**Renaud**") and Soo Kim Lee ("**Lee**").

Some Real estate properties financed by Castor

Montreal Eaton Center

[155] The Montreal Eaton Center ("**MEC**") represented one of the most significant development projects funded by Castor: the redevelopment of an existing retail complex in downtown Montréal, located on Ste.Catherine Street and known as "Les Terrasses".

[105] Alksnis, February 6, 2006, pages 11-12

[156] MEC project consisted of four levels of retail space and a fifth level devoted to cinemas and a restaurant with an expansion onto adjacent land and a connection by underground tunnel to other retail shopping complexes - Place Montréal Trust to the West, and Place Ville-Marie to the South[106] - and to another Castor-financed property known as the Palace Theatre[107].

[157] MEC project was commenced in February 1988, date of the first construction loan advance.

[158] Originally, "Les Terrasses" was owned by a predecessor company of YHDL.

[159] In the early 80s, an undivided interest in one half of the property was sold to 97872 Canada Inc. ("**97872**").

[160] Thereafter, it was owned in undivided co-ownership by York-Hannover Developments Ltd. ("**YHDL**"), except for a short period of 8 days during which it was sold by YHDL to a related entity, and 97872.

[161] 97872 operated from Castor's Montreal premises and the office of Dragonas[108].

[162] Much of the funding for the MEC project came from CHL which ranked in a subordinated position to a first mortgage position for a maximum amount of $125,000,000 from third party lenders.

[163] CHL financed the project with 2nd mortgage security, more than one 3rd mortgage, also with equity loans made to the co-owners and, in the case of 97872, to its parent company, 612044 Ontario Limited ("**612044**").

[164] 612044 owned 100% of 97872.[109] The main asset of 612044 was its investment in common shares of 97872[110]. 612044's investment in 97872 was financed by Castor, with the loan equal to the amount of the investment[111].

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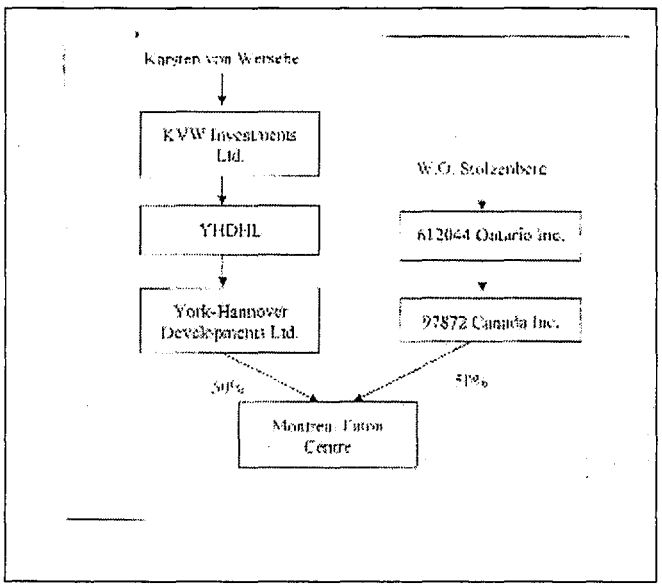
[106] PW-1108, pages 30 to 33.
[107] D-586 : Appraisal dated April 15, 1988 prepared by P.E. Bedard & Associes, p. 6
[108] For example: PW-1102-A-5, page 79 of a Loan Agreement with Bank of Montreal, used an address of Suite 335, 1320 Graham Boulevard for 97872 (PW-565-7C-1 uses this address for Dragonas Goulakos) with a copy to Castor. D-94 is a letter on 97872's letterhead that uses Castor's mailing address
[109] D-94
[110] PW-566-1
[111] PW-1103-1

[165] The ownership and corporate structure of MEC was as follows in the 1988 to 1991 period[112].



[166] Ultimately, there were ten Castor loans related to the MEC project[113], with a further minor loan made to the MEC Tenants' Association[114].

Maple leaf Village

[167] Maple Leaf Village Investments Inc. ("**MLVII**") owned the Maple Leaf Village ("**MLV**") a complex located in Niagara Falls which consisted of two major hotels (Fox Head Hotel and Brock Hotel), a motel (Village Inn Motel), a shopping complex, an amusement park, museums and parking facilities[115].

[168] Commencing in or around 1979, a number of loans were made by CHL, and later by CHIF, to finance MLV, directly and indirectly.

[169] Until 1982, MLVII was 100% owned by Wost Development Corp. and York-Hannover Ltd, two corporations controlled by Stolzenberg and Wersebe who were respectively President and Chairman of Castor[116].

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[112] PW-2941, volume 3, par. 3.18; see also PW-1100 A to C.
[113] CHL loans 1100, 1109, 1163, 1101 and 1103, 1145, 1042 1095 and 1146 and a CHIF loan
[114] Loan 1158
[115] PW-494
[116] Notwithstanding this relationship, no disclosure was made on the consolidated financial statements of Castor that the investments related to MLVII were related party transactions.

[170] In 1982, to finance the properties, a redevelopment plan and the restructuring of existing indebtedness, MLVII offered investment units consisting of subordinated mortgage loans, preferred shares and common shares[117]. The target amount for the new financing was $80.0 million.

[171] Common shares of MLVII were sold to offshore entities[118], together with preferred shares and mortgage debentures, for approximately $60,000,000.

- This $60 million paid by companies in Panama, Curaçao and other secrecy jurisdictions was totally financed by loans provided by CHL and by CHIF.
- Certain loan documents were signed on behalf of the borrowers by individuals closely related to Castor, namely Bänziger and Gambazzi[119].
- These offshore companies never paid any principal or interest on these loans from their inception in 1982 until the failure of Castor in 1992.

[172] By 1984, $63.2 million in mortgage loans, preferred shares and common shares had been subscribed for[120].The $63.2 million of subscriptions remained unchanged thereafter.

[173] From 1988 to 1990, the total Castor loans associated with MLV increased from $96 million to $130 million[121], and they ranked after first and second mortgages totalling between $30 and $40 million.

Toronto Skyline

[174] Located close to Lester B. Pearson Airport in Toronto, this commercial complex was comprised of a hotel of 715 units, a large number of convention and conference rooms, restaurants, recreational facilities, a retail mall, offices, extensive parking, and surplus land.[122]

[175] Until 1981, the hotel was owned by York-Hannover Hotels Ltd. ("**YHHL**") when it was sold to Topven Holdings Ltd. ("**Topven**")[123].

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[117] PW-477

[118] Trade Retriever Corporation, Charbocean Trading, Runaldri S.A., Harling Finance Corporation, Harling International N.V. and Gebau Overseas

[119] D-576, D-577, D-578, D-579, D-580: PW-2177

[120] PW-478: MLVII financial statements as at September 30,1984 and 1985, note 5

[121] CHL Loans 1011, 1012, 1013, 1014, 1015,1016, 1017, 1018, 1019, 1048, 1105, 1125, 1126 and 1136 and CHIF loans 261000004, 385000004, 385000008, 3850053010, 3850090003, 3850093005, 4410033003, 4410040008, 4410043010, 7700010009, 8900000010

[122] PW-423

[123] PW-1083. Mullins Realty Limited appraisal dated May 1984, page 7.

[176] In 1984, Lambert Securities Inc. ("**Lambert**"), a Panamanian company, acquired Topven.

[177] CHIF granted two loans to Lambert: a first loan of $27.5 million was advanced on September 30, 1984[124] and a second loan of $6 million was advanced on October 15, 1985[125]. The security given by Lambert to CHIF was a pledge of its own shares, the shares of its subsidiary, 594369 Ontario Inc. ("**594369**") and the shares of Topven, 594639's subsidiary[126]. The security also included a pledge of Lambert's note receivable from Skyeboat Investments Ltd. ("**Skyeboat**"), a part owner of the Calgary Skyline Hotel.

[178] Castor had serious issues with York-Hannover Hotel's management of the hotel, and with its loans to borrowers connected to the Toronto Skyline[127].

[179] At the beginning of January 1986, Castor sought limits to bank transfers to YHHL, seeking that all cash transfers to YHHL be pre-approved by Castor.

[180] The audit report for Topven's 1986 financial statements, dated May 15, 1987[128], was qualified due to differences of opinion as to the collectability of a receivable from the hotel manager (YHHL), and the definition of related parties[129]. These 1986 financial statements also contained a going concern note that highlighted three years of significant losses, outstanding 1985 and 1986 business and property taxes, and the request by Topven's bank that the company seeks alternate banking arrangements[130].

[181] In 1987, Castor's loans to borrowers connected to the Toronto Skyline continued to accrue interest that was capitalized because of the Hotel's inability to generate sufficient cash flow to meet its debt servicing costs.

[182] In 1988 the property was flipped from Topven to a subsidiary, Topven Holdings (1988) Inc. ("**Topven 88**"). At the time of restructuring, Topven's financial statements disclosed an accumulated deficit of $29.97 million[131]. Property taxes of $3 million, including penalties[132], were in arrears for 1986 and 1987 and $1.3 million of 1988 property taxes remained outstanding. The refinancing included arrangements with the City of Etobicoke to pay all 1986 and 1987 tax arrears by December 31, 1988.

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[124] loan 576000/3002
[125] loan 576000/3009
[126] PW-1460-4 : Balance sheet of 594639 Ontario Limited dated August 31, 1988
[127] PW-1080-2.
[128] PW-187
[129] the auditors believed that there were additional undisclosed related parties : PW-187
[130] PW-187
[131] Exhibit PW-431 : Topven financial statements for the year ended December 31, 1987 disclosed a deficit of $29.97 million prior to the restructuring
[132] PW-211-26.

[183] During 1988, 1989 and 1990, there were two loans by CHL and three loans by CHIF which were ultimately secured by the Toronto Skyline.

- The two loans by CHL were a first mortgage to Topven 88 of approximately $40 million and an operating line to Topven or Topven 88, which increased from $7.6 million as at December 31, 1988 to $26.4 million as at December 31, 1990[133].

- The loans by CHIF consisted of a $20 million second mortgage loan to Topven 88 and the two loans to Lambert made in 1984 which had increased to $35.7 million and $7.7 million respectively by December 31, 1988[134].

Toronto World Trade Center

[184] The Toronto World Trade Centre project ("**TWTC**") consisted of two distinct elements: firstly, the office and commercial complex consisting of three office towers and secondly, the residential and condominium complex consisting of two residential condominium towers.

[185] The eight-acre site was located near the financial core of Toronto, adjacent to the Westin Harbour Castle, and served as a link between the Toronto Harbour area and the downtown financial area.

[186] The condominium project was completed in 1991 but the construction of the three office towers never took place.

[187] The ownership structure was complex.

[188] The project was treated as a joint venture that was owned in the following proportions:

Camrost Office Developments (Lakeshore) Limited ("**Camrost**")	50.000%
752608 Ontario Limited ("**752608**")	12.500%
Toronto World Trade Centre Limited Partnership ("**TWTCLP**")	18.375%
Toronto World Trade Centre Inc. ("**TWTCI**")	19.125%

[189] TWTCI was owned 49% by Toronto Waterfront Development Corp. ("**TWDC**") and 51% by York-Hannover Developments Ltd. ("**YHDL**"). In addition to its own interest in the project, TWTCI also had a 56.8% interest in TWTCLP and, through that interest,

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[133] CHL loan 1107, GL/AC 066 (operating line) and loan 1148
[134] CHIF loan 888,002/20.03, loan 576000/3002 and loan 576001/3009

acquired an additional 10.437% (56.8% of 18.375%) of the project. By virtue of its own 19.125% direct ownership in the project and its 10.437% indirect ownership, TWTCI had a total interest in the project representing 29.562% of the overall project.

[190] CHL made four different loans related to this project[135].

- Separate loans to the two owners of TWTCI, Toronto Waterfront Development Corp. and YHDL, that were primarily secured by a pledge of common shares of the TWTCI;

- A loan directly to the TWTCI, which was primarily secured by a pledge of the TWTC's 19.125% beneficial interest in the project as well as a pledge of its 56.8% ownership of the TWTCLP;

- A loan made to YHDL, which was secured by an assignment of options to acquire 50% of the 12.5% interest in the project held by 752608 Ontario Inc. as well as 76% of the outstanding units of the Skyline Triumph Limited Partnership.

[191] CHL's loans associated with the TWTC increased from $17,589,922, at January 1, 1986, to $84,910,000 at December 31, 1990.

[192] However, during that period, none of the increases in the loans were used to actually finance the project.

[193] The increases in the loans were due to year end reallocations of interest on York-Hannover loans that had been capitalized in account 046 or that was reallocated by circular cash management of funds.

[194] CHL did not have a direct charge against the project but merely an assignment of the shares of TWTCI (its interest in the overall project being 29.562%) and ownership of units in TWTCLP (equivalent to 7,938% of the overall project).

[195] Castor ownership of units in TWTCLP resulted from:

- Five units of the 213 units (2.35%) of TWTCPL, acquired by CHL in 1988. These units represented a 0.432% (2.35% of 18.375%) interest in the project;

- In 1989, CHL acquired a further 7.506% (40.85% of 18.375%) interest in the TWTC project: 607670 Ontario Inc., a wholly-owned subsidiary of CHL, acquired all the shares of 696604 Ontario Ltd. who itself owned 87 of the 213 (40.85%) units of the TWTCPL.

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[135] Loans 1046, 1067, 1120 or 1149 and 1090

Calgary Skyline Hotel

[196] The Calgary Skyline Hotel ("**CSH**" or "**Calgary Skyline**") is a 23 storey hotel of 387 rooms located in downtown Calgary, Alberta[136]. It is directly connected to the Calgary Convention Centre and to the Glenbow Museum, the Calgary Centre for the Performing Arts and the Canadian Pacific's Palliser Square office tower[137].

[197] CHL became involved in 1982 when it purchased a $15.7 million mortgage[138] from YHDL and Robert Lee Ltd., a shareholder of Castor[139] :

- this mortgage was to Skyeboat Investments Limited ("**Skyeboat**"), the 100% owner of the Skyline Calgary; and
- the owner of Skyeboat was Kevin Hsu, who also owned Topven Holdings Ltd.

[198] In 1983-84, the Skyline Calgary mortgage loan became part of the refinancing of the Toronto Skyline Hotel[140].

[199] The hotel was managed through a management agreement by the Four Seasons Hotel Group.

[200] In June 1985, 321351 Alberta Ltd. ("**321351**") purchased from Four Seasons Hotel Ltd. its interest in the hotel lease and the hotel's furniture, fixtures and equipment. CHL provided $6 million in financing to 321351[141] for the transaction and Four Seasons Hotel Ltd. took a Vendor Take Back mortgage ("**VTB**") guaranteed by CHL for an additional $3.6 million.

[201] In the same month, Kevin Hsu abandoned his ownership position in Topven and Skyeboat, and the shares of Skyeboat were transferred to Lakeland Inc. ("**Lakeland**"). The shares of Skyeboat were pledged as security for the CHL loan to Skyeboat.

[202] In June 1986, an additional loan of $10.5 million was made by CHL to Skyeboat to repay a second mortgage loan from Robert Lee Ltd.[142]

[203] During 1986, CHL also advanced additional funds to pay Morguard Trust, the holder of the first mortgage on the hotel.

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[136] PW-469
[137] D-140
[138] PW-1053-48, seq. p. 186
[139] PW-1053-49, seq. p. 279
[140] as outlined in a handwritten memorandum in the 1983 working paper file as working papers E143 to E143M (PW-153-45 seq. pp. 291 to 300
[141] E153, PW-1053-38, seq. p. 154
[142] E135, PW-1053-35 seq. p. 154

[204] At December 31, 1986, loans totalling $36.1 million were owed to CHL and, in addition, CHL was guaranteeing the VTB with Four Seasons Hotel Ltd. for $3.6 million.

[205] In 1987, CHL loaned $6.7 million to Skyeboat to be used to repay the first mortgage on the hotel to Morguard Trust. In addition, the capitalization to the loan balances of interest and fees in the amount of $5 million, and other payments of $1.5 million raised the total amount of CHL's loans to the project to $49.3 million.

[206] By the end of 1987, the total amount of other secured indebtedness on the project was $4.4 million (of which $3.6 million was guaranteed by CHL), giving a total project indebtedness of $53.7 million.

[207] The common shares of Skyeboat were owned by Lakeland and the Class B Special shares were held by Lambert Securities ("**Lambert**")[143]. According to the testimony of Gaston Baudet on May 11, 1998[144], Lakeland and Lambert were owned by Wersebe and the owner of 321351 was 326902 which was held in trust by Granton Patrick and also owned by Wersebe[145].

[208] In February 1988, there was a corporate restructuring and refinancing of the Calgary Skyline project. The property was "flipped" from Skyeboat and 321351 to a new company, Skyview Hotels Limited ("**Skyview**"), with Skyeboat taking back a 70% ownership interest in the new company and 321351 taking a 30% ownership interest.

[209] As part of the restructuring, CHL and CHIF provided first and second mortgages for $25 million and $16 million respectively, and other material loans were secured by pledges of shares.

[210] By the end of 1988, Castor's exposure had increased to $59.4 million, including the $3.6 million guarantee to Four Seasons Ltd.[146], mainly due to the capitalization of interest on the loans arising from the restructuring.

[211] Castor's exposure on this project continued to increase in 1989 and 1990 due to the capitalization of unpaid interest and fees, and the financing in 1990 of the borrower's repayment of the $3.6 million debt to Four Seasons Ltd.

Ottawa Skyline Hotel

[212] The Ottawa Skyline Hotel ("**OSH**") was a 26 storey hotel of 450 rooms located in downtown Ottawa, only two blocks from Canada's Parliament Building[147]. The hotel land and building was held by The Royal Trust Company as Trustee, on behalf of Campeau

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[143] PW-1086-12
[144] PW-1199 : Rogatory commission of Gaston Baudet, May 11, 1998, response to Questions 6b and 16
[145] PW-1086-3 : Letter dated October 9, 1986 from Coopers & Patrick to Castor
[146] CHL loans 1097, 1143, 1147 and GL 408/1154 and CHIF loan 790002/2005 (ou 790002/2995)
[147] D-140

Corporation, the beneficial owner. Constructed in 1967, the hotel's operation was always leased to third parties.

[213] The York-Hannover group of companies became involved with the Skyline Ottawa in early 80s through York-Hannover Hotels Ltd ("**YHHL**"), when YHHL acquired a leasehold interest under the terms of a 1967 lease agreement that terminated in 1987, subject to two 10-year renewal options[148].

[214] In 1984, YHHL sold its interest in the lease, furniture, fixtures and equipment to its affiliate Skyline Hotels (1980) Ltd. ("**Skyline 80**").

[215] At December 31, 1987, the loan from CHL was in the amount of $10.494 million.

[216] At December 31, 1989, the loan balances to the Skyline Ottawa project had increased by $4 million to $14.494 million[149].

[217] In March 1990, 687292 Ontario Ltd. ("**687292**") purchased from Skyline 80 all the assets related to the operations of the Skyline Ottawa Hotel for $1 and assumed the debt related to the Ottawa Skyline[150].

DT Smith projects

[218] The DT Smith Group comprised nine construction projects and eight projects for which the land was being held for development or resale.

[219] The construction projects were as follows:

- Laguna I (David George Ventures, Inc.)[151]
- Laguna II (D.T. Smith Ventures, Inc.)[152]
- San Marcos -The Fairways (D.T. Smith Development, Inc.)[153]
- Wood Ranch I -The Greens (David George Companies, Inc.)
- Wood Ranch II – Village on the greens (D.T. Smith Homes, Inc.)[154]
- Dove Canyon I –Belvedere (David Smith Industries, Inc.)[155]

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[148] PW-462: Appraisal dated March 1, 1987 by A.H. Fitzsimmons & Co. Ltd., pp. 2 to 5; and D-44 Appraisal dated July 22, 1987 by Ron Juteau &Associates Ltd., pp. 7 and 8.
[149] Loans 1049 and 1152
[150] PW-1096-2
[151] Compendium PW-1125
[152] Compendium PW-1116
[153] Compendium PW-1117
[154] Compendium PW-1118

- Dove Canyon II -Club Vista (David Smith Industries, Inc.)[156]
- Chino Hills - Gordon Ranch/ Galloping Hills (D.T. Smith Industries, Inc.)[157]
- Tennis Court Villas at Monarch Beach (D.T. Smith Enterprises, Inc.)[158]

[220] The land development projects were as follows:

- Bonanza Homes (David George Ventures, Inc.)[159]
- Circle "R" Ranch (D.T. Smith Circle R, Ltd.)[160]
- Rancho California (D.T. Smith Communities, Ltd.)[161]
- Rancho Parcel 2 (D.T. Smith Rancho Parcel 2, Ltd.)[162]
- Rancho Parcel 5 (D. T. Smith Rancho Parcel 5, Ltd.)[163]
- Ritz Pointe (D.T. Smith Equities, Ltd.)[164]
- Santiago Ranch (D.T. Smith Properties, Inc.)
- Walker Basin (D.T. Smith Securities, Ltd.)[165]

[221] Laguna I project was part of the master-planned community of Niguel Ranch, adjacent to DT Smith's Laguna II (Vista Monte) project located in Orange County, California, mid-way between Los Angeles and San Diego.

[222] The Laguna II (Vista Monte) project consisted of 111 family homes on 25.4 acres of land within the master-planned community of Niguel Ranch in Orange County. The project was commenced in 1987 and upgraded in December 1988. The lots had good views onto the ocean.

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[155] Compendium PW-1115
[156] Compendium PW-1114
[157] Compendium PW-1119
[158] Compendium PW-1125
[159] D-1123
[160] Compendium PW-1123
[161] Compendium PW-1120
[162] Compendium PW-1121
[163] Compendium PW-1122
[164] Compendium PW-1124
[165] Compendium PW-1125

[223] The San Marcos (The Fairways) project consisted of 128 family homes on 28.9 acres of land within the master-planned residential and golf course community of Lake San Marcos in San Diego County. The project was commenced in 1987 and upgraded in December 1988.

[224] The Wood Ranch I (The greens) project in Simi Valley, Ventura County, successfully closed at profit in 1989 and Castor's loan was subsequently fully repaid. There were no loans outstanding and no cash balances on hand at December 31, 1990.

[225] The Wood Ranch II (Village on the Green) project consisted of 156 residential townhouses and condominium units on 12.6 acres of land within the master-planned residential and golf course community of Wood Ranch in the Simi Valley area of Ventura County. The project was commenced in 1988.

[226] The Dove Canyon 1 (Belvedere) project consisted of 116 single family homes on 21.7 acres of land within the master-planned residential and golf course community of Dove Canyon in Southern Orange County. The project was commenced in 1988.

[227] The Dove Canyon II (Club Vista) project consisted of 106 single family homes on 19.2 acres of land within the master-planned residential and golf course community of Dove Canyon in Southern Orange County. The project was commenced in 1988.

[228] The Chino Hills (Gordon Ranch/Galloping Hills) project consisted of 136 single family homes on 45.5 acres of land within the master-planned residential and golf course community of Gordon Ranch in San Bernardino County. The project was commenced in 1988.

[229] The Tennis Court Villas at Monarch Beach project closed at profit in 1990 and Castor's loan was fully repaid. The units were located across the street from Ritz Pointe.

[230] The Bonanza project consisted of 13.7 acres of land located in La Puente, Los Angeles County. The plan was to develop the property into 78 residential townhouses.

[231] The Circle "R" Ranch project consisted of approximately 54 acres of land within the Circle R Ranch Golf Course in Escondido, San Diego County. The property was to be developed into 212 detached single family homes within a residential and golf course community.

[232] The Rancho California project consisted of 57 acres of land subdivided into five separate but contiguous parcels totalling approximately 533 residential lots which were to be developed into a master-planned residential and golf course community within a project known as Winchester Mesa. Winchester Mesa was to form part of the master-planned community known as Rancho California in Riverside County.

[233] The Rancho Parcel II project consisted of 46 acres of land within the Murietta Hot Springs Golf Course in Rancho California, Riverside County and a master-planned community known as Rancho California. DT Smith purchased this land in 1989.

[234] The Rancho Parcel V project (Eagle Estates) consisted of 36.2 acres of land located within the Murietta Hot Springs Golf Course in Rancho California, Riverside County and within a master-planned community known as Rancho California. DT Smith purchased this land in 1989.

[235] The Ritz Pointe project, located in Dana Point, Orange County, consisted of 15.9 acres of land to be developed into 191 oceanfront residential townhouses and condominium units adjacent to the Monarch Bay Golf Course. The project was adjacent to the Tennis Court Villas project and was to be an integral part of the Laguna Niguel master-planned community of 550 acres, designed to hold 3,400 residential units, a golf course and a resort hotel. DT Smith acquired the property in 1989.

[236] The Santiago Ranch project, located in El Toro Foothills, Orange County, consisted of 120 acres of land to be developed into 162 units. The master-planned community had been approved for a total of 2,200 dwellings. It was located quite close to Dove Canyon, on a ridge with unobstructed views of the canyons and the Anaheim hills, and within commuting distance to Los Angeles.

[237] The Walker Basin project, located in Rancho California, Riverside County, consisted of an option to acquire land from Johnson & Johnson for the development of 631 lots. The land acquisition was to take place in 1991 and would have involved an additional outlay of $19.2 million.

Other properties

Meadowlark

[238] Meadowlark was a shopping center located in Edmonton Alberta, approximately one mile from the West Edmonton Mall.

[239] Castor's involvement in the project dated back to the early 80s.

[240] From September 1985 onwards, 50% of Meadowlark was owned by Leeds, a wholly owned subsidiary of YHDL, and 50% by Raulino Canada.

[241] During 1988, 1989 and 1990, Castor had 2 loans[166] secured by this project in the Montreal portfolio of loans, which ranked behind a $15 to $16 million first mortgage held by BMO[167].

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[166] Loans # 1030 and # 1117

Hazelton Lanes

[242] Hazelton Lanes was a luxury retail and residential development in Toronto's Yorkville area comprised of two sites.

[243] YHDL and Confederation Life held 50% undivided interest in the property.

[244] YHDL held its undivided 50% interest in the first site of the property through two wholly owned subsidiaries, 650188 Ontario Limited and 650189 Ontario Limited and its 50% interest in this second site through Hazelton Lanes Developments Ltd. [168]

Toronto Skyline Triumph

[245] The Toronto Skyline Triumph ("**The Triumph**") was a 10-storey hotel of 380 rooms located on Keele Street, City of North York in Metropolitan Toronto, Ontario[169].

The issues and the task

The issues and their components

[246] There are 5 issues: negligence, reliance, liability, damages and costs.

[247] The negligence issue involves three components: the audited financial statements, the valuation letters and the certificates for Legal for Life Opinions.

[248] The reliance issue involves deciding if there is a causal connection between negligence issue findings and Widdrington's investment decisions.

[249] The liability issue, assessing whether C&L shall be held liable for damages allegedly sustained by Widdrington, necessitates determining the applicable law and its content and, thereafter, its application to the specific facts of the Widdrington file (i.e. the findings on negligence, damages and reliance).

[250] The damages issue involves three components: Widdrington investment of 1989, Widdrington's investment of 1991 and Widdrington's claim for reimbursement of the

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[167] PW-1112A, PW-1112B, PW-1112C: Charts prepared by R. Smith showing the ownership structure of the project and the indebtedness at year-ends 1988, 1989 and 1990.
[168] PW-1059-2, PW-1059-6, PW-1059-8 and PW-1059-11; PW-1059-6A
[169] D-200

amount he paid to settle the claim against him further to the declaration of dividends and Castor's bankruptcy.

[251] The issue of costs involves discussing the costs of the first and of the second trial and ruling on the liability for such costs.

The task

[252] The Court's primary role is to seek the truth and resolve debates by considering both the expert and the lay evidence.

[253] Faced with competing theories, the Court cannot simply view contradictory evidence as the end of the debate – she must reach a conclusion.

[254] In the present case, burden of proof rests on the Plaintiff.

[255] In order for the Plaintiff to be successful, Plaintiff must prove its case on a balance of probabilities: this is not controversial. To meet the balance of probabilities, evidence must show that the events «*more likely than not*»[170] occurred in the manner presented by Plaintiff.

The negligence issue

General considerations

[256] Looking at the negligence issue in a professional liability case calls for the following particular considerations which apply equally in civil law and common law:

- Difference between negligence and error of judgment;
- Importance of the professional standards;
- Solution where there are different schools of thought;
- Warning against hindsight and today's professional standards.

[257] Looking at the negligence issue of an auditor's professional liability case calls for additional particular considerations which also apply equally in civil law and common law:

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[170] *F.H. v. McDougall*, 2008 SCC 53, [2008] 3 S.C.R. 41, para.49, AZ-50514295

- Knowledge of the respective role of management and auditor.

Difference between negligence and error of judgment

[258] Professionals are liable for damages caused by their negligent conduct when such conduct has fallen below the applicable standard of care. They are not liable for simple errors of judgment[171].

[259] Not every decision made is motivated by professional judgment. When it is, the Court must always consider whether the professional involved exercised his judgment honestly and intelligently[172].

[260] It is not defensible to characterize negligence as being part of professional judgment in the hope of escaping liability.

[261] A professional's work, as an auditor's work, is generally judged on the standard of «*whether it can be said that a reasonable professional in the position of the person accused of misconduct [would or] would not have acted as the person in question did*»[173]. Even if the liability of a professional is generally determined by comparing his or her conduct to the conduct of a reasonable professional placed in similar circumstances, based on common professional practice, no professional can exonerate oneself from liability if the common "*practice is not in accordance with the general standards of liability, i.e., that one must act in a reasonable manner*"[174].

[262] Indeed, negligence in the case of a professional cannot be assumed simply because the expected result has not been attained.

Importance of the professional standards

[263] It is generally accepted that when a professional acts in accordance with a recognized and respectable practice of his or her profession, he or she is not found to be negligent[175].

[264] In the case of auditor's liability, the standards involved are detailed and codified in the CICA Handbook, standards which are adopted by the profession following rigorous and thorough procedures. Such detailed and thorough standards are therefore entitled to great deference by the courts.

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[171] *Guardian Insurance Co. v. Sharp*, [1941] S.C.R. 164
[172] *Barrington v. The Institute of Chartered Accountants of Ontario*, [2010] ONSC 338, at para. 158.
[173] *Council for Licensed Practical Nurses v. Walsh*, [2010] NLCA 11 (CanLII) at para. 54; AZ-50610050.
[174] *Roberge c. Bolduc*, [1991] 1 R.C.S. 374, 1991 CanLii 83 (S.C.C.) at page 79; AZ-91111033; J.E. 91-412
[175] *Ter Neuzen v. Korn*, [1995] 3 S.C.R. 674, at page 695; AZ-95111103; J.E. 95-1970

[265] In rare instances, a Court may declare a standard negligent in itself when, for example, such standard is "*fraught with such obvious risks*" and so contrary to common sense that anyone would be capable of finding it negligent.

Solution where there are different schools of thought

[266] It is not the Court's role to choose between two accepted schools of thought within a given profession.

[267] While experts can shed light on a profession's given standards, and therefore help the court determine whether or not a professional has complied with those standards, the Court cannot condemn a professional that has favoured one method or one interpretation of a standard over another when both are accepted professional standards[176].

[268] The Handbook, like the Civil Code of Québec, is principle based and it is possible that there may be more than one reasonable school of thought within the profession with respect to the application of the Handbook in a particular circumstance. However, in order to be recognized, a school of thought must have a reasonable basis and cannot, for example, be an "opinion held by one person"[177].

Warning against hindsight and today's professional standards

[269] The Court should be wary not to use hindsight and cautious not to evaluate past conduct with later standards.

[270] Professional negligence often involves standards which are prone to evolve, such as GAAP and GAAS. As such, it is important to use the standards that existed at the time, in 1988, 1989 and 1990, not the ones that were applicable thereafter[178].

Respective role of management and auditor

[271] The auditor does not prepare the financial statements which are the responsibility of management.

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[176] *Lapointe v. Hôpital le Gardeur*, [1992] 1 S.C.R. 351; AZ-92111029; J.E. 92-302; *Ter Neuzen v. Korn*, [1995] 3 S.C.R. 674; AZ-95111103; J.E. 95-1970; *285614 Alberta Ltd. v. Burnet, Duckworth & Palmer*, [1993] A.J. No. 157; p. 382

[177] See, for example, *Litchfield v. College of Physicians and Surgeons of Alberta*, [2007] ABQB 584 (CanLII), aff'd by the Court of Appeal, *Litchfield v. College of Physicians and Surgeons of Alberta*, [2008] ABCA 164 (CanLII).

[178] *Ter Neuzen v. Korn*, [1995] 3 S.C.R. 674, at page 693; AZ-95111103; J.E. 95-1970.

[272] Management is responsible for the accurate recording of transactions and the preparation of financial statements in accordance with GAAP[179]. An audit does not relieve management of its responsibilities[180].

[273] The auditor conducts an examination of the books and affairs of the company according to the standards of his profession, known as generally accepted accounting standards ("**GAAS**").

[274] The objective of an audit of financial statements is to express an opinion on the fairness with which they present the financial position, results of operation and changes in financial position in accordance with generally accepted accounting principles or, in special circumstances, another appropriate disclosed basis of accounting, consistently applied[181].

[275] The auditor seeks reasonable assurance that the financial statements, taken as a whole, are not materially misstated. He normally designs his auditing procedures on the assumption of management's good faith[182]. The auditor is a watchdog, not a bloodhound[183].

[276] The auditor is not a guarantor of the financial statements issued by management[184].

[277] Since Castor was incorporated under the *New Brunswick Business Corporations Act*[185], and C&L appointed as auditor by the shareholders, various sections of this Act (namely sections 100 to 112) are relevant.

- The directors must place comparative financial statements, prepared in accordance with GAAP before the shareholders at every annual meeting[186] and when the shareholders have chosen to appoint an auditor, the statements must be accompanied by the auditor's report[187];

- The auditor must be independent of the directors and officers of the corporation[188];

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[179] PW-1419-1A, 5000.02 (1988); PW-1419-2A, 5000.02 (1989) and PW-1419-3A, 5000.02 (1990)
[180] PW-1419-1A, 5000.02 (1988); PW-1419-2A, 5000.02 (1989) and PW-1419-3A, 5000.02 (1990)
[181] PW-1419-1A, 5000.01 (1988); PW-1419-2A, 5000.01 (1989) and PW-1419-3A, 5000.01 (1990)
[182] PW-1419-1A, 5000.04 (1988); PW-1419-2A, 5000.04 (1989) and PW-1419-3A, 5000.04 (1990)
[183] *Guardian Ins. Co. v. Sharp*, [1941] S.C.R. 164, p.169-170; *In Re London General Bank (no.2)*, [1895] 2 Ch. 673; *In Re Kingston Cotton Mill Co. (no.2)*,[1896] 2 Ch. 279; *R.M.A. Restaurant Management Ltd v. Gallay*, J.E. 96-586 (S.C.); *Sarraf v. Awad*,J.E. 95-1881 (S.C.)
[184] PW-1419-1A, 5000.01 and 5000.04 (1988); PW-1419-2A, 5000.01 and 5000.04 (1989) and PW-1419-3A, 5000.01 and 5000.04 (1990)
[185] BCA, S.N.B. 1981, c. B-9.1., PW-2312-1
[186] BCA, S.N.B. 1981, c. B-9.1., sections 100(1) and 100(3); PW-2312-1
[187] BCA, S.N.B. 1981, c. B-9.1., PW-2312-1
[188] BCA, S.N.B. 1981, c. B-9.1., section 104(1); PW-2312-1

- The auditor is obligated to "*make the examination that is, in his opinion, necessary to enable him to report on the financial statements required (...)*"[189]- i.e., as to whether, in his opinion, the financial statements prepared by the management of the company and presented at the annual assembly represent fairly the financial situation of the company in accordance with generally accepted accounting principles ("**GAAP**");

- The present and former directors, officers, employees and agents are required «*upon the demand of an auditor*» to furnish the auditor with «*information and explanations*» and «*access to records, documents, books, accounts and vouchers of the corporation or its subsidiaries*» that in the auditor's opinion are necessary to make such an examination, as they are reasonably able to furnish[190];

- The directors are further required, «*upon the demand of an auditor*» to obtain such information and explanations from the present and former directors, officers, employees and agents of the corporation on the auditor's behalf[191];

- The directors must approve the financial statements in order for the corporation to issue, publish and circulate them[192]; and

- The directors are entitled to rely on the auditor that such financial statements fairly reflect the financial condition of the corporation, as they are not liable for various decisions made when they reasonably rely on a report from the company's auditors[193].

Books and records

[278] Defendants assert that there are issues of integrity of books and records available to the Court: Castor's books and records and YH's books and records.

Castor's books and records

[279] Defendants' experts Donald Selman ("**Selman**"), Russell Goodman ("**Goodman**") and Phillip Levi ("**Levi**") assert that there is an issue of integrity of the books and records of Castor.

[280] Selman writes:

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[189] BCA, S.N.B. 1981, c. B-9.1.,section 110(i); PW-2312-1
[190] BCA, S.N.B. 1981, c. B-9.1., section 111(1); PW-2312-1
[191] BCA, S.N.B. 1981, c. B-9.1.,section 111(2); PW-2312-1
[192] BCA, S.N.B. 1981, c. B-9.1., section 102(2); PW-2312-1
[193] BCA, S.N.B. 1981, c. B-9.1., section 80(3); PW-2312-1

"It is unsafe to assume that the Castor documents that are presently before the Court were available to be seen by the auditors in anything like their entirety.[194]"

[281] Goodman writes:

"I'm not satisfied that the complete Lambert Securities loan files in safekeeping contents were preserved and made available to the Court and to the parti es[195]."

[282] Levi writes:

"It is important to consider whether what everyone is looking at today represents what Coopers & Lybrand had available to examine during their audits in 1988, 1989 and 1990.[196]"

[283] It is true that:

- During the spring of 1992, records of the overseas subsidiaries kept in Montreal, Zug and Schaan were shipped to their respective jurisdictions[197] - the accounting records kept in Zug were shipped to Castor's Zurich office, while the non-accounting records kept in Schaan were removed by Gross and taken to his garage (for a period of 2 to 3 weeks) from where they were packed and shipped, together with the accounting records, to the various jurisdictions[198].

- On July 9, 1992, Castor's trustee in bankruptcy Bernard Gourdeau ("**Gourdeau**") took possession of Castor's offices located in Montreal and ascertained the state and condition of the premises - some documents were shredded, some filing cabinets and file folders were empty - all evidenced by video[199].

- The trustee did not take possession of the offices located in Toronto, Calgary and New York City[200] and the records that were located therewith were only obtained from the landlords of such premises after July 9, 1992.[201]

- During the period that the records of the subsidiaries were in the hands of the foreign trustees and/or official liquidators, the Trustee did not ask for detailed and complete inventories of the records found in their possession and did not put into place any control measures to ensure that the integrity of the records would not be compromised[202].

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[194] D-1295, at page 376
[195] D-1312, at page 500
[196] D-1347, at page 8
[197] D-941; Gross October 4, 1999 p. 375-390
[198] Gross October 4, 1999 p.375-390
[199] Video produced as D-644 & D-941 Memorandum dated July 10, 1992, prepared by Gourdeau
[200] Gourdeau February 18, 2008, p. 273
[201] Gourdeau February 18, 2008, p. 273-276
[202] Gourdeau February 19, 2008, p. 5, 58-59, 70-71, 74-76, 104, 106-107, 111, 129-130

- in December 1992, the Trustee authorized the release of all records and documents in the possession of Trust Management and Finance ("**TMF**"), relating to Castor, CH International (Netherlands) BV, Castor Finanz AG and Castor Investment AG, to Gambazzi's attorneys for the purpose of finalizing the companies' 1991 year end books, financial statements and corporate filings, but no inventory was kept of what was released[203].

- Records relating to transactions between Castor and Trinity stored in a warehouse in Connecticut or Vermont were not retrieved by the Trustee (even though he consulted and reviewed such records without making an inventory) and such records were subsequently destroyed[204].

- Gourdeau testified that he collected documents from other sources, such as YH documents from BDO and Whiting, and documents from Dragonas, commingled them with the Castor records he found on premises, and that he is unable today to determine which of the documents now in his possession came from Castor's records and which came from other sources[205].

- Rancourt testified that there were a few loan ledger cards that she worked with that were no longer in the Castor records she was shown in preparation for trial[206].

- When Gourdeau retrieved documents (paper copies) a few years after they were scanned to allow computerized consultation, he had to reorganize them and was no longer able to reconstruct their previous state[207].

[284] Nevertheless, the nature and types of documents that were kept by Castor in Montreal up to July 1992 and the nature and types of documents that were kept by the overseas subsidiaries have been established.

[285] Five lay witnesses employed by CHL testified (Tooke, Rancourt, Simon, MacKay and Ron Smith). All of them, whether called by Plaintiff or Defendants, affirmed that the Canadian books and records that they reviewed in order to testify were accurate concerning what existed at the time that they were employed at Castor.

[286] Regarding the Canadian books and records, the evidence of Tooke and Rancourt clearly demonstrate that the books of original entry that they reviewed for

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[203] PW-2391-5 and Gourdeau, February. 19, 2008, pp. 58-61 and 142- 146; PW-2391-2 and Gourdeau January 14, 2008 p. 98-104 and p. 135-140; PW-2393-1; Gourdeau, February 19, 2008, p. 142-143
[204] Gourdeau, February 18, 2008, p. 277-279
[205] Gourdeau, January 14, 2008 p. 96-97, 144; Gourdeau, January 30, 2008, p. 76-77; Gourdeau, February 19, 2008, p. 214-217: Gourdeau, February 22, 2008, p. 61-63;
[206] Rancourt, February. 29, 2008, p. 164-165 and 176-179 and PW- 167A-1
[207] Gourdeau, February. 19, 2008, pp. 191-192 and 202- 217

purposes of this trial were the same books and records that existed and were made available to C&L for purposes of their audits[208].

[287] Insofar as the books and records of the off-shore subsidiaries are concerned, the exhaustive correlation exercise performed by Vance[209] strengthened the Court's conclusion that the records referred to by C&L in their audit working papers ("**AWPs**") are the same records that are in evidence before her.

[288] There is absolutely no evidence to suggest that documentation was requested by C&L and suppressed by Castor.

[289] Gourdeau explained the source of the records, the manner in which they were stored (and shared with C&L) and the unprecedented efforts made by the Trustee to compile a virtually complete set of documents[210].

[290] There is no credible evidence that the Castor documents that were shown to the auditors for the audits, and that are in the possession and control of the Trustee, are unreliable.

[291] None of the audit staff members ever testified that a document that they relied upon for their audit no longer exists. The sole exception is the case of the alleged Lambert financial statements referred to by Ford during her testimonies[211], statements that are not at all mentioned in her working papers. Given the circumstances surrounding the work performed by Ford in relation to the Lambert loans during the relevant years[212] and taking account of reasons later enunciated in the present judgment in relation to Ford's credibility and reliability[213], the Court grants no weight to Ford's testimony that she would have seen Lambert financial statements.

[292] During the trial, in examination in chief, Levi opined that because certain appraisals which were referenced in the AWPs do not correspond with the dates or the authorship of appraisals filed in the court record, this would be evidence that documents are either unreliable or have been suppressed[214].

[293] Levi went on to state that «*there are other examples in other years where auditors had marked down names of appraisal companies and the appraisals can't be*

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[208] Tooke, February 27, 2008, pp. 62-63; Rancourt, February 29, 2008, pp. 164-165.
[209] Vance, March 5, 2008, pp. 77-79; PW-1484. See for example PW-1484-5-1.
[210] See, for example, Gourdeau, January 14, 2008, pp. 67-73, 93-98, 101-104, 135-143.
[211] Ford, November 9, 1995, pp. 41-44; Ford, November 14, 1995, pp. 67,73,81,83to85, 152; Ford, September 5, 1996, pp. 123; Ford, December 7, 2009, pp 171-174.; Ford, December 11, 2009, pp.66 and followings.
[212] Ford, November 7, 1995, pp. 172-173 and 192 to 197; Ford, November 14, 1995, pp. 49 to 99, 109-110 and 151-154; Ford, September 5, 1996, pp. 88-92 and 129-131; Ford, December 11, 2009, pp. 66 and followings.
[213] See the subheading
[214] Levi, January 13, 2010, pp.50 -59

found in the files. I could understand one auditor making a mistake of this type in one area of the file once. I find it difficult to believe that the same type of error is found in terms of documentation in the files two or three times or more over two or three years».[215]

[294] In cross-examination however, since the evidence before the Court clearly establishes that C&L erroneously recorded information and brought erroneous information forward from audits of previous years, Levi had no choice but to recognise that it was plausible that the so-called missing appraisals were merely errors made by the audit staff. [216]

[295] At the Court's request (since counsel for the Defendants were alleging that documents referred to in the audit working papers had never been found, without Defendants testifying to that effect), counsel for Defendants provided a grocery list of what they purported were missing documents that their clients asserted or referred to in their audit working papers for the years 1988, 1989 and 1990[217]. Counsel for the Plaintiff raised an objection to certain of those references.[218]

[296] Having the list of the documents that are referred to in the audit working papers and that Defendants have characterized as missing (including reference to the same document in multiple audit years) that relate to subject matters that have been discussed in evidence, gives the Court the opportunity to look at them and consider, in a concrete manner rather than an abstract manner (fact rather than theory) the merit of the assertions that there would be a myriad of missing documents such that the Court cannot assess the work performed by C&L.

[297] Having done such an exercise, the Court concludes that the references in the audit working papers that were identified by counsel for the Defendants and which were subject matters discussed in evidence are quite evidently, in most cases, errors made by the audit staff.

- Appraisal by Mullins & Company in 1988[219]
    - On May 16, 2008, Ron Smith testified that there was no appraisal done by Mullins & Co. in 1988 – that the Mullins & Co. appraisal was done in 1983 – that by 1987, Mullins had left and joined Gillis & Co. – and that the appraisal was done by Hughes in mid 1988.[220]

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[215] Levi, January 28, 2010, pp. 118-119.
[216] Levi, January 28, 2010, pp. 166-167.
[217] September 20, 2010 (pm), pp.101 to 121
[218] September 20, 2010 (pm),pp.118 and 121 to 125
[219] PW-1053-23, sequential page 153
[220] Ron Smith, May16, 2008, pp.154-155

- The Court record includes a Gillis appraisal done in 1988, PW-493, and signed by Mullins which supports Ron Smith's assertion that there was no Mullins & Co. to perform an appraisal in 1988.

- Appraisal of 94 million dollars – mention *"(Appraisal)"* beside the "*Total security*" title in the 1989 working papers[221]

  - In 1988, there is a similar schedule in the working papers where it is written *«Total security: 94 million"* without any reference to an appraisal[222].

  - In 1987, we see again the figure of 94 million of security referenced to the working paper B-41. Said working paper B-41 is a memo written by Ron Smith to Mr. Wilson, of Coopers & Lybrand, on February 24th, 1988, where Smith refers to an appraised value of the Maple Leaf Village of 130 million and to first and second mortgages debts. On the memo, beside those figures provided by Ron Smith, there is the handwritten inscription: "approximately 94 million in security".[223]

  The Court concludes that there never was an appraisal for 94 million. Ford added the word "Appraisal" without any further details, work got carried forward year after year mechanically. At the time of the 1987 audit working papers the appraisal that existed was of 130 million.

  The Court also concludes that there was no 1988 separate appraisal by Mullins for 130 million. Clearly in 1987 there was an appraisal already being relied on by Coopers & Lybrand of 130 million which could certainly not be a Mullins appraisal of 1988.

- Thorne-Riddell evaluation showing the common shares to be worth $19.50[224]

  - In both instances, in the 1988 working papers and in the 1989 working papers, the figure is referenced by tick mark "*as per 1986 working paper file*". C&L is relying on its own product work – not on a third party paper.

  - Ron Smith testified that nobody ever questioned him about the common shares value, that the only reference he ever had was a letter from York-Hannover dated December 28, 1984, addressed to Stolzenberg, and that he assumes that Thorne-Riddel were, at the time, the auditors of MLVII[225].

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[221] PW-1053-89, sequential page 261
[222] PW-1053-91, sequential page 248
[223] PW-1053-93, sequential pages 169-170
[224] PW-1053-23, sequential page 157 and PW-1053-19, sequential page 159
[225] Ron Smith, May 16th, 2008, p.150-151

- Daniel Séguin (the auditor who did the investment section in the 1988 audit in Montreal) and Linda Belliveau (the auditor responsible for the investment section in Montreal for the 1989 audit) testified to the effect that they relied on their prior working papers and did not do any independent investigation to determine whether the value of $19.50 was appropriate[226].

- In the 1987 working papers, it is written that Thorne-Riddell performed an evaluation showing common shares to be worth $19.50 each "*as per the 1986 working paper file*". [227]

- In the 1986 working papers, it is written "*appears under secured, however Thorne-Riddell performed a valuation showing common shares to be worth 19.50 each*" without any further reference to support this representation.[228]

- In the 1985 working papers, C&L is concerned that the loans are under secured but still writes "*However, Thorne-Riddell performed an evaluation showing common shares to be worth $19.50 each*" without any tick legend[229].

- On December 31, 1984 and under Stolzenberg's signature, Castor Holdings Limited agreed and confirmed its acceptance of the proposed common shares valuation (at the bottom of the letter mentioned by Ron Smith, a letter dated December 28, 1984 from York-Hannover addressed to Stolzenberg and produced as exhibit PW-1073-1).

- Thorne-Riddell were the auditors of MLVII as of December 1984[230].

Exhibit PW-1073-1 is, in all probability, the source of the repeated reference to a Thorne-Riddell evaluation in the audit working papers of 1985, 1986, 1987, 1988, and 1989.

- Appraisal – Dove Canyon I and Dove Canyon II[231]

  - In 1989, under the column "Appraisal", the amount written for Dove Canyon I is $26,960,000 U.S. and the amount written for Dove Canyon II is $29,710,000 U.S.[232]

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[226] Séguin, December 12, 1995, pp.77-79, 89-92; Belliveau, April 12, 1996, pp.213-214
[227] PW-1053-27, sequential page 96
[228] PW-1053-35, sequential page 113
[229] PW-1053-38, sequential page 159
[230] PW-478
[231] PW-1053-83, sequential page 114 (for 1989); PW-1053-81, sequential pages 78 to 81 (for 1990)
[232] PW-1053-83, sequential page 114 (for 1989)

- In the commitment letter for Dove Canyon I, dated November 3, 1988, the amount is $26,959,590 U.S.[233]

- In the commitment letter for Dove Canyon II, dated November 3, 1988, the amount is $29,716,037 U.S.[234]

- Ron Smith testified that there were no such appraisals.[235]

- Ford acknowledged that she had not written in her working papers that she had actually seen appraisals, that she did not recall when she could have received an appraisal, that she might have seen only a summary report and that her figures resembled seriously the maximum funding for each project.[236]

- The appraisals that existed for Dove Canyon I were done in April and October 1988[237]; the appraisals that existed for Dove Canyon II were done in April and October 1988[238].

There are no missing appraisals for these projects and, in fact and again, this is an excellent example of a very clear audit error by Ford.

- Valuation of Hazelton lanes[239]

  - In the 1988 working paper, on the loan evaluation questionnaire filled by Daniel Séguin, the following inscriptions appear: "*Appraisal (name):Royal LePage; Appraisal (date) 1988; Appraisal (amount), 52.5million*"[240]. There is no specific date for the appraisal.

  - In the 1989 working paper, filled this time by Linda Belliveau, the same types of reference appear: no details and no specific date[241].

  - In the 1990 working paper, filled by Martin Quesnel, again the same types of reference appear: no details, no specific date and no tick marks[242].

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[233] PW-1115-6B
[234] PW-1114-7B
[235] Ron Smith, June 10, 2008, pp.193-196
[236] Ford, December 9, 2009, pp.43-45
[237] PW-1115-4 and PW-1115-7
[238] PW-1114-5 and PW-1114-9
[239] PW-1053-23, sequential page 182, (1988), PW-1053-19 sequential page 183 (1989) and PW-1053-15, sequential page 177 (1990)
[240] PW-1053-23, sequential page 182
[241] PW-1053-19 sequential page 183
[242] PW-1053-15, sequential page 177

- Linda Belliveau cannot indicate what she relied on to write down that Hazelton Lanes had been appraised at 52 million dollars by Royal LePage in 1988. [243].

- Quigley, a witness called by the Defendants, and who was working for YHDL at the time, testified that they had Royal LePage appraisals for various properties, but that they probably had only an internally prepared estimate for Hazelton lanes.[244]

- Whiting's testimony corroborates Quigley's that there was no Royal LePage appraisal performed on Hazelton lanes[245].

- The figure of 52 million appears in a memorandum from Dean Anton of YHDL to Wersebe, Stolzenberg, Dragonas, Levesque and Smith dated December 5, 1988[246] relating to a proposed "*Scotia McLeod transaction*".

Again, nothing is missing.

- Royal LePage appraisal – Southview mall[247]

  - In the 1987 working papers[248], the type of loan is "*second mortgage*"[249], the reference to the collateral given is "*shares*" and their value is 5 million[250], the amount of the first mortgage is 4 million[251] and the reference to the collateral available is 9 million[252] but without any name of appraiser or date of appraisal. This appears to be the genesis of the information that appeared in the subsequent audit working papers.

  - In the 1988 working papers, on the loan evaluation questionnaire filled, the following inscriptions appear: "Appraisal (name): Royal LePage; Appraisal (date) 1987; Appraisal (amount), 9 million" . There is no specific date for the appraisal[253].

  - In the 1989 working papers, on the loan evaluation questionnaire filled by Linda Belliveau, the following inscriptions appear: "Appraisal (name):

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[243] Belliveau, May 22, 1996, pp. 328-330
[244] Quigley, March 15, 2010, p. 91
[245] Whiting, November 30, 1999 p.67
[246] D-137
[247] PW-1053-23, sequential page 178, (1988); PW-1053-19, sequential page 179, (1989); PW-1053-15, sequential page 180, (1990)
[248] PW-1053-27, sequential pages 194, 195 and 196
[249] PW-1053-27, sequential page 194
[250] PW-1053-27, sequential page 194
[251] PW-1053-27, sequential page 194
[252] PW-1053-27, sequential pages 195 and 196
[253] PW-1053-23, sequential page 178, (1988);

Royal LePage; Appraisal (date) 1987; Appraisal (amount), 9 million". There is no specific date for the appraisal[254].

- Linda Belliveau testified and could not say if the collateral available was in fact a mortgage or shares. She acknowledged that she had reviewed the loan as a mortgage loan. She could not recall if she had seen an appraisal but she acknowledged that when she did she usually put a tick mark and that there was none on her working paper.[255]

- In the 1990 working papers, on the loan evaluation questionnaire filled, the following inscriptions appear: again, "Appraisal (name):Royal LePage; Appraisal (date) 1987; Appraisal (amount), 9 million" – no specific date for the appraisal – but an appraisal of Shaske & Associates dated 1991, in the amount of 8.3 million, is also mentioned[256].

- Royal LePage was the only appraiser's name with which many auditors who performed the investment section of the audit of 1988, 1989 and 1990 were familiar with.

- In 1988, the Southview shopping center was valued at approximately 7.8 million as per the audited financial statements of Thorne Ernst & Whinney for the year ended on September 30, 1988[257]. This information is very consistent with the notation in 1990 of the Shaske & Associates appraisal dated 1991, in the amount of 8.3 million.

The Court concludes that nothing is missing.

- MLV project appraisals in 1989 and 1990[258]

  - In the 1989 working papers, there are two appraisals referred to – a Pannell Kerr Forster, 1989, of 104 million for the hotel, and a Hughes & Associates appraisal, 1989, of 40 million for the shopping centre[259]. At the bottom of the page, we see that the total of the appraisal is 144 million. The appraised value gets carried forward onto the next page (Page 170) at 144 million.

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[254] PW-1053-19, sequential page 179, (1989);
[255] Belliveau, May 23, 1996, pp. 516-520.
[256] PW-1053-15, sequential page 180, (1990)
[257] PW-1163-9
[258] PW-1053-19, sequential page 169, (1989), and PW-1053-15, sequential page 160, (1990)
[259] PW-1053-19, sequential page 169

- In the 1990 working papers, the same information is carried forward[260]. This information was mechanically carried forward from one audit year to the next, with no verification of the information.

- Ron Smith testified that he showed the auditors everything he had on hand[261] which was:

  - a Mullin's appraisal of 1983 in the amount of 130 million;

  - a Hughes appraisal dated 1988 with figures of 67.7 million or 104 million and a Pannell Kerr Forster study to back-up the Hughes' appraisal;

  - a McKittrick appraisal dated 1989 for 26 million.

- Ron Smith testified that Hughes never prepared an appraisal in the amount of 40 million[262].

- Prychidny testified that in a memo[263] there was a reference to a 40 million figure for the mall and developable land: 30 million for the mall, based on the McKittrick appraisal of 26 million, and 10 million for developable land, on the input of Wersebe.[264]

Nothing is missing.

- <u>Appraisals for the TWTC in 1989 and 1990</u>[265]

  - In the 1989 working papers, references are made to a Royal LePage appraisal of 70 million for the condominiums and to a figure of 145 million for three office landsites offers, December 5, 1989. C&L added those figures and came up with a total of 235 million (instead of 215 million) – a clear mathematical error.

  - Same information is carried forward the next year, including the error, in the 1990 working papers[266].

  - Ron Smith testified[267] that he never indicated that he had appraisals – he had estimates that had been provided to Castor by YHDL – one of 70

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[260] PW-1053-15, sequential page 160
[261] Ron Smith, May 16, 2008, pp. 171-173
[262] Ron Smith, May 16, 2008, p 173
[263] D-145
[264] Prychidny, November 10, 2008, pp.115-117
[265] PW-1053-19, page 197, (1989) and PW-1053-15, sequential pages 222 and 223, (1990).
[266] PW-1053-15, sequential page 222
[267] Ron Smith, September 16th, 2008 pp. 180-183

million for the condominiums[268] and one of 145 million for the office sites – in both years, he showed the auditor the same thing.

- PW-1069-8 is a letter from YHDL to Castor, dated September 13, 1989, enclosing the agenda for a TWTC partnership meeting which includes value information and where Royal LePage's name appears.

- PW-1069-13 is a confidential agreement dated December 5, 1989, that was made with Coldwell Banker Canada who was granted the exclusive right to obtain offers in respect of the property at a gross sales price of 145 million dollars.

Nothing is missing.

- Appraisals – TWTC for 1988 and 1989[269]

  - In the 1988 working papers, the following information appears: "*Appraisal (name) Stewart Young Mason Limited, (date) April 6th, 1987, (amount) 182 million to 285 million*"[270].

  - The same information appears in the 1989 working papers[271].

  - Ron Smith testified that he never provided the above-mentioned information to the auditors. The only thing he had and he showed them was an appraisal from Stewart Young Mason Limited dated February 12, 1987 with a value range of 62.6 to 104.6 million for the 50% interest on the project controlled by YH and Bimcor[272].

  - PW-1069-17 is an extract from an appraisal from Stewart Young Mason Limited dated February 12, 1987 showing a value range of 62.6 to 104.6 million.

  - Linda Belliveau testified that what appears on working paper E221, in the 1989 working papers, is a copy of the previous year where she had handwritten "Royal LePage" beside the name of Stewart Young Mason Limited[273].

Nothing is missing.

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[268] PW-1069-8
[269] PW-1053-23, page 201 (1988), PW-1053-19, page 198, (1989)
[270] PW-1053-23, page 201
[271] PW-1053-19, page 198
[272] Ron Smith, September 16, 2008, pp.177-178
[273] Belliveau, April 11, 1996, p.41

- Securities kept in Schaan[274]

  - When Ford made her note "*loan supported by securities of other companies held in safekeeping in Schaan*", she was not doing a valuation of Lambert Securities loans[275].

  - The securities of other companies supporting the loan and held in safekeeping in Schaan were described in schedule A of the pledge agreement[276].

  - Other documents are evidence of those securities[277].

  Nothing is missing.

- Cadiz Landfill and appraisal of 6.4. million listed[278]

  - Ford listed an appraisal of 6.4 million for the Cadiz Landfill, but there are no tick marks in her working paper. Moreover, at the bottom of the page, Ford wrote: ""*It is our understanding that appraisal reports are held in Cyprus and we would appreciate receiving a summary of the reports providing the minimum following information.*"

  - The information that was provided to C&L appears in the same volume of working papers[279]: a summary, as requested, indicating a value of 6.4 million.

  Clearly, nothing is missing.

- Some loan ledger cards (part of PW-167)

  - Plaintiff acknowledges that some loan ledger cards are missing. The list of such missing loan ledger cards has been produced as PW-167-1A.

  - Rancourt has testified that the information can be reconstituted from the mortgage spreadsheet (PW-107) as well as the interest receipts.

[298] Other references that were identified by Counsel for the Defendants, under objection from Counsel for the Plaintiff as mentioned previously, are totally irrelevant to

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[274] PW-1053-89, page 255
[275] Ford, December 11, 2009, pp.76-87
[276] PW-1195
[277] PW-1079-4 (Telex from Ron Smith to Banziger), part of PW-136; PW-136 (various shares certificates), PW-1053-93, sequential page 150 (B-26) – working papers of 1987; PW-1053-95, sequential page 181 to 196 (B-31) – working papers of 1986; PW-1079-12
[278] PW-1053-83, sequential page 103
[279] PW-1053-83, sequential page 144

the issues that were raised with witnesses during examination before and during trial. However, given the general issue of reliability of books and records that Defendants have raised and their suggestion to the Court to draw inferences of deceit or fraud on the auditor from any evidence of missing documents, the following remarks are essential.

- If Defendants wanted the Court to draw inferences from the fact that documents would have been seen and used by them whereas they were later missing, the burden of proof rested on them.

- A statement by counsel is no evidence, and the objection raised by Counsel for the Plaintiff on September 20, 2010 is maintained[280].

- As noted during the oral representations on September 24, 2010, Plaintiff's Counsel had things to say and documents to show to rebut Defendants' Counsel suggestions of further missing documents[281].

[299] Bottom line, the Court shares Vance's point of view that the concern about the books and records of Castor "*has no basis, given the documentation that exists and given the correlation between the documents and the working papers*"[282].

[300] In fact, one of the remarkable aspects of the Castor case is the completeness of Castor's documentation. As Vance testified «*it's almost extraordinary the degree of completeness of the Castor's books and records that I reviewed considering that Castor, as an [active] company, was no longer alive as we referred to it.*[283]»

YH books and records

[301] There is no evidence that C&L asked for or relied on any YH documents that were not amongst Castor's books and records.

[302] There is nothing in the evidence of Sharma, trustee in bankruptcy to YHDL, to support the conclusion that the documents in the possession and control of the Trustee of YHDL are unreliable in any way that did or could have affected the audits performed by C&L.

[303] The documents that have been filed into evidence assist the Court in understanding the factual matrix relevant to issues such as the financial condition of Castor's most important group of borrowers and the various YH loans and projects being financed by Castor.

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[280] Transcript, September 24, 2010, p.6
[281] Transcript, September 24, 2010, pp.3 to 8, Trial notes, September 24, 2010, Transcript, September 28, 2010, pp.3-5 ,Trial notes, September 28, 2010 and sealed envelope
[282] Vance, April 16, 2010, p. 79
[283] Vance, April 16, 2010, p. 71.

[304] The evidence is corroborated by the testimony of witnesses from Castor and YH and is reliable.

The negligence issue as it relates to the audited consolidated financial statements

Questions and tools

[305] Deciding the negligence issue as it relates to the audited consolidated financial statements requires answering the two following questions:

- Are the audited consolidated financial statements of Castor for 1988, 1989 and 1990 materially misstated and misleading?
- Did C&L commit a fault in the professional work that they performed in connection with the audits of Castor for 1988, 1989 and 1990?

[306] The identification, interpretation and application of the generally accepted accounting principles ("**GAAP**") are at the heart of the required analysis of the first question.

[307] The identification, interpretation and application of the generally accepted auditing standards ("**GAAS**"), including the impact of fraud on the auditor, are at the heart of the required analysis of the second question.

Overview of expert opinions on GAAP and GAAS

[308] All experts agree that C&L had to comply with GAAP and GAAS at all relevant time.

Plaintiff's experts

[309] Three expert witnesses appeared on behalf of the Plaintiff and testified on the negligence issue as it relates to the consolidated audited financial statements: Keith Vance ("**Vance**"), Kenneth Froese ("**Froese**") and Lawrence S. Rosen ("**Rosen**").

Vance

[310] Vance opines that:

- "*the audits carried out by C&L for each of the years 1988, 1989 and 1990 were inadequate and did not meet GAAS*";[284]

- "*these financial statements contained material misstatements and were misleading owing to (...) departures from GAAP, that, had GAAS been complied with, should have been identified and acted on by the auditors* "[285];

- "departures from GAAP (...) should have been uncovered and/or addressed by an audit that was in compliance with GAAS"[286];

- "*In view of the materiality of the above departures from GAAP, C&L, had they determined the extent of the misstatements, should have seriously considered whether the going concern basis of accounting was appropriate in the circumstances*"[287].

[311] Vance concludes that «*considering the extent of the misstatements in the consolidated financial statements of Castor for the years ended December 1988, 1989 and 1990, C&L should not have issued unqualified opinions on these financial statements, but should have either denied an opinion or issued an adverse opinion indicating the extent to which the financial statements were materially misleading and stating that these financial statements did not present fairly the financial position, results of operations and changes in financial position of Castor.*»[288]

Froese

[312] Froese opines that «*Castor's financial statements for the years ended December 31, 1990, 1989 and 1988 did not comply with GAAP in relation to loans in relation to...*" and that "*the financial implications to Castor of placing the above loans on a non-accrual basis, and the magnitude of the increase in Castor's allowance for loan losses, created uncertainty as to Castor's ability to continue as a going concern at least as early as December 31, 1988*».[289]

[313] On the issue of fraud, Froese opines that

- "*the extent of suspicious circumstances in each of the years from 1988 to 1990 was such that C&L should have had suspicions as to management's integrity and the possibility of material financial statement fraud. Some of the suspicious circumstances were apparent in the scope limitations agreed to by C&L, others were contained in the evidence gathered in C&L's audit working papers but not*

[284] PW-2908, Vol.1, S-22
[285] PW-2908, Vol.1, S-23
[286] PW-2908, Vol.1, S-24
[287] PW-2908, Vol.1, S-25
[288] PW-2908, Vol. 1, S-25; See also PW-3033, pp. 1-3; PW-3034, pp. 9-11, at p. 11.
[289] PW-2941, Vol. 1, pp. 24-26.

identified as such by C&L, and other red flags were apparent in loan files and Castor's financial records";[290].

- *"sufficient appropriate audit evidence" was readily available to C&L to permit C&L to conclude that Castor's consolidated financial statements were materially misstated in each of the years ended December 31, 1990, 1989 and 1988, in spite of the alleged fraud by management and others".*[291]

Rosen

[314] Rosen concludes that GAAP and GAAS were breached and that the audited financial statements had no relationship to the reality of Castor[292].

> A major conclusion is that C&L did not conduct their audit in accordance with generally accepted auditing standards ("GAAS"), that the consolidated financial statements of Castor were not prepared in accordance with generally accepted accounting principles ("GAAP") and that the consolidated financial statements were materially misleading.[293]
>
> Notwithstanding the passage of time and my review of various exhibits produced during the first trial before Mr. Justice Carrière, the conclusions that I reached in the Initial Report have not changed (...)[294]

[315] Rosen also concludes that the claim by C&L that any GAAP and GAAS and related deficiencies in Castor's 1988, 1989 and 1990 financial statements would be due to incomplete, inaccurate, false or misleading information provided to the Defendants by Castor through its Directors, Officers, senior employees and consultants was "*clearly inappropriate and unwarranted*"[295].

Defendants' experts

[316] Three expert witnesses appeared on behalf of the Defendants and testified on the negligence issue as it relates to the consolidated audited financial statements: Donald Selman ("**Selman**"), Russell Goodman ("**Goodman**") and Phillip Levi ("**Levi**").

[317] None of Defendants' expert witnesses provided an overall opinion on the audited financial statements.

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[290] PW-2941, Vol. 1, page 153, paragraph 8.30,
[291] PW-2941, Vol. 1, page 153, paragraph 8.31,
[292] Rosen, Transcript February 5, 2009, pp. 157-158.
[293] PW- 3033, volume 1, « Brief summary section »
[294] PW-3034, page 1
[295] PW-3034, pages 2 and 3

- Selman's mandate was limited to specific GAAP and GAAS issues, excluding the loan loss provision aspect[296].

- Goodman's mandate was limited to the valuations of certain loans and to GAAP issues relating thereto :

  "*Price Waterhouse was engaged by counsel to C&L in 1993 in connection with litigation between the Plaintiffs and C&L relating to the failure of Castor. The purpose of the Price Waterhouse engagement was to provide opinions in connection with the valuations, in accordance with GAAP, of Castor's loans for the years ended December 31, 1988, 1989 and 1990. My report entitled the Price Waterhouse Report on Loans dated May 29, 1998 was issued pursuant to the initial engagement.*

  In February 2008, I was asked by counsel to prepare this Updated Report on Loans in order to consider trial evidence as well as the reports of Messrs. Vance, Froese, Rosen and Brenner. I was asked to consider only Castor's loans to the YH Group and DT Smith Group and to exclude from consideration any loans for which Messrs. Vance, Froese and Rosen did not suggest loan loss provisions. With respect to the loans to the YH Group and DT Smith Group, this Updated Report on Loans replaces my 1998 Price Waterhouse Report on Loans".[297]

- Levi's mandate was "*to provide an expert opinion with regard to any evidence of fraudulent activities or transactions in relation to the audit of Castor Holdings Ltd. for the years ended December 31, 1988, 1989 and 1990 as well as any other matters pertaining to this litigation on which I am able to provide expertise*"[298].

Selman

[318] There is no overall conclusion or opinion section in Selman's report. Selman was engaged to carry out specific assignments[299].

Goodman

[319] Goodman's overall conclusion reads as follows:

> Having carried out my own examination for purposes of this Updated Report on Loans, I conclude that, in my opinion, the consolidated financial statements of Castor for the years ended December 31, 1988, 1989 and 1990 were **not misstated as** a result of errors in the measurement and valuation of Castor's

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[296] D-1295, page 1 section 1.01
[297] D-1312, page ES1
[298] D-1347, page 1
[299] D-1295, page 1

> Investments in mortgages, secured debentures and advances. Castor's loan loss provisions were reasonable, and additional losses were not probable and estimable.
>
> The Plaintiffs' Experts would have one believe that Castor's Investments in mortgages, secured debentures and advances to the YH Group and DT Smith Group were overstated by hundreds of millions of dollars as at December 31, 1990 and by very significant amounts in the years preceding as well. I am of the opinion that the Plaintiffs' Experts' conclusions regarding the valuation of Castor's investments in mortgages, secured debentures and advances for the years ended December 31, 1988, 1989 and 1990 are not in accordance with GAAP.[300] (our emphasis)

Levi

[320] Levi's overall opinion and conclusion reads as follows:

> The ultimate determination of fraud is a decision for the trier of fact. Nevertheless, I am of the opinion that the schemes and activities carried out by Wolfgang Stolzenberg and his co-conspirators are fraudulent in nature and resulted in the deception, concealment and trickery which **prevented the DEFENDANTS from detecting the true nature of <u>some of</u> the transactions** they were auditing.
>
> On the basis of the evidence which I have examined, it is my opinion that the fraudulent activities summarized below and the careful and detailed concealment, deceit and misrepresentation perpetrated by Wolfgang Stolzenberg and his coconspirators was instrumental in preventing the auditor, when applying Generally Accepted Auditing Standards, from detecting any irregularities or improper representations in the audited financial statements of Castor Holdings Ltd.[301] (our emphasis)

<u>General observations on available experts' opinions</u>

[321] Plaintiff's experts were assigned similar mandates, and each brought a unique perspective and experience to his assessment of the fundamental questions that the Court must answer in this auditors' negligence case.

[322] Plaintiff's experts, with distinctly different background and experience, all independently arrived at the same conclusion that the audited financial statements of Castor for 1988, 1989 and 1990 contained material misstatements that should have been identified and would have been identified by C&L but for their negligent audit work.

[323] Defendants' experts were assigned different mandates, exclusive of each other.

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[300] D-1312, page ES-35
[301] D-1347, page 245

[324] Defendants' expert witnesses advanced a number of theories contradictory at first glance, if not mutually exclusive. For example:

- Levi and Selman opined that the failure of C&L to detect the "true nature" of the transactions they were auditing resulted, in the words of Levi, from the fact that: «*Wolfgang Stolzenberg managed to organize a group of co-conspirators to participate in an elaborate, complex and massive fraud*»[302]. Goodman opined that Castor was a legitimate business model and that the carrying values of the YH and DT Smith loans were not misstated on the audited consolidated financial statements of Castor during the relevant years (although he ultimately conceded a small loss exposure for 1990)[303].

- Selman and Levi opined that various loans were fraudulent[304] while Goodman opined that these same loans were made for a valid business purpose and were not misstated on the audited consolidated financial statements[305].

- Selman and Levi opined that cash circles at year-end which involved transfers to and from a law firm were a fraud[306] while Goodman opined that these same transactions were a positive and legitimate business practice and mechanism being utilized by Castor[307].

- Selman and Levi opined that Castor used backdated documents to deceive the auditors and to demonstrate the existence of transactions at times when they did not occur[308] while Goodman opined that back-dating documents could be a normal part of Castor's business raising no problems of GAAP[309].

General observations on expert evidence

[325] The Court cannot express the duties and responsibilities of an expert witness better than Justice Cresswell did in *National Justice Compania Naviera S.A. v. Prudential* [310]:

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[302] D-1347. P.2. para.1.2
[303] D-1312-6
[304] For example – the 40 million$ loans (called the "nasty nine") made at the end of 1990: Selman – D-1295, p.366 and Selman, May 25, 2009, pp. 211 to 215; Levi – D-1347, p.85 and January 28, 2010, pp. 38-39, 46-47
[305] For example - the 40 million$ loans (called the "nasty nine") made at the end of 1990: Goodman, September 22, 2009, pp. 97-98; October 9, 2009, pp. 113, 156, 160 to 171, 189-190;October 26, 2009 pp. 271-272
[306] Levi, January 28, 2010, pp.241-243; Selman, May 7, 2009, pp.42-46
[307] Goodman, October 26, 2009, p.257:October 27, 2009, pp.105-107; November 24, 2009, pp.244-247
[308] D-1347, pp. 2, 87, 99-103, 147, 150, 152, 159, 207, 214, 246; Selman, May 7, 2009, p. 53; Selman, May 26, 2009, pp. 65-66.
[309] Goodman, October 27, 2009, pp. 29-32.
[310] [l993] 2 Lloyd's Rep. 68

1. Expert evidence presented to the Court should be and should be seen to be independent product of the expert uninfluenced as to form or content by the exigencies of the litigation (...)

2. An expert witness should provide independent assistance to the Court by way of objective unbiased opinion in relation to matters within his expertise ... An expert witness (...) should never assume the role of advocate.

3. An expert witness should state the facts or assumptions on which his opinion is based. He should not omit to consider material facts which detract from his concluded opinion (...)

4. An expert witness should make it clear when a particular question or issue falls outside his expertise.

5. If an expert's opinion is not properly researched because he considers that insufficient data is available then this must be stated with an indication that the opinion is no more than a provisional one (...)

6. If after exchange of reports, an expert witness changes his views on a material matter (...) such change of view should be communicated (...) to the other side without delay and when appropriate to the Court.

7. Where expert evidence refers to photographs, plans, calculations, survey reports or other similar documents they must be provided to the opposite party at the same time as the exchange of the reports.

Credibility and reliability of expert evidence

Legal principles and tools to assess credibility and reliability

[326] *"Before any weight can be given to an expert's opinion, the facts upon which the opinion is based must be found to exist"*[311].

[327] *"As long as there is some admissible evidence on which the expert's testimony is based it cannot be ignored; but it follows that the more an expert relies on facts not in evidence, the weight given to his opinion will diminish"*[312].

[328] An opinion based on facts not in evidence has no value for the Court. [313]

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[311] *R. v. Abbey*, [1982] 2 S.C.R. 24 at p. 46; AZ-82111071; J.E. 82-762; *R. v. Warsing*, [1998] 3 S.C.R. 579 at para. 54; AZ-99111001; J.E. 99-107.

[312] *R. v. Warsing*, [1998] 3 S.C.R. 579 at para. 54 ; AZ-99111001; J.E. 99-107

[329] With respect to its probative value, the testimony of an expert is considered in the same manner as the testimony of an ordinary witness[314]. The Court is not bound by the expert witness's opinion. [315]

[330] An expert witness's objectivity and the credibility of his opinions may be called into question, namely, where he or she :

- accepts to perform his or her mandate in a restricted manner[316];
- presents a product influenced as to form or content by the exigencies of litigation[317];
- shows a lack of independence or a bias[318];
- has an interest in the outcome of the litigation, either because of a relationship with the party that retained his or her services or otherwise[319];
- advocates the position of the party that retained his or her services[320]; or

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313 *RCMP v. Tahmourpour*, [2009] FC 1009 (CanLII), paras, 61-67; *Paillé v. Lorcon Inc.* [1985] AZ-85011264 (QC CA); J.E. 85-841.

314 *P.L. c. Benchetrit* [2010] QCCA 1505, para.25 to 31; AZ-50666756; J.E. 2010-1600; *Shawinigan Engineering Co. c. Naud*, [1929] R.C.S. 341 at 343; *Lapointe c. Hôpital Le Gardeur*, [1992] 1 R.C.S. 351 at 358; AZ-92111029; J.E. 92-302.

315 Royer, Jean-Claude, *La preuve civile*, 4 éd. Cowansville, (Qc), Yvon Blais, 2008, at §120, 484; *Droit de la famille – 103252*, [2010] QCCA 2173; AZ-50695343; *P.L. c. Benchetrit* [2010] QCCA 1505, para.25 to 31; AZ-50666756; J.E. 2010-1600; *L.F. c. A.D.*, AZ-50342156 at paras. 76, 81, 83, J.E. 2006-9, [2006] R.D.F. 175 (rés.).

316 *Club de voyages Aventures (Groupe) inc. c. Club de voyages Aventure inc.*, REJB 1999-13211 at paras. 31, 56-58, 82, AZ-99021695 (S.C.); *Tremblay c. Perrone (Succession de)*, [2006] QCCS 3073 at paras. 69-71, AZ-50376939; J.E. 2006-1624 appeal dismissed, [2007] QCCA 1604; *Danny's Construction Company Inc. c. Birdair inc.*, EYB 2010-169584 at paras. 381, 392, 396-398, 404-405, 412-413, 416-417, 453 (S.C.); *Tourbières Premier ltée c. Société coopérative agricole régionale de Rivière-du-Loup*, REJB 2001-23507 at paras. 30-35, 50 (C.A.); J.E. 99-1435 (S.C.), appeal abandoned, (C.A., 1999-11-25), 500-09-008380-990.

317 *National Justice Compania Naviera S.A. v. Prudential* [l993] 2 Lloyd's Rep. 68

318 *National Justice Compania Naviera S.A. v. Prudential* [l993] 2 Lloyd's Rep. 68

319 *Club de voyages Aventures (Groupe) inc. c. Club de voyages Aventure inc.*, REJB 1999-13211 at paras. 31, 56-58, 82, AZ-99021695 (S.C.); *Orenstein-Little c. Héneault & Gosselin inc.*, [2008] QCCS 3730 at paras. 73-76, AZ-50509716, J.E. 2008-1713; *Perron c. Audet*, AZ-50113443 at paras. 217, 230-242 (S.C.); *Audet c. Landry*, [2009] QCCS 3312 at paras. 82-83, 93, 98, AZ-50566973, J.E. 2009-1472, [2009] R.R.A. 796, inscription in appeal, 200-09-006776-097.

320 *Perron c. Audet*, AZ-50113443 at paras. 201, 239-242 (S.C.); *Fortin c. Compagnie d'assurances Wellington*, AZ-00026200 at 12-15 (S.C.), B.E. 2000BE-416, appeal dismissed, AZ-50522725, leave to appeal to S.C.C. refused, 28149, revision of decision refusing leave to appeal to S.C.C. dismissed, 28149; *Compagnie d'assurances St-Paul/St-Paul Fire & Marine Insurance Company c. SNC-Lavalin inc.*, [2009] QCCS 56 at paras. 68-77, AZ-50530600, J.E. 2009-255, inscription in appeal, 500-09-019384-098; *Convergia Networks inc. v. Bell Canada*, REJB 2003-41397 at para. 168-169 (S.C.); *Danny's Construction Company Inc. c. Birdair inc.*, EYB 2010-169584 at paras. 381, 396, 433-435, 449-450 (S.C.).

- selectively examines only the evidence that supports his or her conclusions or accepts to examine only the evidence provided by the party that retained his or her services[321].

Assessment of credibility and reliability

Plaintiff's experts

General comments

[331] None of the Plaintiff's experts has embarked into the project or the task of redoing the 1988, 1989 and 1990 audits of Castor: it was neither possible nor called for.

[332] Plaintiff's experts have provided opinions on the actual work performed by C&L, using as starting points actual figures and information C&L was provided with, as it appears from C&L's working papers[322] and C&L's employees' examinations by the Trustee in bankruptcy.

Vance

[333] Even though he has never audited a client like Castor, a factor which is not decisive since Castor was quite a unique organisation, Vance has knowledge and experience that is directly applicable to this litigation.

- During the most relevant years, 1988 to 1991, he served on the CICA auditing standards committee, which was charged with determining GAAS and updating the Handbook[323].

- His clients have included secured and unsecured lenders and real estate developers, such that he has experience applying standards at issue in the present case, and he has carried out reviews of large credit union files, such that he is well placed to compare them to Castor[324].

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[321] *Audet c. Landry*, [2009] QCCS 3312 at paras. 61-68, AZ-50566973, J.E. 2009-1472, [2009] R.R.A. 796, inscription in appeal, 200-09-006776-097; *X Merchant inc. c. Ginsberg, Gingras & Associés inc.*, EYB 2009-158718 at paras. 199-209 (S.C.); *Boiler Inspection and Insurance Co. of Canada c. Manac inc./Nortex*, AZ-50194738 at paras. 176-193, J.E. 2003-2156, [2003] R.R.A. 1415 (rés.), Principal grounds of appeal dismissed and incidental appeal allowed with partial dissent, [2006] QCCA 1395, Principal appeal allowed and incidental appeal dismissed, [2006] QCCA 1398; *Perron c. Audet*, AZ-50113443 at para. 99 (S.C.).

[322] Exhibits PW-1053 (PW-1053-1 to PW-1053-121)

[323] Vance, March 4, 2008, p. 28.

[324] Vance, March 4, 2008, pp. 30-32.

[334] Vance made changes to his loan loss provisions as they appeared in his first report for the first trial, and these were incorporated in his second report, for the second trial. The fact that he made changes is not decisive: all experts have made changes and experts are expected to communicate any change of views. The issue is not whether experts have changed their views, but why they have (or have not) done so, and whether they volunteered the change or waited until they were challenged in cross-examination.

[335] On one hand, Vance was cross-examined in the first trial and debriefed by counsel prior to testifying in the second trial[325]. On the other hand, counsel for the Defendants had unprecedented tools to conduct their cross-examination in the second trial, namely thousands of pages of prior testimony of Vance.

[336] In his report and in his testimony, Vance stated the facts and assumptions on which his opinions were based and more often than not those facts and assumptions are found to exist or to be right, as later discussed in the present judgment.

[337] Vance's mandate does not raise an issue of restrictions or limitations.

[338] Vance has advocated the position of the claimants sometimes. To various extents many of the expert witnesses who appeared before the Court did advocate the position of the party that retained their services. Although Vance did, the Court concludes that it was done out of conviction and not out of a lack of independence or a bias. Besides, there is no evidence to suggest that Vance has an interest in the outcome of the litigation that could impair his objectivity.

[339] In a few occurrences in cross-examination, if he had to qualify a previous remark or acknowledge a mistake, Vance reluctantly did so. Although not leading to a negative assessment on credibility and reliability, such an attitude attracted the Court's attention. It is a factor taken into account when time come to assess opinions on specific topics.

Froese

[340] Froese has knowledge and experience that is directly applicable to this litigation.

- In 1985, Froese joined the firm Doane Raymond in the professional standards department, researching and providing advice on Canadian GAAP and GAAS.
- From 1985 to 1988, he converted his firm's audit approach to a risk-based approach.
- During the relevant years, Froese devoted more than half of his professional practice to the audit of Central Capital, first as audit manager and then as senior audit manager. He testified that Central Capital had a merchant financing

[325] Vance, April 17, 2008, pp.143-144

department with loans to both real estate developers and to operating businesses and its portfolio was, in a number of ways, comparable to Castor.

- Froese was involved in the planning of the audits, supervising the audit team and reviewing the loan files and the financial statements.
- Froese requested appraisals for collateral in the form of real estate when he, as auditor, determined that the existing appraisal was stale-dated, and he conducted site visits to the properties, such as Chino Hills in California.

- His experience as an auditor and in professional standards is exceptionally relevant in assessing the adequacy of the work performed by C&L, including on the issue of the review of appraisals by auditors.
- In 1991, Froese was named partner of Doane Raymond and it was at this time, after the relevant years for the present litigation, that Froese's practice became primarily focused on forensic accounting.

[341] Froese's mandate does not raise an issue of restrictions or limitations.

[342] Froese has not advocated a position. Straightforward, he gave his candid opinion on the issues he looked at.

[343] In cross-examination, if he felt he had to do so, Froese neither hesitated to acknowledge a mistake or to qualify a previous remark.

[344] In his report and in his testimony, Froese stated the facts and assumptions on which his opinions were based and more often than not those facts and assumptions are found to exist or to be right, as later discussed in the present judgment.

[345] Because Froese did not bring forward admissions he would have made during cross-examination to a corrected report he provided during his testimony, Defendants argue it impeaches his credibility. The Court does not share this view: the purpose of the corrected report was specific, there was not enough time to ask for more and Froese's testimony was already part of the Court record.

Rosen

[346] Rosen has knowledge and experience that is directly applicable to this litigation.

- Since 1972, Rosen has taught and continues to teach accounting, auditing and the integration of a professional accounting program at York University.

- His opinion is sought frequently by audit firms and by audit committees on the types of issues that would be considered by an engagement partner, and on the preparation of financial statements in accordance with GAAP[326].

- Over the years, he has been hired by accounting firms, namely the "big 4", to teach and lecture their students on GAAP and GAAS issues[327].

- However, Rosen's experience is limited since he has never signed an audit opinion and he has never prepared financial statements for a company that has activities similar to Castor.

[347] During his cross-examination, Rosen was challenged as to the kind of opinion he was providing the Court with. Rosen affirmed that he was providing the Court with his professional opinion as to what the generally accepted standards of the profession were during the relevant time and not with his personal views as an educator.

[348] Defendants argue that Rosen is using the present case as a platform or illustration to vindicate the view that he's taken publicly for over 20 years. Because he is an advocate for change, they suggest that he does not have the required neutrality and objectivity.

[349] Defendants further argue that the Court should give no credibility to Rosen's opinions, namely and not restrictively because:

- Rosen would have admitted changing his stated views to suit his audience, including having written something in an expert's report that he did not believe because it was easier than quarrelling with the lawyers[328];

- Rosen did not volunteer known errors in his report even though he knew about the read-in rule applied by the Court ;

- Rosen gave an opinion about the share valuation letters, despite having tried to pass the exam for his Chartered Business Valuator designation ("**CBV**") 4 times, and failed[329];

- Rosen has referred to Castor or this litigation in public articles[330];

- Rosen did not provide contrary views even when he was aware they existed, knowing however he should do so since it is part of his writings about what an expert should do[331];

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[326] PW-3030; Rosen, January 28, 2009, pp. 195–203; January 29, 2009, pp. 32–35.
[327] Rosen, January 29, 2009, pp. 104-106
[328] Rosen, January 29, 2009, pp. 58-59; Rosen April 6, 2009, pp. 110-114
[329] Rosen, January 29, 2009 p. 111-120
[330] D-1107, D-1108, D-1097, D-1109, D-1098

- Rosen is of the view that C&L is behind the problems with GAAP as he perceives them[332] ; and

- Rosen has business interest in a corporation which offers advice to end-users of financial statements; he is therefore in a fundamental situation of conflict of interest.

[350] Rosen has unequivocally taken a very public position on the standards he is being called upon to provide his expert opinion. He's a vociferous critic of those norms, of those standards. He has called those standards *loose*[333], *pathetic*[334] *and full of contradictions and feeble definitions*[335]. He has also referred to Castor or to this litigation in public articles. These are factors taken into account when the time comes to assess specific opinions.

[351] Adapting writings or presentations to the sophistication of a particular audience and the nature of its interest in a topic, that is not at all surprising and that is not the point. The crux of the matter is whether it entails distortion or misrepresentation.

[352] Rosen tried four times to pass the CBV exam and failed: those are facts that he admitted without hesitation when questioned in cross-examination. However, in all fairness to Rosen, relying on appearances is not acceptable in light of the circumstances described by Rosen which have not been contradicted.

> Right. And you wrote by name and I regret this has to come up, but it was very political. I was the architect of the CAs case exam, I was asked to introduce it into the CBVs, it got into a political fiasco and there were two (2) camps, a group that supported me, a group that didn't support me. And the outcome was I never got the CBV and I gave up[336].
>
> Two (2) were challenge exams, two (2) were written, but I had passed all of the exams of the University of Toronto in preparation for the CBV[337].
>
> I was failed by them four (4) times, but it was very political. You're not being fair. People who were marking my exams were people who had failed the CA exams or had considerable trouble in my courses, so when you write by name and you have those problems, like I've passed everything else in my life, it seems a little odd that I somehow could not pass this particular technician-type CBV[338].

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[331] Rosen, February 17, 2009 p. 36-57; Rosen, February 20, 2009 p. 248-249
[332] Rosen, January 29, 2009 p. 104-109; D-1106
[333] Rosen, January. 29, 2009 p.36-37; D-1097 and D-1098
[334] Rosen, January. 29, 2009 p. 48-51; D-1100
[335] Rosen, January. 29, 2009 p. 38-42; D-1099
[336] Rosen, January 29, 2009, p.119
[337] Rosen, January 29, 2009, p.119
[338] Rosen, January 29, 2009, p.120

[353] Not providing contrary views when one is aware they exist is detrimental to one's credibility. However, given the need to look at things in a context, the following few extracts of Rosen's testimony put things in perspective.

Extract # 1

Q. You understand that, in your role as an independent expert of the Court, your views and opinions are to be expressed in a neutral and objective manner?

A. I understand that, I think this is an unusual case in the sense that it didn't take very long looking at the documents to realize there was a very serious problem here.

So I think you'll find in the reports there are just many, many situations where the benefit of the doubt was given to Coopers & Lybrand, but by the same token the dollar is so huge and the evidence to me was so overwhelming that it may be difficult to detect.

Like there are times where I just couldn't possibly think of any support for what Coopers & Lybrand was saying, especially in the working papers[339].

Extract # 2

Q. (...) is it fair for the Court to understand, Mr. Rosen, that if, in fact, you've rejected evidence because you concluded it was not credible from your perspective as an accountant, you have and should advise the Court of that?

A. I think that's just about impossibility, especially in this case, so that if it appears that there are two sides on an issue, clearly you would bring that out. If there's a situation where there are just overwhelming facts and (inaudible), and you're saying to yourself, yes, there could be two or three tiny things, I tend to just let them go because I can't see how that's going to affect the calibre of the financial statements and the quality of reporting in fairness.

So there's just... this is not a single or double issue case, this is a multiple, multiple issues. So I think what you're asking is, I agree with in theory, but in practicality, it's almost impossible to achieve. You would have volumes and volumes and volumes in a report[340].

[354] Rosen believes that there should be independence in the standards. He wrote "*The solution to this problem is to have a total independent body*" and *"The problem again comes back to the self-regulation of auditing firms in Canada*". Concluding from this, as the Defendants are suggesting that "*Rosen is of the view that C&L is behind the problems with GAAP as he perceives them"* and that he has a grudge against C&L that should negatively impact the assessment of his credibility is a step not to be taken.

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[339] Rosen, February17, 2009, p.36-37
[340] Rosen, February 17, 2009, pp.41-42

[355] Before cross-examination started, and as he admitted under cross-examination on February 19, 2009, Rosen was aware of errors or corrections to be made to his 1997 reports, volume 1 and volume 2, but errors and needed corrections were not brought to the Court's specific attention[341]. Rosen explained they were not significant and had no impact on his overall conclusions.

> No, I'm saying the overall part is, because the numbers are so huge, that it doesn't affect my conclusions on GAAP, GAAS and free of material misstatements[342].
>
> We're talking about huge huge numbers here on the losses (...), so that the listing of all of the mistakes, if you want to call it, that I made or misinterpretations that I made are still very small[343].
>
> (...) so that there are just many many situations where I always gave the benefit of the doubt to Coopers & Lybrand and so now, I find I made the inevitable mistakes here and there, but they don't change my overall conclusions[344].

[356] Immediately, on February 19, 2009, concern was expressed given the read-in rule and measures were taken to address such concern[345].

[357] The day after, on February 20, 2009, before cross-examination resumed, Rosen produced two documents, PW-3033-1 and PW-3033-2, and gave further details[346].

[358] Disclosure of corrections or errors to an expert's report is expected at the earliest opportunity. Absence of disclosure or delay to disclose is a factor taken into account when time comes to assess opinions on specific topics. However, and while disclosure did only happen further to questions put to Rosen in cross-examination and further to the Court's intervention, the measures taken on February 19, 2009 are satisfactory given the limited significance of such errors and corrections and the unique circumstances of the present file.

[359] Rosen has business interest in a corporation which offers advice to end-users of financial statements. The outcome of the present file is of interest to him but not to the extent of a conflict of interest. Such interest is a factor taken into account when time comes to assess opinions on specific topics.

[360] In his report and in his testimony, Rosen stated the facts and assumptions on which his opinions were based and more often than not those facts and assumptions are found to exist or to be right, as later discussed in the present judgment.

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[341] Rosen, February 19, 2009, pp. 239-267
[342] Rosen, February 19, 2009, p.239
[343] Rosen, February 19, 2009, p.241
[344] Rosen, February 19, 2009, p. 244
[345] Rosen, February 19, 2009, pp.251 to 268
[346] Rosen, February 19, 2009, pp. 51 to 65

Defendants' experts

General comments

[361] The present case is an auditor's negligence case. The inter-relationship between the concepts of GAAS and GAAP is essential to the audit process.

[362] None of the Defendants' experts has provided an opinion about the inter-relationship of GAAS and GAAP, despite being chartered accountants with audit experience.

[363] Defendants' experts have performed restricted mandates that do limit rather than complete the understanding of the fundamental issues of the case. The concepts of GAAS and GAAP have been severed so that none proffer an opinion on the fundamental question in this case: did C&L conduct its 1988, 1989 and 1990 audits in accordance with GAAS and, if not, what were the consequences of such failure?

[364] None of Defendants' experts has opined on the actual C&L's audit of the loans and the loan loss provisions, a fact that surprised Levi[347], and their various opinions cannot be assembled and taken as a whole.

Selman

[365] Selman's mandate was narrowly circumscribed to exclude:

- whether Castor's audited consolidated financial statements were materially misleading or, as a whole, present fairly the financial position of Castor in accordance with GAAP;
- whether C&L conducted its audits of Castor in accordance with GAAS;
- whether C&L conducted its audit of loans in accordance with GAAP and GAAS;
- whether C&L followed proper procedures in respect of planning, supervision and review; and
- whether the staff that did the audit work on the investment section in Montreal was sufficiently experienced to undertake those procedures[348].

[366] Selman's methodology did not require that he bring to the attention of this Court the information that C&L should have requested from Castor.

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[347] Levi, February 1, 2010, pp. 32–40.

[348] Selman, May 4, 2009, pp. 125, 165-168, 186-188; May 5, 2009, pp. 40, 41; May 25, 2009, pp. 141, 199, 226-227; May 26, 2009, pp. 22-23; June 1, 2009, pp. 96-97, 106, 109, 134.

[367] When he was confronted with the fact that he had given many opinions in his report (on numerous pages) as to information that Castor should have provided to Coopers & Lybrand and when he was asked why he did not indicate to the Court, firstly, what information Coopers & Lybrand should have requested from the audit client, Selman answered: "*I was dealing with the issue from a different point of view*"[349].

[368] Unlike Goodman and Levi, Selman has limited experience as an auditor.

[369] His experience auditing businesses similar to that of Castor was limited to a single client, the Bank of British Columbia, and it ended in 1981, well before the years relevant to the case at bar[350].

[370] It is noteworthy that Selman is the expert mandated to opine at all on GAAS given his limited experience in the field, and not one of the experts with relevant experience as a practitioner during the period between 1987 and 1991(Goodman or Levi).

[371] In preparing his report, Selman did not consider the evidence of the C&L audit staff members relating to the work they performed on the investment section[351], nor the differences in the way the audit was conducted in Europe as opposed to the way it was conducted in Montreal[352].

[372] With Selman's opinion, the Court has a sketchy picture of the situation. As Selman himself pointed out, because his work was limited to certain aspects, he was "*not in a position to deal with the question of whether or not the financial statements have been presented appropriately, and the Court will have to take my testimony, and later witnesses' testimony and sew it together to get to that conclusion, and that's just the fact of the matter*"[353].

[373] This methodology limited his analysis of the errors made by C&L while it enabled him to gather evidence to support C&L's defense of "fraud against the auditors".

[374] In various instances, the Court observed reluctance to answer simple and clear questions in a precise factual context that were put to him by Counsel or by the Court. From such behaviour, and on some of those specific topics, the Court draws adverse inferences. As an example, the Court refers to the exchange that took place on May, 21, 2009 during Selman's examination in chief (on the topic of the 1988 maturity changes) when she asked such a question and never got a direct answer[354].

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[349] Selman, May 26, 2009, p. 59
[350] Selman, May 4, 2009, pp. 114, 198-199.
[351] Selman, June 4, 2009, pp. 51-52.
[352] Selman, May 26, 2009, p. 103-104.
[353] Selman, June 1, 2009, p. 95.
[354] Selman, May 21, 2009, pp.31 -43

[375] Acting more like a critic of the Plaintiff experts' reports and testimonies than as an analyst of C&L's work, Selman talked mainly about principles, or only about principles, rather than the application of same.

Goodman

[376] Goodman has knowledge and experience that is directly applicable to this litigation.

[377] Clearly, Goodman has substantial relevant audit experience[355].

- Goodman spent over 20 years of his professional career performing audits of large companies involved in real estate investment and development, namely with a real estate client whose business was very similar to that of Castor;
- Goodman joined Price Waterhouse's Montreal office as a member of its audit department in 1977, and the focus of his work over the next few years was the audits of privately-owned commercial and real estate development companies, holding companies and investment holding companies;
- Goodman participated in the audit of a chartered bank (RBC) and was responsible for the analysis of the loans and the loan loss provisions;
- Goodman continued to pursue his career in audits in the 1980s by working, inter alia, on the audits of Alcan, both in Canada and in Europe;
- Goodman was appointed as an audit partner of Price Waterhouse in 1987 and focused his practice on developing a real estate audit and an advisory practice;
- In 1988, Goodman became the lead audit partner for a number of real estate companies;
- From 1987 to 1997, Goodman served on the Audit Committee of the Société d'habitation et de développement de Montréal, which held over $400 million in residential real estate;
- Goodman was the audit partner for the audit of Standard Life in respect of the mortgage loan portfolio and the real estate holdings as late as 1995;
- Goodman lectured at McGill University for the Chartered Accountants' programme, providing "the most advanced auditing course that's offered in the McGill chartered accountancy program" for which he "led the restructuring, the

[355] D-1310 and Goodman, September 3, 2009, pp. 20-23, 28, 34-36, 53-55, 82, 108-110, 221-222

preparation, the material, the preparation of the exams, the correction of the exams;

- Goodman became the second partner on the Castor mandate in March 1996, and took over the lead on the file for Price Waterhouse in mid 1997.

[378] Goodman's report was written from the point of view of a "*hypothetical honest preparer of Castor's financial statements with access to all of the available information that WOST (*Stolzenberg*) permitted this individual to have as at the audit report date of each the years*"[356].

[379] Four inescapable remarks stem from the above:

- Goodman's exercise was performed from the point of view of a person that never existed at Castor[357]

- Goodman's exercise was performed from the point of view of the audited client;

- Goodman's exercise is reliant on his understanding (or his belief) of accessible available information – access being under the direct constraint of Stolzenberg;

- Goodman's exercise was not performed from the point of view of an auditor who has to apply GAAS to figures he is provided with and who interact with numerous sources of information.

[380] Goodman's mandate excluded any GAAP disclosure issues, any evidence as to the disclosure of related party transactions, disclosure of economic dependence and maturities in the Notes, disclosure of capitalized interest, any issues of fraud, any issues of overall financial statement presentation and any issues of GAAS[358].

[381] When asked why he restricted his opinion to a non-auditor GAAP perspective, Goodman's response was that he was not comfortable in dealing with audit matters, and he repeatedly asserted that he was uncomfortable opining on GAAS[359]. A surprising and unreliable answer in the circumstances.

[382] Goodman's interest in the present litigation, ensuing from his relationship with Defendants, puts into question his ability to be objective and unbiased.

- Goodman assumed primary responsibility for Castor's mandate in mid 1997[360];

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[356] D-1312, p.ES-1
[357] Goodman, October 9, 2009, pp. 134-135.
[358] Goodman, September 15, 2009, p. 130; October 9, 2009, pp. 83-84, 120, 133, 157; September 4, 2009, pp.10-13.
[359] Goodman, September 4, 2009, pp. 5-6; Goodman, October 9, 2009, pp. 83-84.
[360] Goodman, September 3, 2009, pp.54-55

- At that time, Goodman was a managing partner of Price Waterhouse[361];

- Goodman testified that he gave his initial opinion verbally to Heenan Blaikie (that no loan loss provisions were necessary as at December 31, 1990 for the 5 projects he reviewed), together with a written analysis on or about September 30, 1997 during a meeting at the offices of Defendants' counsel[362]. There is no documentary evidence to support this testimony as Goodman's invoices for this period do not indicate any preparation of a preliminary opinion or any meetings with counsel;[363]

- Goodman asserted, in response to a question from Defendants' counsel, that this initial opinion was communicated months prior to when he became aware of the possibility of the merger of Price Waterhouse and C&L which was «sometime in January 1998»;[364]

- Goodman was adamant that he only learned of the possible merger in January 1998;

  Q- And is it possible that you're confusing the timing and that in fact, this advice to you was given in Septem ber of nineteen ninety-seven (1997)?

  A- Oh, it's absolutely inconceivable[365]».

- As a managing partner and member of the national management committee of Price Waterhouse Canada, Goodman was alerted to the possibility of the merger before the public announcement[366];

- Contrary to Goodman's testimony, the possibility of the merger was announced throughout the media on or by September 18, 1997[367];

- Clearly, Goodman was aware of the possible merger within 2 months of becoming the lead partner in the Castor file and before the date that he asserted providing his preliminary opinion to Defendants' counsel.

[383] Confronted with the evidence as to when the public announcement was made of the possible merger of Price Waterhouse and C&L, Goodman altered his testimony and stated that his opinion was provided to Defendants' counsel prior to the announcement

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[361] Goodman, September 3, 2009, pp.44 and followings
[362] Goodman, September 3, 2009, pp.111-113
[363] D-1314
[364] Goodman, September 3, 2009, p.127
[365] Goodman, September 3, 2009, p.143
[366] Goodman, September 3, 2009, pp.149-150
[367] Goodman, September 3, 2009, pp.143-152; PW-3065

of the merger (i.e., early in September 1997)[368]. The Court does not find this testimony reliable.

[384] After the public announcement, Goodman and PriceWaterhouse agreed to examine additional loans and to opine on other issues, including Castor's status as a going concern and the share valuation letters[369].

[385] Assuming a certain responsibility to pursue a mandate that had started before merger discussions took place, why did Goodman and Price Waterhouse agree to an expansion of their mandate after the public announcement was made in mid September 1997 of the potential merger?

[386] Goodman asserted to the Court that he had no qualms about fulfilling his mandate because of the high degree of scepticism he had that the merger would proceed[370]. However, his initial report was dated May 29, 1998 (filed into the Court record but not produced), 9 days after the European Commission granted the approval of the merger on May 20, 1998[371], such an approval being considered by the firms themselves to be the last major obstacle to the merger of Price Waterhouse and C&L.

[387] The merger was effective as of July 1, 1998.

[388] The last question put to Goodman by Defendants' counsel during the "voir-dire" was whether, as a partner in PriceWaterhouse Coopers, he had any financial interest in the outcome of this litigation, to which Goodman replied: «*To the best of my knowledge, I have absolutely none.* »

[389] When challenged on this testimony, Goodman suggested to the Court that there are 5,000 partners in the Canadian firm, and the international firm is much larger, so even if 100 of his partners were found liable, he doesn't think that this would have a major impact on PriceWaterhouse Coopers. Moreover, in Goodman's opinion, there is a firm culture whereby everyone would chip in if a significant number of partners were in trouble[372].

[390] Goodman admitted that, as managing partner, he was served with the proceedings taken by the Trustee in Bankruptcy for Castor against Pricewaterhouse Coopers relating to the assets that PriceWaterhouse Coopers acquired from C&L and seeking an order of the Court that in the event that the plaintiffs prevail in their actions, that they could look to those assets for recovery[373].

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[368] Goodman, September 3, 2009, pp. 149-150.
[369] Goodman, September 3, 2009, pp. 112–117; D-1312, p. 1.
[370] Goodman, September 3, 2009, pp. 127–128.
[371] PW-3068; PW-3069.
[372] Goodman, September 3, 2009, pp. 192–193, 200-201.
[373] PW-3071

[391] It is not believable that Goodman would assume that he has and had no economic interest in the outcome of the present litigation either directly as a partner of PriceWaterhouse Coopers or indirectly because of the potential liability of a number of his partners.

[392] In assessing the carrying value of the loans and the requirement for loan loss provisions, he did not consider whether the borrowers were related to Castor[374], and he did not look for or consider the existence of fraud[375].

[393] He admitted that he intentionally disregarded evidence that would have allowed him to opine on C&L's analysis of audit evidence and their conclusions as to GAAP or GAAS[376]. In a case dealing with alleged auditor's negligence, it is revealing that Goodman deliberately avoided examining evidence as to whether C&L had obtained sufficient information to address adjustments to Castor's financial statements[377].

[394] Confronted at trial with a C&L statement appearing in the AWPs, and reproduced as a value indicator in his report, Goodman refused to acknowledge that it indicated what C&L knew at the time[378].

[395] Goodman was also inconsistent in his methodology, insisting that documents (that do not support his view) are less relevant because they are unsigned[379], but stating that this Court should still give weight to unsigned documents cited by him in support of his own views[380].

[396] Goodman's opinions are predicated on his determination of the credibility of witnesses,[381] a situation he acknowledged: "*The opinion I'm giving is based upon the facts that I saw, My Lady, and my assessment of the facts*"[382]. If this Court does not share Goodman's views on the credibility of witnesses, his opinion could become moot for that reason alone.

Levi

[397] Levi has knowledge and experience that is directly applicable to this litigation.

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[374] Goodman, October 9, 2009, pp. 116-128.
[375] Goodman, October 9, 2009, p. 157
[376] Goodman, November 23, 2009, pp. 24-25.
[377] Goodman, November 23, 2009, pp. 26-27.
[378] Goodman, November 24, 2009, pp. 168-169. See also D-1312, p. 496.
[379] See, for example, the appraisal PW-1108B.
[380] Goodman, November 3, 2009, pp. 25-26.
[381] See for example : Goodman, October 9, 2009, pp. 213-217.
[382] Goodman, October 9, 2009, p 159

- Levi obtained his CA designation in 1971 and, as mentioned in his curriculum vitae, he has "*extensive expertise and experience over the past 39 years in GAAS and GAAP in Canada*"[383].

- During the years 1975 to 2004, Levi was the senior partner responsible for his firm's standards and quality control with the mandate "*to review and establish procedures, forms and staff training.*"

[398] Although he clearly had relevant experience and knowledge on the issues of GAAP and GAAS, Levi's mandate excluded whether there was a failure of GAAS, including whether C&L obtained sufficient appropriate audit evidence ("**SAAE**"), any issues related to GAAP and loan loss provisions, including whether the loans were in default or whether there was a valuation issue[384].

[399] As Levi explains, somebody made a determination, before he got involved, that Defendants had to partition the work between experts given the magnitude of the case, the magnitude of documentation and the magnitude of issues[385].

[400] Levi's mandate was restricted to identifying areas of fraud that he could detect and to analyze which of those would or could have impacted on the auditors' ability to do their audit in accordance with GAAS[386].

[401] Partition is not a prerogative of the Court: all pieces have to be linked together[387].

[402] Usefulness of Levi's opinion is thus limited since:

- It is focused on fraud detection;

- It does not address GAAP and GAAS compliance by the auditors;

- It is entirely dependent on Levi's reading of certain facts and certain facts only.

[403] On page 2 of his report, at item 8 of his summary of conclusion and opinion, Levi writes "*Considering the extent of the fraud, the elaborate and widespread management collusion, the outside collusion and the intentional deception and misrepresentations made by Wolfgang Stolzenberg and his co-conspirators to the auditors, it is my opinion that it was not possible for Coopers & Lybrand to have detected the fraud during the performance of their year-end audits in accordance with Generally Accepted Auditing*

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[383] D-1346
[384] Levi, January 11, 2010, pp. 63-64, 76-77, 134, 164-166; January 27, 2010, p. 207; January 29, 2010, pp. 118–119.
[385] Levi, January 29, 2010, p.122
[386] Levi, January 29, 2010, p. 123.
[387] Levi, January 29, 2010, p.123

Standards for 1988-1990"[388]. The central issue of Levi's report is fraud detection - whether C&L could or could not have detected the full spectrum of the alleged fraud.

[404] The main issue in the present file is not fraud detection – the Court is not asked to determine whether C&L could or could not have detected the full spectrum of an alleged fraud: C&L are not sued because they would have failed to detect fraud.

[405] The Court has to decide if C&L did their work in accordance with GAAP and GAAS.

[406] If the Court concludes that C&L did not comply with GAAP and GAAS, the following question is whether C&L would have been in a position to sign a similar unqualified audit opinion in 1988, 1989 and 1990, had they complied with GAAP and GAAS.

[407] The mandate requested of Levi to identify signs of an alleged fraud on the auditors, without any consideration of the audit work performed, is a hollow exercise. How can someone conclude that it was impossible for the auditor to have detected material misstatements, without considering what GAAS required the auditor to do, and then assessing whether such auditor complied with the requisite standards?

[408] Levi stated that, in performing his mandate in the Castor file, he complied with "*Standard Practices for Investigative and Forensic Accounting Engagements*", which required him to "*identify, analyze, assess and compare all relevant information*" and *"develop and test, as needed, hypotheses for the purpose of evaluating the issues*[389]. However, in cross-examination, he admitted that he had not complied as he was confronted with the situation where he had failed to identify, analyze, assess and compare all relevant information and test alternative hypotheses[390].

[409] Levi reviewed the testimony that was provided to him; he did not review all of the testimony[391].

[410] Although Levi asserted that his mandate excluded a determination as to whether C&L obtained sufficient appropriate audit evidence ("**SAAE**") and generally complied with GAAS[392], he opined in his report: «*I have examined the working paper files prepared by Coopers & Lybrand for the audits of the Castor Holdings Ltd. group of companies for the years 1988 to 1990 and have not found any failures in their application of generally accepted auditing standards which could have resulted in the*

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[388] D-1347, p.3
[389] D-1313, p. 9, paras 400.04 and .05; Levi, January 12, 2010, pp. 66-68.
[390] Levi, January 28, 2010, pp. 65-69; February 3, 2010, pp. 125-126.
[391] Levi, February 3, 2010, pp. 80-82.
[392] Levi, January 11, 2010, pp. 64-66.

auditor's failure to detect the fraudulent activities which occurred at Castor Holdings Ltd. as described herein»[393].

[411] His opinions were tainted at the outset by his assumption that C&L would not have made errors. By way of example, he relied on notations in the AWPs to attack the integrity of underlying documents, asserting that it was not plausible that the notations could be consistently erroneous[394]. After being confronted with evidence in cross-examination as to the fallacy of his assumption, Levi was forced to acknowledge the audit errors, but then reversed his position and began to defend them as being allegedly commonplace[395].

[412] Levi admitted that he did not know if the Matters for attention of partners ("**MAPs**") brought forward the points that should have been brought forward to the partner[396]. He assumed that if Wightman was presented with a document that he felt was incomplete or inaccurate, he would have required it to be corrected[397].

[413] He initially suggested to this Court that Wightman reviewed the working paper files before meeting with Stolzenberg for the year-end wrap-up, but he then admitted that he did not verify the testimony of Wightman to ascertain if that was true[398]. As a matter of fact, Wightman did not review the working paper files[399].

[414] Levi opined as he did by taking for granted that C&L audits in 1988, 1989 and 1990 had been performed as "*a normal financial audit applying GAAS*".

[415] Levi became an advocate for Defendants by assuming fraud and a deception on the auditors. He identified in his report and testimony what he deemed to be indicia of fraud without considering the evidence suggesting an alternative explanation, the underlying transaction, the nature of the audit work performed or the books and records.

[416] If one looks at the evidence for the sole purpose of identifying indicia of fraud, there is a risk of misinterpreting facts and distorting reality. In fact, Levi's own invoices could be characterized as forgeries if one applied his methodology. Plaintiff's counsel was provided one version of these invoices in response to a subpoena *duces tecum*, but the version produced into the record [400]contained different information. There was neither fraud nor any intention to mislead but if one looks at these documents the way that Levi approached the Castor mandate, one would or could talk of "false documents"

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[393] D-1347, p. 31.
[394] Levi, January 28, 2010, pp. 118-120, 130.
[395] Levi, January 28, 2010, pp. 199-208.
[396] Levi, February 2, 2010, pp. 63-64
[397] Levi, February 2, 2010, pp. 64-65.
[398] Levi, February 1, 2010, pp. 133-134, 189.
[399] Wightman, February 11, 2010, pp.73-74
[400] PW-3096.

and the fact that legal counsel was involved in the communication of the documents could or would suggest a conspiracy to deceive[401].

Are the audited consolidated financial statements of Castor for 1988, 1989 and 1990 materially misstated and misleading?

Conclusion

[417] The audited consolidated financial statements of Castor for 1988, 1989 and 1990 are materially misstated and misleading.

[418] The Auditors' Reports, issued by C&L on the consolidated financial statements of Castor for the years ended December 31, 1988, 1989 and 1990, state that the financial statements present fairly, in all material respects, the financial position of Castor as at December 31, and the results of its operations and changes in its net invested assets, for the year then ended, in accordance with GAAP[402].

[419] The 1988, 1989 and 1990 audited consolidated financial statements do not present fairly, in all material respect, and in accordance to GAAP, the financial situation of Castor namely because of (pursuant to) the:

- Absence of a Statement of Changes in Financial Position showing the sources and uses of cash and cash equivalents;
- Undisclosed related party transactions;
- Artificial improvements of liquidity and undisclosed restricted cash;
- Undisclosed Capitalised interests and inappropriate revenue recognition;
- Understatement of Loan loss provisions and overstatement of carrying value of Castor's loan portfolio and equity;
- The reality of diversion of fees.

[420] «*The reports of the auditors were absolutely clean, as clean as white snow in Montreal five minutes after it snowed*»[403]. The trends in financial performance with respect to revenue, net earnings, retained earnings, assets/liabilities, capital stock as

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[401] Levi, February 3, 2010, pp. 196-205.
[402] PW-5 (tab 10, 11 and 12)
[403] Jarislowsky, April 4, 2005, p. 323

well as shareholders' equity, evident from Castor's audited consolidated financial statements[404], "*portrayed an uninterrupted pattern of yearly improvement and success in all those categories*"[405]. These financial trends were described as "outstanding"[406], "highly impressive"[407], "spectacular"[408] , and even "magnifique"[409].

[421] In reality, things were otherwise.

[422] The presentations, disclosures and omissions of disclosure combined and complemented each other to effectively conceal the fact that Castor's operations were not generating cash but rather draining the cash resources of the company, a vital fact that could not be ascertained from the financial statements.

General state of affairs – 1988, 1989 and 1990

Loan portfolio

[423] Castor's investment portfolio was comprised of two parts: the "*relationship*" loans which comprised 95% of the portfolio and the "*third party*" loans which comprised the remaining 5%. The relationship loans included the loans to the YH group, the loans connected to the three Skyline hotels, the loans to the MLV project, the loans connected to the MEC project, the loans to the DT Smith group and the loans to the Wost group.

Loan commitment and renewal letters - covenants

[424] Castor's loan commitment and renewal letters generally followed a consistent pattern in respect of loan covenants. Borrowers were requested to:

- Pay monthly or quarterly the interests;
- Pay the commitment or renewal fees at the time of the making or the annual renewal of a loan;
- Provide audited or unaudited financial statements regularly;
- Provide legal opinions confirming the validity and enforceability of security; and,
- Provide financial information related to the status and progress of the project, in the case of actual construction loans.

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[404] Respectively, PW-2888, PW-2889, PW-2890, PW-2891 and PW-2892, all based on data from PW-5-1
[405] PW-2908, Vol. 1, p. S-4, S-16 and S-17.
[406] Lowenstein, March 21, 2005, p.137
[407] Morrison, October 10, 2006, pp. 218-220, at p. 220; October 11, 2006, pp. 9-21, at pp. 12, 16.
[408] PW-2405, pp. 6-7.
[409] Lajoie, November 19, 2009, pp. 128-131, at p. 131. See also Jarislowsky, April 4, 2005, p.39

[425] Castor's borrowers were breaching these loan covenants, both before and during 1988 to 1990.

[426] Looking at YH group, DT Smith, MEC, MLV, TSH, CSH, OSH, TWTC and Meadowlark loans, there is not one single instance where the borrowers complied with all of their loan covenants. As a matter of fact, in most of the cases, the borrowers did not comply with any of their covenants.

[427] For 1988, 1989 and 1990, the YH borrowers did not and could not provide Castor with audited financial statements.

[428] Furthermore, in respect of the various real estate projects, borrowers were in default of their obligations to make payments of taxes as well as payments to prior ranking secured lenders or co-owners.

[429] The failure of Castor's borrowers to respect their covenants was documented in hundreds of memos in Castor's loan files and in Castor's books and records.

Security profile

[430] There was a marked shift in Castor's security profile over the 1980s.

[431] In its promotional materials published annually, Castor stood out as a lender whose preferred investments were first and second mortgage interim loans on income producing properties[410]. However, by 1988, loans secured by mortgages represented less than 50% of Castor's portfolio and, in each subsequent year, such loans represented an increasingly smaller percentage of Castor's total portfolio[411].

[432] By 1986, Castor had run out of YH projects on which to re-allocate the ever increasing (snowballing[412]) year-end YH indebtedness and, consequently, was obliged to commence making equity loans to parent and grand-parent companies.

State of projects

[433] With respect to Castor's loans connected to the various hotels (the Skyline hotels and the MLV hotels):

- The operations were in deficit and operators incapable of meeting their obligations (MLV - non-payment of taxes, OSH - non-payment of rent and TSH - non-payment of taxes)[413]; and

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[410] E.g. PW-1057-1, PW-1057-2 and PW-1057-3
[411] PW-2893-24; Ron Smith, May 14, 2008, pp. 63-64
[412] Vance, April 9, 2008, p. 178; R. Smith, September 3, 2008, pp. 88-89, R. Smith, October 2, 2008, p. 62.

- Each property required renovations, but as financing to carry them out could not be raised or was misappropriated for other purposes, the project's losses continued to increase.

[434] Castor's development loans to the DT Smith group were characterized by delays and cost overruns.

Financial situation of borrowers

[435] The YH group and the DT Smith group were financially dependent on Castor for their liquidity needs[414]. It was unrealistic to expect anything but capitalized interest revenue on their loans[415].

[436] During the 1988 to 1990 period, and absent Castor's ongoing life support, Castor's principal borrowers were not financially viable:

- YH group of companies were likely insolvent in that they could not pay their liabilities in the normal course of business without Castor's continuous financial support [416];

- the Wost group of companies relied on funds received by Castor to pay liabilities in the normal course of business as they generated no cash or very little cash from their own operations[417]; and

- the DT Smith companies were totally dependent on Castor for their liquidity needs. [418]

[437] By 1988, Castor was financing unpaid taxes, project deficits and other operating expenses of the properties in order to avoid foreclosure by prior ranking lenders or sales for taxes[419].

[438] The YH borrowers were insolvent during 1988, 1989 and 1990[420]. In December 1989, documents were shown by YH to Castor evidencing such insolvency[421]. YH

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[413] Prychidny, October 14, 2008, pp. 44-48
[414] D-1324
[415] D-1324
[416] D-1312, ES-25 (Goodman's report)
[417] See Books and records of the Wost group
[418] D-1324
[419] PW-167
[420] R. Smith, May 14, 2008, p. 183; PW-1153; Prychidny, October 14, 2008, pp. 83-85; D-1312, ES-25, 154; Whiting, February 22, 2000, pp. 67, 70-79; May 9, 2000, p. 54.
[421] PW-1149; PW-499C-1; PW-1153; Whiting, November 17, 1999, pp. 93-103.

management threatened to resign en masse unless Castor agreed to fund YH's operating requirements[422].

[439] Castor was "trapped" and had no choice but to keep tolerating YH's defaults: YH could not survive without Castor's support and the failure of YH would lead to the demise of Castor[423].

Capitalized interest and fee income

[440] For 1988, 1989 and 1990, and based on a sample of more than 60% (average 64.05%) of Castor's investment portfolio, the minimum amount of capitalized interest and fee income was:

- 1988: 92.4% or $79.3 million;
- 1989: 96.9% or $121.1 million;
- 1990: 96.2% or $159.7 million[424].

[441] Very little of Castor's revenue was collected in cash.[425]

[442] Virtually 100% of the interest recognized by Castor on YH loans was either capitalized to new or existing loans or paid through cash circles at year-end.[426] The same pattern was prevalent in respect of the loans to the three Skyline Hotels, MLV, MEC, Meadowlark and DT Smith.[427]

Loan loss provisions

[443] Until 1988, Castor had no policies on loan loss provisions and, in fact, never took a provision prior to that year[428].

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[422] Quigley, March 15, 2010, pp. 213-214; March 16, 2010, pp. 63-64
[423] R. Smith, May 14, 2008, pp. 139-140, 175; September 3, 2008, pp. 50-51; September 15, 2008, pp. 138-139
[424] PW-1485R
[425] Tooke, February 27, 2008, pp. 98-99; PW-98 A, PW-98 B, PW-98 C and PW-98 D
[426] PW-1056 F; R. Smith, May 14, 2008, pp. 138-139.
[427] PW-167 and PW-2908
[428] Ron Smith May 14, 2008, pp. 121-126.

Applicable GAAP rules (in a nutshell) [429]

Nature and sources of GAAP

[444] GAAP are promulgated by the Canadian Institute of Chartered Accountants ("**CICA**") through published reports, including "recommendations with respect to matters of accounting practice". These recommendations are contained in the CICA Handbook and are revised and updated periodically.

[445] GAAP is the term used to describe the basis on which financial statements are normally prepared[430].

[446] No rule of general application can be phrased to suit all circumstances or combination of circumstances that may arise, nor is there any substitute for the exercise of professional judgment in the determination of what constitutes fair presentation or good practice in a particular case.

[447] The term GAAP encompasses not only specific rules, practices and procedures relating to particular circumstances but also broad principles and conventions of general application, including underlying concepts described in section 1000 of the Handbook.

[448] Most sections of the Handbook contain discussions and prescriptive statements. When a paragraph is italicized, the paragraph is determinative of the issue the section is addressing - as an Accounting Recommendation.

[449] Specifically, GAAP comprise the Accounting Recommendations in the Handbook and, when a matter is not covered by a Recommendation, other accounting principles:

a) generally accepted by virtue of their use in similar circumstances by a significant number of entities in Canada; or

b) consistent with the Recommendations in the Handbook and developed through the exercise of professional judgment[431].

[450] In those rare circumstances where following a Recommendation would result in misleading financial statements, GAAP encompass appropriate alternative principles[432].

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[429] PW-1419-1 (1988), PW-1419-2 (1989) and PW-1419-3 (1990)
[430] PW-1419-2,1000.48
[431] PW-1419-1,1000.49
[432] PW-1419-1,1000.50

Other Financial statements concepts (section 1000)

[451] Financial statements are designed to meet the common information needs of external users of financial information about an entity. [433]

[452] Financial statements normally include a balance sheet, income statement, statement of retained earnings and statement of changes in financial position. Notes to financial statements and supporting schedules to which the financial statements are cross-referenced are an integral part of such statements. [434]

[453] The content of financial statements is usually limited to financial information about transactions and events. Although they often require estimates to be made in anticipation of future transactions and events, and include measurements that may, by their nature, be approximations, financial statements are based on representations of the past, rather than future, transactions and events. [435]

[454] The objective of financial statements focuses primarily on information needs of investors and creditors[436] but the benefits expected to arise from providing information in financial statements should exceed the cost of doing so. [437]

[455] Investors and creditors, for the purpose of making resource allocation decisions, are interested in predicting the ability of an entity to earn income and generate cash flows in the future to meet its obligations and to generate a return on investment. [438]

[456] As a general rule, materiality should be judged in relation to the significance of financial statement information to decision makers. An item of information, or an aggregate of items, should be deemed material if it is probable that its omission or misstatement would influence or change a decision[439].

[457] Qualitative characteristics define and describe the attributes of information provided in financial statements that make that information useful to investors, creditors and other users. The four principal qualitative characteristics are understandability, relevance, reliability and comparability[440].

[458] Although information provided in financial statements will not normally be a prediction in itself, it may be useful in making predictions. The predictive value of the

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[433] PW-1419-1,1000.01
[434] PW-1419-1,1000.04
[435] PW-1419-1,1000.05
[436] PW-1419-1,1000.09
[437] PW-1419-1,1000.13
[438] PW-1419-1,1000.10
[439] PW-1419-1,1000.14
[440] PW-1419-1,1000.15

income statement, for example, is enhanced if abnormal items are separately disclosed[441].

[459] For the information provided in financial statements to be useful, it must be reliable[442].

[460] Financial statements are prepared on the assumption that the entity is a going concern – it will continue in operation for the foreseeable future and will be able to realize assets and discharge liabilities in the normal course of operations.[443]

General standards of financial presentation (section 1500)

[461] *"Any information required for fair presentation of financial position, results of operations, or changes in financial position, should be presented in the financial statements including notes to such statements and supporting schedules to which the financial statements are cross-referenced"*[444].

[462] Financial reporting is essentially a process of communication. The extent of disclosure has an impact on the success of such communication.

[463] Decisions as to disclosure require the exercise of sound judgment[445] .

Disclosure of accounting policies (section 1505)

[464] *"A clear and concise description of the significant accounting policies of an enterprise should be included as an integral part"*[446].

[465] The usefulness of the financial statements is enhanced by the disclosure of the accounting policies.

Statement of changes in financial position (section 1540)

[466] The objectives of the statement of changes in financial position ("**SCFP**") are:

- To provide information about the various activities of the enterprise (operating, financing, investing) and their effect on cash resources;
- To assist the user in evaluating the liquidity and solvency of the enterprise;

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[441] PW-1419-1,1000.17
[442] PW-1419-1,1000.18
[443] PW-1419-1,1000.47
[444] PW-1419-1,1500.05
[445] PW-1419-1,1500.02
[446] PW-1419-1,1505.04

- To assist the user in assessing the ability of the enterprise:
    - to generate cash from internal sources;
    - to repay debt obligations;
    - to reinvest; and
    - to make distributions to owners[447].

[467] The SCFP focuses on cash and cash equivalents – liquid financial resources readily available.

[468] *"The SCFP should report the changes in cash and cash equivalents resulting from the activities of the enterprise during the period"*[448].

Accounts and Notes receivables (Section 3020)

[469] *"An account or note receivable should be written-off as soon as it is known to be uncollectible"*[449].

[470] *"An account or note receivable should be written down to its estimated realizable value as soon as it is known that it is not collectible in full"*[450].

Revenue (section 3400)

[471] The amount of revenue generated by an enterprise is an important indicator of the level of the activity of the enterprise[451].

[472] Revenue should be recognized when the requirements related to performance as set out in sections 3400.07 or 3400.08 of the Handbook are satisfied, provided that ultimate collection is reasonably assured at the time of performance.

Subsequent events (section 3820)

[473] Subsequent events can provide evidence relating to conditions that existed at the financial statement date or can be indicative of conditions which arose subsequent to that date[452].

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[447] PW-1419-1, 1540.01
[448] PW-1419-1, 1540.04
[449] PW-1419-1, 3020.10
[450] PW-1419-1, 3020.10
[451] PW-1419-1, 3400.20
[452] PW-1419-1, 3820.03

[474] *"Financial statements should be adjusted when events occurring between the date of the financial statements and the date of their completion provide additional evidence relating to conditions that existed at the date of the financial statements"*[453].

[475] *"Financial statements should not be adjusted for, but disclosure should be made of, those events occurring between the date of the financial statements and the date of their completion that do not relate to conditions that existed at the date of the financial statements but (a) cause significant changes to assets or liabilities in the subsequent period; or (b) will, or may, have a significant effect on the future operations of the enterprise"*[454].

Related party transactions and economic dependence (section 3840)

[476] Parties are considered to be related when one party has the ability to exercise control or significant influence, directly or indirectly, over the operating and financial decisions of the other[455].

[477] Two or more parties are also considered related when they are subject to common control or significant influence[456].

[478] *"When a reporting entity has participated in transactions with related parties during a financial reporting period, disclosure should be made"*[457].

[479] *"When the ongoing operations of a reporting entity depend on a significant volume of business with another party, the economic dependence on that party should be disclosed and explained"*[458].

Interests Capitalized (section 3850)

[480] *"The amount of interest capitalized in the period should be disclosed"*[459].

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[453] PW-1419-1, 3820.06
[454] PW-1419-1, 3820.10
[455] PW-1419-1, 3840.03
[456] PW-1419-1, 3840.03
[457] PW-1419-1, 3840.10
[458] PW-1419-1, 3840.18
[459] PW-1419-1, 3850.03

The 1988 audited financial statements

Some Figures and notes content of the 1988 statements

[481] According to its balance sheet, Castor had:

- 1 005 992$ of investments in mortgages, secured debentures and advances more fully disclosed in notes 2, 3, 4 and 10;
- 100 000$ of liabilities through debentures, more fully disclosed in note 6.

[482] According to the consolidated net earnings statement, Castor's revenues for 1988 were of 132 410 000$, more fully disclosed in note 9, and Castor's net earnings for 1988 were 22, 236 000$.

[483] According to note 10 on related party transactions:

- secured debentures and advances due from shareholders in the amount of 7 016,728$ were included in investments in mortgages, secured debentures and advances; and
- transactions during the year, and amounts due to or from shareholders and directors not otherwise disclosed separately in the financial statements, were as follows:
    - accrued interests and other payables : 1,187 000$
    - interest revenue : 611 000$
    - other expenses: 333 000$

[484] Notes 2, 3, 4, 6 and 9 read as follows:

2. Investments in mortgages, secured debentures and advances

The investments in mortgages, secured debentures and advances are in various currencies and bear interest at varying rates from 6% to Canadian bank prime rate plus 6% per annum and mature as follows:

	(thousands of Canadian dollars)
1989	712,455
1990	94,995
1991	50,667
1992	10,172
1993	133,508
1994	3,806
1998	358
2005	31
	1,005,992

3. Notes payable

(a) These notes are payable in various currencies and bear interest at varying rates from 4% to 12. 5% and mature as follows:

	TOTAL	1989	1990	1991	1998
			(thousands of Canadian dollars)		
SECURED	173,040	130,540	42,500	-	-
UNSECURED	268,196	241,294	25,846	698	358
	441,236	371,834	68,346	698	358

(b) Mortgages having an approximate book value of $172,176,000 have been pledged as security for the secured notes payable.

4. Bank Loans and advances

(a) Bank loans and advances are classified as follows:

	1988	1987
	(thousands of Canadian dollars)	
Demand loans and advances bearing interest at floating rates	-	7,400
Term loans and advances bearing interest at floating rates and varying fixed rates from 4.125% to 12.625% per annum	376,531	281,731
	376,531	289,131

(b) The term loans and advances mature as follows:

1989	1990	1991	1993
	(thousands of Canadian dollars)		
296,537	35,822	20,310	23,862

(c) Mortgages having an approximate book value of $143,953,000 have been pledged as security for the bank loans totalling $141,609,000..

6. Debentures

	1988	1987
	(thousands of Canadian dollars)	
(a) Debentures maturing on June 30, 1997 bearing interest at The Royal Bank of Canada prime rate plus 2 ¼% but not less than a minimum of 11% per annum. After June 30, 1992, the company has the right to prepay the principal amount. Interest on the debentures is payable semi-annually.	50,000	50,000
(b) Debentures maturing on June 30, 2002 bearing interest at The Royal Bank of Canada prime rate plus 2 3/8% but not less than a minimum of 11% per annum. After June 30, 1994, the company has the right to prepay the principal amount. Interest on the debentures is payable semi-annually.	50,000	50,000
	100,000	100,000

9. Revenue

Details of revenue are as follows:

	1988	1987
	$	$
	(thousands of Canadian dollars)	
Interest and discounts	117,366	89,298
Commissions	14,689	8,817
Share of revenue from investments and joint ventures	355	281
	132,410	98,396

Materially misstated (1988)

[485] The 1988 audited financial statements were materially misstated.

Absence of a Statement of Changes in Financial Position showing the sources and uses of cash and cash equivalents

Historical information

[486] Since its inception and until 1985, Castor had used a Statement of Changes in Net Investment Assets ("**SCNIA**")[460].

[487] This early format of the SCNIA referred to "*proceeds*" from bank loans, notes payable, advances from shareholders, and other items, and to "*receipt of payments of matured portion of mortgages, secured debentures and advances*". Accordingly, the reader could see what payments were made by Castor's borrowers during the year on account of the matured portion of mortgages, secured debentures and advances. Similarly, the statement reflected "*payments*" made by Castor to its own lenders of notes payable and bank loans.

[488] Until 1985, the user of Castor's financial statements could see what portion of the investments maturing in the following year was, in fact, repaid[461].

- The user of these financial statements could see that the investments maturing in the following year were, in fact, repaid up to 1982.

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[460] PW-5-1

[461] PW-2908, Vol. 1, p. 4-C-6 and 4-C-7.; Vance, March 10, 2008, pp. 123 and following; Rosen, February 3, 2009, pp.42 and following.

- One-third of the portion of matured investments was repaid by borrowers during 1983 and less than 15% during 1984.

[489] As an example, the SCNIA for the year ended December 31, 1984 showed the following:

	1984	1983
NET ASSETS AVAILABLE FOR INVESTMENT		
Provided from operations	9,087	7,467
Proceeds from notes payable	229,796	176,376
Proceeds from bank loans and advances	48,185	18,597
Increase in other liabilities	2,183	(1,494)
Proceeds from loans and advances from shareholders	19,924	11,173
Proceeds from issue of capital stock	3,726	4,979
Receipt of payments of matured portion of mortgages, secured debentures and advances	25,340	43,531
Disposal of marketable securities	----	863
Disposal of income producing property	----	2,857
	338,241	264,349
LESS:		
Payment of notes payable	150,244	113,841
Payment of bank loans	20,012	3,205
Payment of 12% mortgage	----	2,064
Payment of loans and advances from shareholders	12,213	12,174
Redemption of Class "A" pref. shares	263	190
Redemption of Class "B" pref. shares	----	83
Redemption of Class "A" com. shares	473	302
Redemption of Class "B" com. shares	----	4
Dividends paid	5,809	3,556
Increase in other assets	22,631	102
	126,596	128,828
NET ASSETS INVESTED AS FOLLOWS		
Purchase of mortgages, secured debentures and advances	125,471	126,330
Investment in joint ventures	1,125	2,498
	126,596	128,828

[490] Therefore, this early format of the SCNIA purported to disclose, in part, cash inflows and cash outflows.

[491] In 1985, the disclosure requirements for a Statement of Changes were amended to require that this financial statement report the changes in cash and cash equivalents, in order to provide a better indication of the liquidity and solvency of an enterprise as well as its ability to generate cash resources. These amendments came into effect in October of 1985.

[492] Section 1540 of the CICA Handbook required that the Statement of Changes in Financial Position ("**SCFP**") show sources and uses of cash from operations as well as from financing and investing activities.

[493] As Grezlak testified, "*the change took focus away from working capital and put it to cash*"[462].

[494] The use of a SCFP in Castor's financial statements would not have provided misleading information, a fact Wightman acknowledged[463].

[495] Two statements of changes were prepared prior to the wrap up meeting by Grzelak[464], a SCFP and a SCNIA, and both were presented to Stolzenberg.

[496] What happened next?

[497] Wightman's descriptions of the events vary significantly. In 1996, he had no precise recollection. In 2010, in direct examination, he came up with very specific and "self-serving" information. In cross-examination, when asked to explain what had triggered his memory, 14 years later, Wightman gave explanations but he could not support them with the specific references when challenged to do so. This is one of many situations where all of a sudden Wightman's memory has "improved"[465] : no credibility is attached to Wightman's recollection at trial.

- Wightman said during discovery in 1996:

  Q-And did you understand or do you understand from reading this that Mr. Clark apparently wants to know whether a format using cash should be employed?

  A- I think that he was asking the question, yes.

  Q- Did in fact you review this matter with Mr. Grzelak?

  A- I can't remember, I might have reviewed it with Steve Clark, but I don't remember that either. I explained to you before I didn't recall specifically. On the other hand, Mr. Clark may have reviewed it with Mr. Grzelak and not with me, I don't remember specifically.

  Q- Well let's restrict ourselves to what you were involved in.

  A -Hm,hm.

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[462] Grezlak, October 21, 1996, p.111 Q. 414
[463] Wightman, March 11, 2010, pp. 64-65
[464] Grezlak, October 21, 1996, pp. 115-116
[465] For other examples - see namely the following sections of the present judgment : Independence,

Q- Is it your testimony today that you're not able to give us any additional information as to any meetings or discussions which took place subsequent to these particular queries?

A- In early 1986, no[466].

- Wightman said at trial, in direct examination

Q-Now, during the... over the course of the years that you were involved as the audit partner for the audit of Castor, did you ever have any discussions with Mr. Stolzenberg having regard to changes in the presentation of the financial statements?

A- Yes.

Q- Okay. With respect to which issue, do you recall?

A- I remember suggesting to them that they consider adopting a statement of changes in financial position, and I think that was in eighty-five ('85) or eighty-six ('86). At the time, I requested that the audit manager, who I believe at that time was Mr. John Grzelak, I asked him to, during the course of the audit, to prepare a draft statement of changes in financial position, and preparatory to visiting with Mr. Stolzenberg and showing him. I told him about it prior to showing it to him, and said that I was recommending it because the Institute had introduced the presentation that they recommended, highly recommended that the use of statement of changes in financial position be adopted and so, I told him that I recommended that Castor do that.

Q- Okay. And what transpired in this regard?

A- For that specific issue, John Grzelak prepared a draft financial statement showing the statement of changes in financial position along with the regular statement from... following the same format as preceding years, which was the statement of changes in net invested assets, and that was... I can't recall specifically whether we sent a copy of the draft to Stolzenberg before we went to see him, or whether we took it with us.

Q- Okay. And who else was involved, from Castor's side of the table, in that discussion?

A- Mr. Dragonas.

Q- And did you have a meeting when you discussed this particular issue?

A- Yes.

[466] Wightman, September 13, 1996, pp. 138-140

Q- And do you recall... What's your recollection of the discussion that took place at that meeting?

A- Yes. With respect to that particular item, they said that they had looked and considered the statement of changes in financial position, and that they felt it was more appropriate for Castor to continue to use their statement of changes in net invested assets.

Q- And ultimately, the Court knows that the statement of changes in net invested assets continued to be used. What was your view, based on... further to that discussion, as to the SCFP and the use of the SCNIA, Mr. Wightman?

A- I think I testified a long time ago that I felt that Castor was what I considered almost an investment club, and that the shareholders and the lenders were all closely connected, that if any of the shareholders or the lenders, they wanted a statement of changes in financial position, they would phone. I was unaware of anyone ever phoning and asking[467].

- Wightman said at trial, in cross examination

Mr. Wightman, what explanation do you have for the differences in your testimony before this Court this week and the testimony that you gave on September the thirteenth (13th), nineteen ninety-six (1996) concerning the meeting with Mr. Stolzenberg, two (2) versions of the statement of changes and the presence of Mr. Dragonas at the meeting?

A- Again, I... Since this was raised with me when I hadn't previously spent very much time and I didn't know what the questions were going to be, I had an opportunity to examine the working papers and I also believe that I saw some extracts from the testimony of Mr. Grzelak which refreshed my memory.

Q- Now which working papers specifically are you referring to?

A- I don't recall, but I think it would have been at or about the time that the Handbook changed.

Q-You just said in your answer as part of the reasons for the difference in testimony is you examined the working papers.

A- Yes, I went more carefully through everything and I also had an opportunity to look at extract of Mr. Grzelak's testimony.

Q- Now when you say you went more carefully through everything, which specific working papers are you referring to that bear on this issue?

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[467] Wightman, February 8, 2010, pp.171-173

A- I don't recall. I said at or about the time of the change in the Handbook.

Q- So what years working papers?

A- I don't know how many times I can tell you, but it's at or about the time of the change and I don't recall the change offhand.

Q- Okay. But was it around nineteen eighty-five (1985) or nineteen eighty-six (1986)?

A- I believe so.

Q- Then what working papers did you look at in the nineteen eighty-five (1985) or nineteen eighty-six (1986) working papers that caused you to better recall as you testify this week?

A- I would have looked at probably the MAPS, I would have looked at the miscellaneous notes, I would have looked at all parts of the working papers.

Q- But what was there specifically dealing with the statement of changes in the financial position that you saw in the working papers that caused you to change your testimony?

A- .At this point, I don't recall.

Q- Okay. Then I would like you to look at the MAPS and the miscellaneous notes for the years nineteen eighty-five (1985) and nineteen eighty-six (1986) and tell the Court which documents in the working papers account for the change in your testimony.

(***witness is looking at various PW-1053 exhibits and he does not find***)

(...)

(***Counsel for plaintiff asks for an undertaking – Counsel for the Defendants does not agree***)

(...)

The Court - I'm not directing that the exercise be done. I'm not asking that it be done, but if there is anything specific to which I should have a look, I'm expecting that I will be made aware of this at some point.

So I'm not directing Mr. Wightman to do work. The answer we have is what we have. And there is nothing he can point us to as of now. And we know that we've been through two (2) of the three (3) elements. And in the two (2) of the three (3), we found nothing. It's going to stay there at this point[468].

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[468] Wightman, February 11, 2010, pp. 45 to 61

[498] Castor decided to continue to use a Statement of Changes in Net Investment Assets ("**SCNIA**") and a conscious decision was made by C&L not to force the use of the SCFP and, moreover, to accept changes to the usual presentation of the SCNIA[469].

[499] Indeed, starting with the 1985 financial statements, changes were made to the SCNIA including the elimination of information concerning what portion of the investments maturing the following year was in fact repaid[470]. Had the format of the SCNIA of previous years been used for 1985, the 1985 financial statements would have disclosed that only $27.4 million was received out of a total of $189 million of maturing investments.

[500] From 1985 onward, there was no disclosure of (i) proceeds from bank loans, notes payable and other items (but rather reference to "increases" thereof), (ii) the receipt of payments of the matured portion of mortgages, secured debenture and advances, and (iii) what payments were made by Castor to its lenders (but rather reference to "increases" in these liabilities).

[501] As an example, the SCNIA for the year ended December 31, 1985 showed the following:

	1985	1984
NET ASSETS AVAILABLE FOR INVESTMENT		
Provided from operations	10,887	9,087
Increase in notes payable	32,626	79,552
Increase in bank loans and advances	45,728	28,173
Increase in other liabilities	308	2,183
Proceeds from loans, debentures and advances	32,482	7,711
Proceeds from issue of capital stock	3,342	3,726
	125,373	130,432
LESS:		
Conversion of shareholder loans and advances into subordinated debentures (note 6 (a))	24,602	----
Redemption of common and preferred shares	300	736
Dividends paid	6,587	5,809
Increase in other assets	2,243	22,631
	91,641	101,256
NET ASSETS INVESTED AS FOLLOWS		
Purchase of mortgages, secured debentures and advances	91,132	100,131
Investment in joint ventures	509	1,125
	91,641	101,256

[469] Rosen, February 4, 2009, p.188

[470] Vance, March 10, 2008, pp.126 and following; Rosen, February 4, 2009, pp.160 and following (namely pages 170 and following) and Appendix A of PW-3034

[502] While the Handbook focused more and more on cash, Castor's financial statements moved in the opposite direction.

Positions (in a nutshell)

[503] There is a dispute between experts as to whether the inclusion of the SCFP was required. Vance and Rosen opine that the statement was required[471]; Selman opines that it was not[472].

Vance and Rosen

Vance

[504] On March 10, 2008, Vance testified that:

- section 1540 was changed to require the Statement of Changes in Financial Position to portray only the cash resources, one of the reasons being cash is not a subjective asset, cash is cash, it's not easily manipulated or subject to management bias at all, and all entities under the Handbook were then required to move to the Statement of Changes in Financial Position[473].

- After the introduction of section 1540, no provisions permitted anything other than cash resources to be used. Other suitable titles for this statement were "cash flow statement, statement of operating, financing and investing activities or statement of changes in cash resource"[474], all of them dealing with cash[475].

[505] Vance pointed out the following objectives and main features of the SCFP:

- To provide information about the operating, financing and investing activities of an enterprise and the effects of those activities on cash resources.

- To assist users of financial statements in evaluating the liquidity and solvency of an enterprise, and in assessing its ability to generate cash from internal sources to repay obligations, to reinvest and to make distributions to owners.

- To focus on the liquid financial resources readily available to the enterprise (its cash and cash equivalents).

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[471] Vance, March 10, 2008, pages 144 following; Rosen, February, 4, 2009, pp.138-190; Rosen, February, 25, 2009, pp.111-119, 124
[472] Selman, May 8, 2009, pages 171 and following
[473] Vance, March 10, 2008, p. 17
[474] PW-1419-1, section 1540, footnote (1988); PW-1419-2, section 1540, footnote (1989); PW-1419-3, section 1540, footnote (1990)
[475] Vance, March 10, 2008, p. 19

- To disclose separately the amount of cash generated from operations because it is one of the key indicators of the ability of the enterprise to pay debts, replace assets, make due investments and distribute dividends to owners without drawing on external sources of capital.

- To complement and present information that is not provided or is only indirectly provided in the other statements (the balance sheet and income statement of retained earnings).

[506] Vance emphasized on the 3 following italicised recommendations:

> **1540.05**: The statement of changes in financial position should report the changes in cash and cash equivalents resulting from the activities of the enterprise during the period.
>
> **1540.06**: The components of cash and cash equivalents should be disclosed.
>
> **1540.12**: The statement of changes in financial position should disclose at least the following items:
>
> a) cash from operations. The amount of cash from operations should be reconciled to the income statement or the components of cash from operations should be disclosed; (...)

[507] On the italicized recommendation 1540.12 (a), Vance explained that such disclosure was to allow a link from net profit to cash from operations so that the reader could be able to follow the trail[476].

[508] Vance mentioned that section 1540.19 provided an exception that would permit a company to use a format other than the Statement of Changes in Financial Position, but he confirmed that such exception could not apply to Castor[477].

[509] Section 1540.19 reads as follows:

> When a separate statement would not provide additional useful information, the presentation of cash flows in a financial statement format would not be necessary. For example, an enterprise may have relatively simple operations with few or no significant financing and investing activities and information about these activities and their effects on cash resources may be readily apparent from the other financial statements or could be adequately disclosed in notes to the financial statement.[478]

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[476] Vance, March 10, 2008, pp.28-29
[477] Vance, March 10, 2008, pp.32-33 and pp. 71-72
[478] PW-1419-1 (1988); PW-1419-2 (1989) and PW-1419-3 (1990)

[510] Vance also explained that, in certain circumstances which were not present in the Castor situation, sections 1000.04 and 1000.50 could impact the issue of a SCFP[479].

> 1000.04: "Financial statements normally include a balance sheet, income statement, statement of retained earnings and statement of changes in financial position. Notes to financial statements and supporting schedules to which financial statements are cross-referenced are an integral part of such statements."
>
> 1000.50 : In those rare circumstances where following a handbook recommendation would result in misleading financial statements generally offsets that accounting principles encompass appropriate alternative principles, when assessing whether a departure from handbook recommendations is appropriate, consideration would be given to
>
> a) the objective of the handbook recommendation and why that objective is not achieved or is not relevant in the particular circumstances;
>
> b) how the entity circumstances differ from those of other entities which follow the handbook recommendations and,
>
> c) the underline principles of accounting alternatives by referring to other sources, and as referenced to paragraph 1000.49 where it sets out what we would refer to as a hierarchy of GAAS
>
> The identification of these circumstances is a matter of professional judgement. However, there is a strong presumption that adherence to handbook recommendations results in appropriate presentation and that a departure from such recommendations represents a departure from generally accepted accounting principles."

[511] Vance also testified that during the relevant years, namely in 1988, it was in the lending industry a standard to use a financial statement presentation that referred to cash and cash equivalents, the only two exceptions known to him being Royal Trust who had dragged to its feet and only changed in 1989 and Roynat, a subsidiary of Montreal Trust Co. while however Montreal Trust Co. itself had a proper SCFP on its consolidated financial statements[480].

[512] Moreover, Vance added that, as mentioned in section 1000.49 of the Handbook, industry practices did not override applicable handbook recommendations in determining GAAP except to the extent that circumstances peculiar to the industry

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[479] Vance, March 10, 2008, pp.71-75
[480] Vance, March 10, 2008, pp.128-130

would make it misleading to follow a particular recommendation, which was not the case[481].

[513] Vance summarized his position on the SCFP as follows:

> There are a number of issues involved with the statement of changes in financial position. Firstly, this statement is designed to provide meaningful information to readers and users about the liquidity insolvency (sic – should be and solvency) of an enterprise.
>
> Had such a statement been used and presented, it would have firstly categorized the activities into operating, investing and financing activities and also, in so doing, would have shown that operations were draining the cash resources of the company significantly rather than operations generating cash, which they would do in a successful company.
>
> The statement could also have easily shown, as a line item, the amount of capitalized interest, which was not disclosed anywhere in PW-5, either as a policy or as to the amount that was occurring each year, and instead, Castor presented a statement of changes in net invested assets and what I find egregious is the asset they used to show the funds of the company was an asset that was grossly inflated by virtue of capitalized interest and by virtue of not writing... taking a loan loss provision.
>
> So they used probably the asset that was most misstated and focused on it as the fund statement. And that, I think, again, was very misleading to a reader. And as it was a departure from generally accepted accounting principles and as a significance or result of the departure was so material, I feel Coopers & Lybrand should have qualified their reports, but they did not do so[482].

Rosen

[514] Rosen emphasized on sections 1540.01, 1540.02, 1540.04 and 1540.06 of the handbook[483]:

> **1540.01. (...)**
>
> The statement of changes in financial position assists the users of financial statements in evaluating the liquidity and solvency of the enterprise, and in assessing its ability to generate cash from internal sources to repay debt obligations, to reinvest and to make distributions to owners."
>
> **1540.02**. The statement of changes in financial position focuses on the liquid financial resources readily available to the enterprise, its cash and cash equivalent. This focus provides a better indication of liquidity and solvency and

[481] Vance, March 10, 2008, p.133
[482] Vance, March 10, 2008, pp.137-138
[483] Rosen, February 3, 2009, pp.38 and following

> the ability of an enterprise to generate cash resources than does a focus on working capital or other non-cash groupings.
>
> **1540.04** The statement of changes in financial position should report the changes in cash, in cash equivalence, resulting from the activities of the enterprise during the period."
>
> **1540.06**. The components of cash and cash equivalents should be disc losed."

[515] Rosen explained that section 1540 of the CICA Handbook required cash disclosures[484].

[516] Rosen described the evolution of the section in the following terms:

> (...) the evolution of this particular statement, like it's the newest of the statements in terms of accounting, was cash was the centre point, because it was necessary to separate between cash transactions and accrual-type transactions that make up the income statement and chunks of the balance sheet[485].

[517] Rosen compared the content of the SCNIA before and after 1985, before and after the change was made to section 1540 of the Handbook[486].

[518] Rosen explained his writings "*Castor's revised SCNIA was clearly designed to be virtually the opposite in concept to what the CICA was directing*": some of the most crucial information that investors and creditors would want to know about liquidity and solvency, cash items and information, were hidden in the SCNIA included in Castor's audited financial statements of 1988[487] (as it had been the case since 1985).

[519] Rosen concluded that the 1988 audit report of C&L should have been qualified "*that GAAP is not being complied with and the thrust of section 1540 has not been met*"[488].

Selman

[520] Selman's view, which according to him was amply supported by the factual diversity of practice that existed at the time, was that section 1540 of the Handbook did not require a SCFP but merely indicated what it should contain if one was provided[489].

[521] Selman suggested that Castor was not the only one not to provide a SCFP and so the Court should conclude that a SCFP was not required.

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[484] Rosen, February 4, 2009, pp.138 and following
[485] Rosen, February 4, 2009, p.140
[486] Rosen, February 4, 2009, pp.168-169
[487] Rosen, February 4, 2009, pp.175-179
[488] Rosen, February 4, 2009, p.188
[489] Selman, May 13, 2009, p.120

[522] Selman's overall opinion on the SCFP was:

> My position is that Castor's financial statements met GAAP despite the substitution of a statement of changes in net invested assets, for the form that we have seen being used by others' statement of changes in financial position. I think such a substitution was permitted, it was fully disclosed, it did not reduce the amount of information to which a reader was entitled to under generally accepted accounting principles of the day[490].

[523] However, Selman acknowledged that Castor's SCNIA did not meet the literal requirements of section 1540 of the Handbook.

> Mr. Vance may be correct in saying that the statement of changes format used by Castor did not meet the literal requirements of the Handbook, section 1540 to provide a SCFP, although the Handbook states only that it would normally appear and provides some room for exception (paragraphs 1000.04 and 1000.05). [491]

A SCFP was required

[524] A SCFP was required – section 1540 and its italicized recommendations were clear. This separate statement would have provided additional useful information (and therefore the exception of section 1540.19 could not apply) and there was no risk to provide misleading information through a proper SCFP (and therefore the exception of section 1000.50 could not apply either).

[525] The simple fact that some financial statements identified by Selman did not include a SCFP is not conclusive.

[526] It is significant, however, that a SCFP was required by C&L in its own technical material.

- The specific need for a SCFP appears in C&L's Tips and Tidbits dated April 25, 1986, in section 12[492].

- The Technical Policy Statements of C&L which were in force during the period dealt specifically with the issue of a departure from a Handbook recommendation as follows[493]:

> *«Accordingly, a departure from the Handbook Recommendations will almost always require a reservation in the auditors' report on*

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[490] Selman, May 13, 2009, p.129
[491] D-1295, p.112, para. 4.5.4.05
[492] PW-1420-1D, T&T Summary Bulletins 1 to 63, p. 10.
[493] PW-1420-1B, TPS-A-400.

financial statements purporting to be presented in accordance with GAAP.

(...) Unless applying the Recommendation results in a misleading financial statement, the Recommendation must be followed».

[527] The audit clients of Wightman whose financial statements have been produced in the record all included a SCFP[494].

[528] Mitchell, the audit manager in charge of the 1988 audit in Montreal (and also of the 1989 audit), stated that he did not recall having any other clients using the format used by Castor in the statement of changes. [495]

[529] Picard, the auditor in charge of the field work in Montreal during the 1989 audit stated that the format of the statement of changes must have been at the request of the client because the CICA Handbook was modified in 1985 and «*donc, dans mes autres dossiers chez Coopers, j'avais modifié l'état d'évolution.*»

[530] Hayes, who did reviews of Castor's audited financial statements as the second partner and who was handling many other client lender's audits[496], testified as follows:

> Q. Do you recall having looked at the consolidated statement of Changes and Net Invested Assets?
>
> A. Yes.
>
> Q Is this the same type -of presentation that was used on banks that you were familiar with?
>
> A. Not at that time.
>
> Q When you say "not at that time", could you be more specific?
>
> A In earlier years, this had been a general statement, a general standard for statements such as this.
>
> Q. Until when?
>
> A. Until 1986.
>
> Q And after 1986 what was the change in presentation that was made?

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[494] PW-2908, Vol. 1, p. 4-C-6; PW-1053-23, seq. pp. 101, 112; PW-662-1; PW-662-1A; PW-662-1B; PW-662-1C; PW- 567-37

[495] Mitchell, April 25, 1996, p. 136.

[496] Hayes, October 31, 1995, pp. 20-22

A. The general change in presentation was to regroup the numbers shown on this statement into different groupings.

Q. And what were the different groupings?

A. Funds provided from operations, funds provided from borrowing and funds provided from - or funds used in investment.

Q. And what was the reason that that type of presentation was not used for Castor's financial statements?

A. I don't know specifically. These are the client's Statements, that would have to be asked of the client.

Q But did you ever ask Mr. Wightman or anybody else why the changes in the presentation were not made for CASTOR's statements?

A. I don't recall specifically.

Q You don't recall having asked anybody?

A. No.

Q Do you know whether it was the client's desire to retain this form of presentation?

A No, I assume it was.

Q But this was not the form of presentation that you were using for other lender clients?

A. No[497].

[531] In the present litigation, during the cross-examination of Vance, he was criticized for a purported failure to identify to the Court that in "*The External Audit*", the textbook by Anderson, the author indicated that there were two schools of thought in the profession regarding the use of a statement of changes[498]. However, the Anderson textbook was published in 1984 and, as correctly noted by Vance, any debate in the profession was ended in 1985 when section 1540 was amended[499]. From 1985 onwards, it was mandatory for an operating company like Castor to include a SCFP showing its cash flows[500] (unless the inclusion of such would be misleading to readers).

[532] Castor came nowhere near qualifying for the exception provided for in section 1540.19:

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[497] Hayes, October 31, 1995, pp.80-82
[498] PW-1421-7, pp. 584–585.
[499] Vance, May 27, 2008, pp. 226-228.
[500] PW-2908, Vol. 1, p. 4-C-10; PW-3108-3.

- Castor's operations were not simple;
- Castor had many financing and investing activities;
- Information about these activities and their effects on cash resources were neither readily apparent from the other financial statements nor disclosed in the notes[501].

[533] In its own internal material, C&L expressed the opinion that section 1540.19 would apply in very rare situations, almost never achievable by a company with active business operations (such as Castor).

> "Paragraph 1540.19 of the handbook permits the omission of a separate statement of changes in financial position where the presentation of cash flows in a financial statement format would not provide additional useful information. In such situations, it is not necessary to include a note explaining why a separate statement has been omitted. **We expect the instances where this is acceptable to be very rare and almost never achievable by a company with active business operations**[502]." (Emphasis added)

[534] Moreover, in the same internal material, C&L acknowledges the necessity to qualify the audit opinion paragraph in those circumstances:

> "If a separate statement of changes in financial position is not presented, the scope paragraph that the audit report should be silent with respect to changes in financial position, however the opinion paragraph should clearly state whether the financial statements present fairly the changes in the company's financial position in accordance with GAAP. If the effects of financing, investing and operating activities on cash resources are not adequately disclosed in the notes or apparent in the other financial statements, the audit report should be suitably qualified[503]."

[535] The key underlying fact that leads to Vance's criticism of the Castor financial statements in relation to not using a SCFP is the non-disclosure of capitalized interest and the fact that there just was not a disclosure of cash from operations.

[536] Vance opines that the SCNIA provided by Castor did not meet the requirements of Section 1540 of the CICA Handbook. Selman acknowledges that Vance may be right.

[537] Castor's financial statements were in breach of GAAP in that they did not follow the italicized recommendation contained in the Handbook in October 1985 for a SCFP that would disclose the amount of cash generated by operations in the current year.

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[501] Vance, March 10, 2008, pp. 32-33
[502] PW-1420-1D; Vance March 10, 2008, p.37-
[503] PW-1420-1D

[538] In Castor's case, investments and mortgages were not and could not be treated as "*cash or cash equivalent*"[504].

[539] Mitchell testified as follows:

> Q. Does the statement of changes of net invested assets provide cash and cash equivalents derived from operations?
>
> A. It has net assets provided from operations, but does not have cash and cash equivalents provided from operations."
>
> Q. Why is that?
>
> A. This statement is not intended to give... to provide that information. It's not a statement of changes in financial position[505].

[540] Higgins, a C&L partner who did a peer review of the 1987 Castor audit, stated:

> Q. I would like to look at the 1987 financial statements with you again, which is in file one. Based upon the financial statements before you, would you indicate to us what cash was generated from operations of Castor in 1987?
>
> A- There is no specific reference to the cash generated.
>
> Q- I understand from your previous testimony that you were aware at the time that the CICA handbook required that such disclosure be made?
>
> A- I was aware.
>
> Q- Why, based upon your audit experience, must what cash is generated from operations be disclosed?
>
> A- Generally speaking, it provides a reader of the financial statements, specifically, what cash or working capital has been generated from the operations.
>
> Q- Why is that information provided?
>
> A- It provides the reader with the amount that has been generated from operations.
>
> Q- It allows the reader ---?
>
> A- One of the elements in the review of the financial statements.

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[504] Hayes, October 31, 1995, pp. 65 to 68; Grezlak, October 21, 1996, pp.229 -230
[505] Mitchell, April 25, 1996, p. 134

Q- So it allows the reader to know whether the company will have sufficient cash flow to finance its ongoing activities?

A- It's an indicator of how much cash is being generated from operations.

Q- Did you understand, in 1988 when you did the review that Coopers standards required that such cash flow information should be disclosed in financial statements?

A- It was a requirement at the time of the CICA to prepare such a statement.

Q-You were aware of that?

A- And I was aware of that.

Q- No such information is contained in this particular financial statement?

A- The statement that was prepared was a statement of changes in net invested assets.

Q- Which does not provide the information required by the handbook?

A- It does not, specifically, refer to cash provided.

Q- Which was the recommendation of the handbook?

A- Yes, that was one of the elements to that statement,-- yes[506]."

[541] C&L collaborated with management to use a form of presentation that failed to comply with the revisions made to section 1540 of the Handbook in 1985. It was the obligation of C&L to express an opinion to the effect that the audited financial statements were not prepared in accordance with GAAP or to require management to use a SCFP in order for C&L to express an unqualified opinion. Alternatively, if management still insisted upon the use of a SCNIA, C&L was obliged to express a reservation of opinion and to disclose that the SCNIA was not in accordance with GAAP.

[542] Had C&L required a proper SCFP, same would have disclosed inflows and outflows of cash, including cash provided by operations. This would have required a disclosure of the amount of revenue recognized by Castor which was not received in cash, such as capitalized interest.

Undisclosed related party transactions

[543] No doubt related party transactions ("**RPTs**") were undisclosed in the 1988 financial statements.

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[506] Higgins, December 18, 1996, pp.110-112

[544] The Handbook defines related parties[507].

[545] Section 3840.03 of the Handbook provides:

> Parties are considered to be related when one party has the ability to exercise, directly or indirectly, control or significant influence over the operating and financial decisions of the other. Two or more parties are also considered to be related when they are subject to common control or significant influence[508].

[546] The key element that must exist is one of control over operating and financial decisions regarding the transaction between the reporting entity and the other party.

[547] Only transactions which fit that description - an auditor cannot oblige his client to disclose more than GAAP requires- but all such transactions are required to be disclosed.

[548] Given his actual role, and not because of his title, Stolzenberg had the ability to exercise control or significant influence, directly or indirectly, over the operating and financial decisions of Castor and its subsidiaries. Stolzenberg was related to Castor and its subsidiaries.

[549] Transactions between Castor and Stolzenberg[509], or between Castor and companies in which Stolzenberg had significant control or influence, were RPTs to be disclosed[510]. Castor's audited consolidated financial statements disclosed some of those transactions as RPTs[511], but not all of them.

[550] Stolzenberg was the owner of record of 612044 Ontario[512] and through it, of 97872 Canada. Stolzenberg was the incorporator, the President and a director of the 97872[513]. 612044 had pledged its shares of 97872 to secure a loan from Castor[514].

[551] Because they were subject to common control or significant influence through Stolzenberg, Castor's transactions with 97872 Canada and 612044 Ontario should have been disclosed. [515]

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[507] PW-1419-1, sections 3840.03 to 3840.08 (1988)
[508] PW-1419-1 (1988)
[509] Wightman, September 5, 1995, p. 121.
[510] Wightman, July 18, 1996, p. 90.
[511] Transactions with 606752, Wost Holdings and Wost Development
[512] PW-338
[513] PW-1102A-6
[514] PW-2908, vol.1. p.4-E-32 and PW-1102A-6
[515] PW-1102-A6 ; O' Connor, January 14, 2009; O'Connor, January 15, 2009; PW-167 Y, PW-292, PW-323, PW-324, PW-325, PW-340, PW-565, PW-566-18, PW-571-15A, PW-571-15B, PW-571-15C, PW-571-22, PW-571-23, PW-572-2, PW-572-4, PW-572-5, PW-572-10, PW-572-13-1, PW-572-27, PW-573-51,PW-573-53, PW-668-1a, PW-668-1c, PW-669-1e, PW-669-2a, PW-669-3a, PW-1101, PW-1102, PW-1103, PW-1159-A-1, PW-2400-88, PW-2400-104,PW-2400-112,PW-2400-118, PW-

[552] Stolzenberg had the ability to exercise, and did exercise significant control or influence on Trinity Capital Corporation ("**Trinity**")[516]. Because they were subject to common control or significant influence through Stolzenberg, Castor's transactions with Trinity should have been disclosed[517].

[553] Given their actual role, not because of their titles and notwithstanding the fact that Stolzenberg had generally the final decision-making authority, Gambazzi and Bänziger had the ability to exercise control or significant influence, directly or indirectly, over the operating and financial decisions of Castor and its subsidiaries. Gambazzi and Bänziger were related to Castor and its subsidiaries.

[554] Section 3840.04 (d) provides:

> The extent to which a relationship between two parties can be clearly perceived will vary, but the most commonly encountered and easily identifiable related parties of a reporting enterprise would include the following:
>
> (...)
>
> (d) management: any person(s) having authority and responsibility for planning, directing and controlling the activities of the reporting enterprise. Thus, in the case of a company, management would include the directors, officers and other persons fulfilling a management function;

[555] In fact, Castor, as well as C&L, considered all shareholders and directors to be parties related to Castor.

[556] Wightman testified that he considered Castor to be «*almost an investment club, so that the shareholders and the lenders were all closely connected*»[518] and «*that the directors represented the ... most of the shareholders, directly or indirectly.* »[519]

[557] Several corporate entities, both borrowers and lenders to Castor, were represented by Gambazzi, a director of CHL, a director of several of its subsidiaries and the managing director of CHIF[520].

2400-119, D-94, D-97, D-115, D-1078 ; PW-326, PW-327, PW-328, PW-566-18, PW-566-25a, PW-1103, PW-1053-23-12

[516] Finn, July 25, 2000, pp. 241 to 245, 283, 284, 287 to 292; Finn, July 26, 2000, pp.400,401, 437, 439, 462, 469, 471, 494, 495, 511 and 512; Binch, October 29, 2001, pp.30, 45; Binch, October 30, 2001, pp.197, 219, 232; Binch, October 31, 2001, pp.392,393, 394, 402, 471, 480; Vance, June 4, 2008, pp.43-46, Rosen, March 31, 2009, pp 204-210 and Selman, May 7, 2009, pp. 69-70; See also exhibits D-600, D-601, D-602, D-603, D-604, D-869, D-872, D-873, D-875, D-876, D-899, D-901.

[517] PW-1419-1, 3840.03 and 3840.10 (1988); PW-1419-2, 3840.03 and 3840.10 (1989) and PW-1419-3, 3840.03 and 3840.10 (1990)

[518] Wightman, February 8, 2010, p. 173

[519] Wightman, October 11, 1995, p.69

[520] PW-2908, Vol. 1, pp. 4-E-33, 4-E-34.; PW-1053-22

[558] Several corporate entities, both borrowers and lenders to Castor, were represented by Bänziger, a director of CHINBV[521] who «*was tremendously involved in the operations of Castor Europe*»[522], who was part of Castor's management[523] and who had the same powers regarding CHIO as Stolzenberg did[524].

[559] Castor's files contain hundreds of documents signed by either Gambazzi or Bänziger such as loan agreements, promissory notes, pledge agreements, audit confirmations, and commitment letters. In some instances, Gambazzi signs «in trust» but in many other instances there is no indication of «in trust»[525].

[560] For disclosure purposes, when one of the parties to a transaction is acting through a person acting "in trust", it is not the relationship between the person acting "in trust" and the reporting entity that matters, but the relationship between the actual parties to the contracts – i.e. the principals. There is therefore no automatic reportable relationship between two entities when a person acting "in trust", who is director of the first entity, is acting for a second entity, even when he sits on the Board of that second entity and is therefore also presumed to be related to it. Both entities will be related if and only if the person acting "in trust" has the actual ability to exercise control or significant influence, directly or indirectly, over the operating and financial decisions of both entities.

[561] Because Gambazzi and Bänziger signed loan documents and audit confirmations on behalf of offshore borrowers and lenders, and because of Gambazzi and Bänzinger's respective role regarding those offshore borrowers and lenders, which allowed them to exercised control or significant influence, directly or indirectly, some transactions between Castor or its subsidiaries and those offshore borrowers and lenders should have been disclosed as RPTs.

[562] Gambazzi was a close personal friend of Stolzenberg and acted on his behalf[526] in related entities that Stolzenberg owned or controlled or in which he had an interest, and which had transactions with Castor and its subsidiaries.

[563] CHIF made loans to companies in which Bänziger was involved, such as Investamar[527]: These transactions were not disclosed as RPTs and they should have been.

> On page B46 of the CHIF 1988[528] working papers in connection with two loans to Investamar S.A., the following notation appears :

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[521] PW-2400-34.; PW-2282;
[522] Wightman, September 7, 1995, pp. 138-139 and September 8, 1995, pp. 42 and 46. See also PW-1053-63C-4, PW-2400-34 and PW-2400-42
[523] PW-1053-91-2, PW-10
[524] Zampelas, March 15, 1999, p. 12; PW-931.
[525] PW-1496-4-88-N-1C
[526] PW-1053-49, seq. p. 264
[527] Jean Guy Martin, August 26, 1996, p.84

> *"This shortfall on the other loan is acceptable as the company is Mr. E. Bänziger".*

[564] It is highly probable that much more needed to be disclosed given the numerous and strong indicia revealed by the evidence[529] but, more than 20 years later, indicia are not enough to reach final conclusions. However, and not surprisingly, Defendants wrote in their written argument submitted on July 8, 2010:

> Defendants acknowledge that based on the partial record before the Court, there is a possibility that the disclosure in the 1988 financial statements did not meet GAAP in that some transactions that now appear to have related party indicators may have been RPTs.

Artificial improvements of liquidity and undisclosed restricted cash

[565] Castor's liquidity was artificially improved in the 1988 consolidated audited financial statements as a result of the following elements:

- The maturities used in notes 2, 3 and 4;
- The 100 million debentures transaction;
- The undisclosed restricted cash in the amount of $US 20 million.

Liquidity improvements (notes 2, 3 and 4)

Positions (in a nutshell)

Plaintiff

[566] Plaintiff argues:

- Notes 2, 3 and 4 to the 1988 consolidated audited financial statements were materially misleading and disclosed a false picture of liquidity matching and solvency.
- The maturity notes conveyed to the reader that there was good maturity matching but in reality, it was just the opposite. There was no reasonable expectation that the loans included as "current" would be or could be repaid during the current year.

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[528] PW-1053-91-8, seq. p. 241. See also same kind of annotation in the 1989 AWP – PW-1053-89-6, sequential page 257).

[529] See Vance, March 12, 2008 pp. 50 and following (discussions on the YH and the DT Smith group) Vance, May 12, 2008, pp.197 and following; Vance, June 4, 2008, pp. 118 and following; see also the testimony and the written report of Levi

- Maturity dates of various assets (loans receivable) and liabilities (loans payable) were altered during the audit; changes, unsupported by audit evidence, were accepted by C&L to the maturity dates. By advancing the due date of various receivables before their actual due dates and by extending the due date of various liabilities beyond their actual due dates, Castor improved its apparent liquidity position.

Defendants

[567] Defendants argue:

- Plaintiff's experts have misread the notes to the financial statements. Vance and Rosen have asserted that these notes were misleading because they were possibly incorrect with respect to the amounts shown as maturing in future years, and because they misled the reader into believing that Castor was going to receive as much as 70-80% of its revenue in cash within the next year, whereas in reality, Castor's assets were not that liquid. Rosen described the mismatch as being between long-term lending and short-term borrowing.

- Defendants submit that Plaintiff's experts are attempting to read something into the financial statement notes that is not there, nor required to be there. Rosen and Vance confused the concepts of "maturity" and "liquidity".

- Plaintiff has failed to demonstrate that the disclosures as to contractual maturity dates made in the 1988 financial statements were not materially correct.

    - For the vast majority of transactions, the evidence demonstrates that the note disclosure was accurate.

    - The only significant transaction for which there is inadequate evidence to determine whether the note was accurate is the transaction involving Gambazzi. Plaintiff could have met his burden of proof by calling Gambazzi. He did not and, therefore, the Court should draw an adverse inference in this respect.

Evidence – Maturity matching notes 2, 3 and 4

[568] The 1988 overseas Matters for Attention of Partners ("**MAPs**"), sent to Wightman, addressed the issue of "matching of maturities" as follows:

> «When reviewing the CHI N.V. and CHI B.V. consolidated financial statements, it is difficult to judge whether or not the companies will be able to meet their obligations when they come due as the intercompany account must be used to offset the shortfall. Therefore, a liquidity matching should be prepared on a

consolidated basis in Montreal (asset vs. liability maturities) to ensure that the Castor group as a whole are in a good position. »[530]

[569] Thus, C&L prepared a consolidated liquidity schedule[531] for Castor and reported the results in the 1988 MAPs[532].

[570] Since Castor prepared a non-classified balance sheet in order to evaluate the company's short-term obligations as well as its ability to meet these obligations, one had to refer to the Maturity Notes[533]. As a matter of fact, and to prepare their liquidity test which was a crucial aspect to consider[534], that is exactly what C&L did[535].

[571] On the basis of the content of these Notes, several of the experts, including Defendants' expert Selman as well as witnesses from C&L, indicated that Castor had no liquidity problem[536]. Selman's answer included the following reserve "*providing the loans that they were using had the value that they were being carried at*[537]" – a premise which, in Castor's case, was part of the "appearances" but not part of the "reality", as discussed earlier and further in the present judgment.

[572] Castor's intent, with respect to the Maturity Notes was evidenced by:

- their promotional materials[538];
    - For example: "*The short term nature of Castor's portfolio and careful attention to asset and liability matching enable the Company to ensure liquidity and funding stability.*"
- the Minutes of the meetings of the Board of Directors[539];
- the supplemental information packages prepared to assist the funding officers to interpret the financial results when they were meeting with lenders and potential lenders;
    - For example: «compares the maturity structure on the assets side to the maturity structure on the liability side, and people at times asked the

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[530] PW-1053-74, seq. p. 5;
[531] PW-1053-22, seq. p. 193;
[532] PW-1053-21, seq. p. 373,
[533] PW-2908, Vol. 1, p. 4-F-1.
[534] Hayes, October 31, 1995, pp. 88, 94, 101, 108 to 111
[535] PW-1053-22, seq. p. 351, PW-1053-17, seq. pp. 382-383, PW-1053-21, seq. p. 373, PW-1053-17, seq. p. 18, PW-1053-12, seq. p. 74; Hayes, October 31, 1995, pp.88, 94, 111
[536] For example : Prikopa, January 12, 2005, p. 65; Lowenstein, March 21, 2005, pp. 40-41; Jarislowsky, April 4, 2005, pp. 141-142; Higgins, December 18, 1996, pp. 51-54; Cunningham, December 13, 1996, pp. 96-102; Selman, June 4, 2009, pp. 223-224.
[537] Selman, June 4, 2009, pp. 223-224
[538] PW-1057-1, PW-1057-2, PW-1057-3, D-186 & D-187
[539] PW-2400-23

question «*Well, what is your liquidity exposure or liquidity risk? And this presentation addresses that question...*»[540].

[573] Selman criticized Vance's opinion that the primary purpose of the Maturity Notes was liquidity testing. He opined that they were rather intended to convey interest rate risk, which would be adjusted when the loans were rolled over and renewed[541].

[574] Selman's critic of Vance's position contradicts the evidence showing the purpose of the Maturity Notes from Castor's perspective[542]. Moreover, in order to maintain his position, Selman was forced to disagree with the C&L witnesses such as Higgins and with the explanation of these Maturity Notes that appear in the AWPs (which equate maturities with cash to be received in the coming year)[543]. When asked directly by the Court whether he was opining that C&L's conclusions in their AWPs were incorrect, Selman tried to "improve" his response by suggesting that the work performed by C&L was only a "*short-cut applying a standard commercial method of doing liquidity testing*"[544].

[575] Before the finalization of the 1988 consolidated financial statements, Bänziger suggested that changes be made to maturity dates: these changes related to the maturity dates of receivables and liabilities. Bänziger was suggesting that the maturity dates of certain receivables be disclosed at an earlier date than that shown in C&L's audit evidence and Castor's records. And he further requested that certain liabilities be shown as maturing at a later date than that shown on the audit confirmations.

[576] Vance opined that there was $134,973 of unsupported changes to maturity dates[545].

[577] Selman opined that the changes were acceptable except for a few, most of which were not material.

CHL- Skyeboat and 321351 Alberta

[578] Vance opined that CHL's loans to Skyeboat and 321351 Alberta Ltd were incorrectly reclassified as maturing in 1989 whereas external evidence in C&L's hands (confirmations and promissory notes) showed they were maturing on January 31, 1991[546].

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[540] D-1045, Schedule IV
[541] D-1295, pp. 295–296, para. 6.9.52.
[542] PW-1057-1, PW-1057-2, PW-1057-3, D-186 & D-187 ; PW-2400-23; D-1045, Schedule IV.
[543] Selman, June 4, 2009, pp. 218-219.
[544] Selman, June 4, 2009, pp. 215-224.
[545] PW-2908, volume 1, chapter 4F and revised schedule 4F-13 (PW-2908 A). On that topic, see Vance, March 12, 2008, Vance, June 5, 2008 and Vance, September 2, 2008.
[546] PW-1053, E-172 and E-174; Vance, March 12, 2008, pp.101-103

- The AWPs contain nothing that would show, or could show, why and how C&L proceeded to (or accepted) such a reclassification.

- Moreover, and as a matter of fact, in the documentation provided by Castor to C&L for the 1989 audit, on the mortgage continuity schedule, those loans were again shown as maturing on January 31, 1991[547].

[579] In the cases of Skyeboat and 321351 Alberta, Selman suggested that the maturity changes were appropriate based on letters sent by Ron Smith to those debtors on December 15, 1988, in which Smith wrote[548]:

> Letter to Skyeboat:
>
> With reference to the abovementioned grid promissory note, we hereby confirm that, notwithstanding the maturity date mentioned in the grid promissory note, the loan shall be:
>
> 1) Subject to an annual review which should take place no later than April 30th of each year, commencing April 30th, 1989; and
>
> 2) On a demand basis at the option of Castor Holdings Limited."[549]
>
> Letter to 321351 Alberta
>
> "We hereby confirm that, notwithstanding the maturity date mentioned in the promissory note, it will be subject to an annual review, and then will be on a demand basis at the option of Castor.[550]"

CHIBV- Lambert and Skyview

[580] Vance opined that CHIBV's loans to Lambert and Skyview were incorrectly reclassified as maturing in 1989 whereas evidence in C&L's hands showed that the Lambert loan was to mature in 1990 and the Skyview loan in 1993.

- The reclassification was done by Ford further to a written request received from Bänziger[551].

- The amount for Lambert represented capitalized interest and placement fees that were added to the loan balance in CHIF, a subsidiary of CHIBV. The amount of the capitalized interest and placement fees that were owed for the 1987 year, as at December 31, 1988, were paid in early 1989, before the 1988 audit was

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[547] PW-1053-19-32, E-10 and E-11; Vance, March 12, 2008, pp.101-103
[548] Selman, May 20, 2009, pp.134-136
[549] D-573
[550] D-574
[551] PW-1053-74-9

completed and those payments were noted by the auditors[552]. The remaining balance was recorded as paid during 1989 but, as will be discussed further in the present judgment, this payment was a circular movement of Castor's own cash.

- The amount for Skyview represents unpaid interest and was never paid as it was capitalized to the loan balances in Montreal.

[581] In the case of the Lambert loans, Selman suggested that the maturity changes were appropriate for the following reasons:

- capital and interests have to be segregated;
- as per the loan agreement, interests had to be kept current;
- evidence that a circular transaction would have taken place in 1989 is irrelevant – in relation to decisions to be taken by the auditors for the 1988 financial statements, it would constitute hindsight[553].

[582] In the case of Skyview, Selman acknowledged that it was a mistake to change the maturity date; he indicated that the amount was dealt with through a CHL account[554] and he added that the amount was not material[555].

CHIO – DT Smith – Tennis Court Villas and Wood Ranch

[583] Vance opined that CHIO's loans to DT Smith for the Wood Ranch and Tennis Villas projects were incorrectly reclassified as maturing in 1989 while they were originally shown as maturing in 1990[556].

- The reclassification was done by Ford further to a written request received from Bänziger[557].
- In the working papers, the maturity date was shown as 1990[558].
- Confirmations sent and received showed a maturity date of 1990[559].
- D.T. Smith's own auditors (Rogoff – Strassberg) had sought confirmation from CHIO of the loans, shown on DT Smith's financial statements as payables, and

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[552] PW-1053-91, sequential pages 231-232 (B-36 and B-37); Vance, March 12, 2008, pp.108 and following
[553] Selman, May 20, 2009, pp.137 -141
[554] PW-167T
[555] Selman, May 20, 2009, pp. 153 and 154 and D-1295, pages 282-283
[556] Vance, March 12, 2008, pp. 113 and following
[557] PW-1053-74-9
[558] B-3, B-5, B-7 and B-11
[559] PW-1133B, Bates numbers 2067 and 2069 and numbers 2072 and 2074

both confirmations received from CHIO showed Wood Ranch and Tennis Court Villas' loans as maturing on October 31, 1990[560].

- The AWPs contain nothing that would show, or could show, why and how C&L proceeded to (or accepted) such a reclassification.

[584] In the case of Tennis Court Villas, Selman agreed with Vance that the agreements called for a 1990 maturity date[561]. However, Selman added that same agreements included a provision requiring early payment in order to release CHIO's rights against the units that were sold and, therefore, he qualified the issue as follows:

> The issue for the auditor faced with the client's assertion that the acceleration clause such as this one existed and will become operative is whether that anticipation that the client can be supported by persuasive audit evidence[562].

[585] Selman suggested that the provision had "*to be read as an agreement to a reciprocal change in the date payment in the event of the specific change circumstances of a sale of a lot-by-lot basis*"[563]. He invited the Court to look at "*how much information there actually was with respect to the sale of lots*"[564].

[586] In the case of the Wood Ranch project, Selman mentioned there were comments in his written reports[565] but he did not expand at all on that topic, in examination in chief[566].

[587] In his report D-1295, Selman wrote "*I will deal with the issues that this raises under Tennis Court Villas. My general comment there have equal application here.* "[567]

[588] Selman acknowledged that he could neither say if the documents he was looking at were seen by Ford nor point out what Ford might have looked at[568].

[589] In both cases, Tennis Court Villas and Wood Ranch, Selman mentioned that he would have liked to see more information for the revisions[569] and in cross-examination, on June 10, 2009, he made it clear that he had not opined that the changes were acceptable.[570]

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[560] PW-1118-6-1 and PW-1125-11-1
[561] Selman, May 20, 2009, p.156
[562] Selman, May 20, 2009, p 157.
[563] Selman, May, 20, 2009, pp. 157-158
[564] Selman, May 20, 2009, pp. 158-164
[565] Selman, May 20, 2009, p.154; Selman, May 21, 2009, p.68
[566] Selman, May 20, 2009 and Selman, May 21, 2009
[567] D-1295, para. 6.9.23, p. 283
[568] Selman, June 10, 2009, p.136, 143, 148
[569] Selman, May 21, 2009, p. 68; Selman, June 10, 2009, pp.136 and following
[570] Selman, June 10, 2009, pp. 205-206.

CHL- National Bank, Société Générale and Caisse Centrale Desjardins

[590] Vance opined that CHL's liabilities to various banks which were initially indicated as being due either on demand or in 1989 were incorrectly revised to show maturity dates of 1990 or 1991.

- CHL's liability to National Bank of Canada was revised to March 13, 1991[571].
    - The confirmation signed by the National Bank indicated February 17, 1989 as the maturity date.[572]
    - The AWPs contain nothing that would show, or could show, why and how C&L proceeded to (or accepted) such a reclassification[573].
- CHL's liabilities to Société Générale (Canada) were revised to January 19, 1991[574].
    - The liabilities were composed of an operating loan, in the amount of $1,945,320 at year-end, and of two term loans totalling $6.8 million at year-end ($4,276,228 plus $2,531,490)[575].
    - The confirmations signed by Société Générale (Canada) indicated March 21, 1989 for the operating line and March 28, 1989 for the two term loans.[576]
    - The AWPs contain nothing that would show, or could show, why and how C&L proceeded to (or accepted) such a reclassification[577].
- CHL's liabilities to Caisse Centrale Desjardins were revised to April 30, 1990 and April 13, 1991[578].
    - There were two liabilities to Caisse Centrale Desjardins: 7.5 million and 5 million.
    - The term of the 7.5 million was, initially, December 31, 1988[579] but it was extended to February 28, 1989[580].

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[571] PW-1053-25-1 BB-101
[572] PW-1053-25-7, sequential page 148 (BB 236)
[573] Vance, March 12, 2008, pp.122 to 126
[574] PW-1053-25-1, sequential page 49 (BB 101)
[575] PW-1053-25 and D-563 and D-564
[576] PW-1053-25-7, sequential 151 to 153 (pages BB 239, BB 240 and BB 241); Vance, September 2, 2008. pp. 99 and following.
[577] Vance, March 12, 2008, p.122
[578] PW-1053-25-1, BB-102 (sequential page 51) and BB-103 (sequential page 53)
[579] D-567-1 and D-567-1, Appendix 1; Vance, September 2, 2008, pp.48 and following. See also PW-2483 and PW-2484
[580] PW-2485 (see also PW-2485-1 and PW-2486)

- The term of the 5 million is "on demand".
- The confirmations signed by Caisse Centrale Desjardins indicated
  - for the 7.5 million loan : February 28, 1989.[581]
  - For the 5 million loan: On demand.[582]
- The AWPs contain nothing that would show, or could show, why and how C&L proceeded to (or accepted) such a reclassification[583].
- It was totally reimbursed in 1989[584].

[591] In the cases of the loans payable by CHL to National Bank, Selman opined that the changes were acceptable based on:

- The evidence[585] concerning the computer systems in use – since they were not programmed to distinguish between maturity date of capital and due dates of interest instalments, the confirmations that had been sent out did use the interest payment due dates instead of the contractual maturity dates[586].
- The evidence concerning the various facilities.[587]
- The capacity of CHL to rollover[588] and the general GAAP rule of looking at the substance of things rather than looking at their form[589].

[592] To conclude in such a way, Selman said the following about the confirmation process:

> the confirmations were for the purpose of providing assurance as to the existence of the loans and the amounts of the loans, the amounts owing, that's the purpose of confirmations. So the fact that the confirmations showed interest due dates was no more than to assist the Bank to situate itself in terms of what the amount was that it was being asked to confirm, because it included the interest.

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[581] PW-1053-25-7, BB 155 and BB 196
[582] PW-1053-25-7, sequential page 105
[583] Vance, March 12, 2008, p.122
[584] PW-2921
[585] Simon, April 28, 2009, 218 to 221, 226, 232 to 237 and 245 to 256; PW-1053-18-3; (D-1295, pp. 286 and following - see also PW-1053-12 and D-333-1)
[586] Selman, May, 20. 2009, pp.188 and following
[587] D-562 (National Bank credit facilities)
[588] Selman, May 20, 2009, pp. 195-196
[589] Selman, May 20, 1989, p. 196

> The confirmations didn't have the purpose of providing the evidence for the maturity schedules in the financial statements (...)
>
> in my view, that those confirmations were not reliable audit evidence as to the maturity dates of the loan and there wasn't a contradiction[590].

[593] Selman acknowledged that one of the notes concerned the "facility B" and that in 1989 Castor treated that as a "*short term facility*", but he said they did not have to[591].

[594] Selman said that Vance's position was also acceptable but that it was wrong for Vance to opine that his view was the only one acceptable in those circumstances[592].

[595] Selman summarized his understanding and his views on Vance's position regarding note 2 as follows:

> So Castor wasn't required to provide the information in note 2 in respect of its own lendings, but it did.
>
> But Mr. Vance won't accept the same principle with respect to note 2, which is one of the difficulties that I'm having with this, and as well, he's insisting that, when there is a short-term note within the long-term facility, when you do this table, you have to use the short-term note on the liability side, and it's inconsistent, it's illogical and it's wrong[593].

[596] In the case of CHL's loans to Société Générale, Selman explained that the facility was an "*evergreen facility*" [594] and that, therefore, there was always a legal right to use the facility for an extension[595].

> "Extendable annually at the anniversary of the loan for an additional year based on the last audited financial statements of the borrower and subject to Société Générale Canada's approval. "[596]

[597] Selman acknowledged that the note had been signed with a maturity date of 1989, but he said that under the "*evergreen facility*" the Bank could not prevent CHL from extending it to 1990[597] ; the facility included an "*events of default provision*", but the credit facilities could not be withdrawn at will[598].

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[590] Selman, May 20, 2009, pp.189-190
[591] Selman, May 20, 2009, pp. 195-196
[592] Selman, May 20, 2009, pp.198-199
[593] Selman, May 20, 2009, pp.201-202
[594] Selman, May 20, 2009, p.202; Simon, April 8, 2009, pp.174-179
[595] Selman, May 20, 2009, p.204
[596] D-563
[597] Selman, May 20, 2009, pp.204-205
[598] Selman, May 20, 2009, p.206

[598] Selman mentioned that in January 1989 Société Générale extended its evergreen facility to 1991[599] and he suggested that C&L had probably seen that since they accepted to change the maturity date from 1989 to 1991[600].

[599] However, since it was not part of the evergreen facility, Selman opined that C&L should not have accepted the change of maturity date on the operating line of 2 million with Société Générale[601].

[600] In the case of Caisse Centrale Desjardins, Selman invited the Court to look at the wording of a credit facility, another evergreen facility.

> "The nature of credit A will take the form of revolving loans for an initial period of twenty four (24) months to April thirtieth (30th), nineteen ninety (1990). During the credit period, the company will then retain the option to borrow, repay and reborrow any amounts. "
>
> "Credit A may also be extended for additional periods of twelve (12) months by mutual agreement on April thirtieth (30th) of each year, evergreen option. Should credit A not be renewed at any one of the evergreen dates, the remaining credit period would be reduced to twelve (12) months."
>
> "Credit period: this credit facility covers an initial period of twenty-four (24) months with an annual evergreen option."[602]

[601] Selman added that the wording in the case of the $5 million loan was similar[603].

[602] He thereafter looked at the wording of the facility relating to the $10 million loan to refinance existing indebtedness on the Toronto Skyline[604] - which was, in his opinion, the most relevant to the issue- and suggested that, in fact, it was a 5 year loan[605].

> "The credit facility will be for a period of two (2) years to April thirtieth (30th), nineteen ninety (1990), but may be extended at Castor's option for a first renewal period of two (2) years from May one (1), nineteen ninety (1990) to April thirtieth (30th), nineteen ninety-two (1992), and for a second renewal period of one (1) year from May one (1), nineteen ninety-two (1992) to April thirtieth (30th), nineteen ninety-three (1993)."

[603] Selman mentioned that the right to extend was subject to various conditions, namely that the ratio of first mortgage loan to value of the Toronto Skyline should not exceed 60% and that the debt service coverage ratio should not exceed 1.1 to 1[606].

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[599] D-565
[600] Selman, May 20, 2009, pp.205-206
[601] Selman, May 20, 2009, pp.207-208; Selman, June 10, 2009, p.174
[602] D-567-1
[603] D-567-3
[604] D-567-4
[605] Selman, May 21, 2009, p.23

[604] Based on the "*evergreen stipulations*", Selman opined that Castor could not have less than 2 years outstanding at December 31, 1988, because if the facility was not extended by mutual agreement at April 30, 1989, Castor still had the right to use it until April 30, 1990[607].

[605] Selman acknowledged that looking at the working papers made it difficult to reach a conclusion[608] and that he could not tell, from those AWPs, how and why the audit staff who had accepted the maturity changes had done so[609].

[606] Selman added that the notes themselves were short-term but only for the purpose of allowing an adjustment of interest rates[610].

CHIBV- White

[607] Vance opined that CHINBV's notes to the White, which initially had maturity dates of 1989, were incorrectly changed to 1990.

- There were three notes totalling 15 million.
- These notes were not confirmed, but internal records of Castor indicated February 22, 1989 as maturity date, in all cases. [611]
- On the lead sheet of the AWPs completed by the audit staff, C&L wrote «*As per Mr. Baenziger, all notes payable are of a current nature.*"[612]
- The reclassification was done by Ford further to written requests received from Bänziger[613].
- Except for the above mentioned written requests made by Bänziger, the AWPs contain nothing that would show, or could show, why and how C&L proceeded to (or accepted) such a reclassification.

[608] Selman opined that the changes were acceptable looking at Bänziger's explanations:

> "Customer number 949001, White deposits, totalling to Cdn $15 million are by special agreement due in 1990 only and not in 1989. Maturity date of 1989 is for interest calculation purposes only.[614]"

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[606] Selman, May 21, 2009, pp.23-24
[607] Selman, May 21, 2009, p. 26
[608] Selman, May 21, 2009, p. 29
[609] Selman, May 21, 2009, pp. 40-41
[610] Selman, May 21, 2009, p. 32
[611] Vance, March 12, 2008, p. 129, PW-1053-92-7 and PW-1053-92-5 sequential page 91
[612] PW-1053-92, AA-51
[613] Three letters from Edwin Bänziger to George Dragonas dated February 22, 1989 (PW-1053-74-9), February 23, 1989 (PW-1053-74-12) and February 27, 1989 (PW- 1053-74-11)

since "*it would be an odd thing for Mr. Baenziger to assert that the maturity date was nineteen ninety (1990) if the notes were in fact due the day before his request.*" [615]

[609] Selman acknowledged that he had not seen that "*special agreement*"[616] and he mentioned that he would have liked to see more information for the revision[617].

CHIBV- Gambazzi

[610] Vance opined that CHINBV's notes to Gambazzi, which initially had maturity dates of 1989 were incorrectly changed to 1990.

- Those notes totalled 25 million.
- All the confirmations showed 1989 maturity dates.[618]
- On the lead sheet of the AWPs completed by the audit staff, C&L wrote «*As per Mr. Baenziger, all notes payable are of a current nature.*[619]»
- The reclassification was done by Ford further to written requests received from Bänziger[620].
- Except for the above mentioned written requests made by Bänziger, the AWPs contain nothing that would show, or could show, why and how C&L proceeded to (or accepted) such a reclassification.

[611] Selman testified that he could not find any explanation for the maturity change in the case of the notes to Gambazzi in the amount of 25 million[621].

[612] Selman also said:

> I really have nothing to add to the paragraph[622]. I've seen no support or explanation for the change in the Gambazzi deposit. It may be correct, it may not be correct. At the end, the only factual matter that I think you have to consider and give some weight to is that notwithstanding that all of these notes have due dates in nineteen eighty-nine (1989), the entire fifty (50) million dollars remained outstanding at the end of nineteen eighty-nine (1989) and there was still twenty

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[614] PW-1053-74-10, sequential page 34
[615] Selman, May 21, 2009, p.66
[616] Selman, May 21, 2009, p.67
[617] Selman, May 21, 2009, p.69; Selman, June 10, 2009, pp. 136 and following
[618] PW-1133A and Vance, March 12, 2008, p.130
[619] PW-1053-92, AA-51
[620] Three letters from Edwin Bänziger to George Dragonas dated February 22, 1989 (PW-1053-74-9), February 23, 1989 (PW-1053-74-12) and February 27, 1989 (PW- 1053-74-11)
[621] Selman, May, 20 2009, p.133
[622] D-1295, page 294, para. 6.9.47

> (20) million of it outstanding at the end of nineteen ninety (1990). So, in fact, it continued to be an outstanding amount, but I don't have any support for it.[623]

CHIBV- Pinecrest

[613] Vance opined that the maturity date change in the case of Pinecrest, from 1989 to 1990, was incorrectly done.

- No substantial audit was performed.
- On the lead sheet of the AWPs completed by the audit staff, C&L wrote «*As per Mr. Baenziger, all notes payable are of a current nature.*[624]»
- The reclassification was done by Ford further to written requests received from Bänziger[625].
- Except for the above mentioned written requests made by Bänziger, the AWPs contain nothing that would show, or could show, why and how C&L proceeded to (or accepted) such a reclassification.

[614] In a nutshell, on Pinecrest's situation, Selman opined as follows:

> Information that we did have substantiated, strongly substantiated, the... or provided a foundation for the recommendations that Mr. Dragonas received from Mr. Baenziger that these deposits be considered for reclassification. Mr. Vance has some reservations respect to the three hundred thousand (300,000) US deposit.[626]

[615] Selman indicated that when the note was paid it was paid to Pinecrest[627].

CHIBV - Bayerische Bank

[616] Vance opined that the CHINBV's liabilities (bank loans) to Bayerische Bank (total of $13.6 million) were incorrectly reclassified with a 1990 maturity date instead of a 1989.

- Bayerische Bank confirmations indicated the following maturity dates: January 9, 1989 and January 31, 1989[628], as recorded in Castor's own records[629].

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[623] Selman, May 21, 2009, p.67
[624] PW-1053-92, AA-51
[625] Three letters from Edwin Bänziger to George Dragonas dated February 22, 1989 (PW-1053-74-9), February 23, 1989 (PW-1053-74-12) and February 27, 1989 (PW- 1053-74-11)
[626] Selman, May 21, 2009, pp.64-65
[627] PW-145-A, Bates number 55919
[628] PW-1133A, at Bates 1545
[629] PW-805 and PW-807

- The reclassification was done by Ford further to written requests received from Bänziger[630].

- Except for the above mentioned written request made by Bänziger, the AWPs contain nothing that would show, or could show, why and how C&L proceeded to (or accepted) such a reclassification.

- As a matter of fact, Castor did reimburse Bayerische Bank at the indicated maturity dates in January 1989[631], even before the audit was completed.

[617] Selman opined that the change was acceptable in light of the stipulations of the credit facility in force[632].

> "The facility shall terminate on April 30, 1990."[633]

CHIBV - Berliner Bank

[618] Vance opined that the CHINBV's liabilities (Bank loans) to Berliner Bank (total of $5.965 million) were reclassified with a 1990 maturity date instead of a 1989.

- Berliner Bank confirmations indicated maturity dates in March, 1989. [634]

- CHIFNV's original agreement with Berliner Bank provided that borrowings were for a maximum period of 6 months and for payments at maturity date, absence of payment being an event of default[635].

[619] Selman opined that the change was acceptable in light of the wording of the credit facility in force. [636]

> "The facility may be drawn and unless an event of default has occurred and is continuing before the date of such drawing, in amounts of no less than US $1 million or the equivalent in other convertible currencies, for periods of one, three or six months, no period ending later than six months after the end of the availability period, i.e. March 5, 1990."[637]

Ford's testimony

[620] On September 6, 1996, Ford testified at length on the maturity matching issue, namely of the following facts:

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[630] PW-1053-74-9, sequential pages 42 and 46 to 57
[631] PW-805 and PW-807
[632] Selman, May 21, 2009, pp. 73 and following
[633] PW-1053-74, sequential pages 46-60 (namely page 50)
[634] PW-1133A, Bates number 1568
[635] PW-2924
[636] Selman, May 21, 2009, pp.75-79
[637] PW-1053-74, sequential page 58

- Bänziger wrote three letters (February 22, 1989, February 23, 1989 and February 27, 1989) – copies of which were in the AWPs in front of her[638], but she could not say how copies of those letters came into her possession[639] - she could not say if those were handed to her – she could not say who would have handwritten "*To Maribeth*" on the copy of the February 27, 1989 memo[640] ;

- She made all the maturity changes that Bänziger was suggesting in his three letters[641];

- She neither verified with Bayerische Bank nor with Berliner Bank the proposed change in maturities[642];

- The only documentation she can show in support of any of the changes that were proposed and that she made are the letters received from Bänziger with the attached documents[643];

- For the Lambert loan, she reviewed her working paper on B-36 and noted that the 1987 interests had been paid in January 1989 – a fact that supported Bänzinger's position that those amounts (interests) were current – she did not ask for further documents[644];

- In the Skyview review file, B-43, she noted that interest was generally payable monthly – that would be considered an amount in a current status. The only month that was outstanding was December. She did not trace payment to cash and she was not aware interest were paid through an increase of a loan made in CHL[645];

- She could not recall any other procedure she would have performed[646];

- She could not recall what information she had to reclassify in the Wood Ranch loan, but she did [647]; Wood Ranch loans had been confirmed with a maturity date of October 31, 1990 – she had so written into her AWPs after a verification

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[638] Ford, September 6, 1996, p. 133
[639] Ford, September 6, 1996, p.167
[640] Ford, September 6, 1996, p. 180
[641] Ford, September 6, 1996, pp. 133 and following
[642] Ford, September 6, 1996, p. 123
[643] Ford, September 6, 1996, pp.129, 172, 178
[644] Ford, September 6, 1996, pp. 127-128
[645] Ford, September 6, 1996, pp.128-129
[646] Ford, September 6, 1996, p. 137, 171
[647] Ford, September 6, 1996, p.132

of the loan file[648]; she did not communicate directly with the borrower (DT Smith)[649];

- She acknowledged that instead of being repaid in 1989, the balances of the loans to Wood Ranch increased during 1989 by almost 10 million[650];

- She was not prepared to attest to the fact that the three letters and the attached documents from Bänziger were the only documents she saw – she maintained she would have seen other documents which would have allowed her to be satisfied that the classification recommended by the client was proper – she could not remember specifically what other documents she would have seen – what questions she would have asked - she could not remember any procedure she would have performed[651];

- She acknowledged that there were neither documents in her file nor documents that she would have reviewed during the course of her field work that would have indicated that the maturity date for the Tennis Court Villas could be anything but 1990 – she said that if she had seen any such documents during her field work, she would have changed the maturity date then[652];

- She had no recollection of discussing the proposed changes of maturities with Stolzenberg[653];

- She acknowledged that Bänziger was the person who had represented to her colleague Janet Cameron that the maturity date for the White's notes was 1989 – that Cameron's work showed that (AWP : AA-51) and that the same Bänziger was a few weeks later representing otherwise (maturity in 1990)[654];

- Stolzenberg and Bänziger were provided with the drafts of the financial statements of the companies she was working on– she did not recall anything to the effect that they would have been disappointed in the maturities that were reflected in Notes 2, 3 and 4[655];

- According to all the records she had, including the field work done, Gambazzi's notes were maturing in 1989[656]; she never discussed that specifically with

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[648] Ford, September 6. 1996, pp. 137-138
[649] Ford, September 6. 1996, pp. 138-139
[650] Ford, September 6. 1996 p.141
[651] Ford, September 6, 1996, pp.129,131, 147,148, 149, 171
[652] Ford, September 6, 1996, p.149
[653] Ford, September 6, 1996, p. 144
[654] Ford, September 6, 1996, p. 170
[655] Ford, September 6, 1996, pp. 174-175
[656] Ford, September 6. 1996, p. 181

Gambazzi – she never had communication with Gambazzi concerning reclassification of maturity[657].

[621] At trial, on the maturity issue, Ford testified as follows:

- The maturity dates at note 3 brought forward for Castor overseas subsidiaries reflected the date of the principal balance[658].
- When she performed her audit work, she was not aware that all records of actual sales, including sales reports, were kept in Castor's files in Montreal[659].
- She was never advised that Ron Smith was the contact person for the DT Smith loans[660].
- She never discussed the DT Smith projects with Ron Smith[661].

[622] At trial and for the first time (in 2010), Ford maintained that she had received further information and consulted other documents during meetings with Goulakos[662]:

> Extracts of December 7, 2009
>
> Q-First of all, with respect to nineteen eighty-eight (1988) audit, when you came back in February nineteen eighty-nine (1989), did you go to Castor's premises?
>
> A- Yes, I did.
>
> Q- Okay. And when you went to Castor's premises, for what purpose did you go to Castor's premises and what did you do there?
>
> A-There were a couple of reasons I went to Castor's premises, one was to be able to interact with the Coopers & Lybrand team doing the Castor Montreal year-end file to clear off some of the intercompany balances that were required in completing my work, as well as any other information that might have not been available to me in Europe and that had been now sent to the offices that I could review on site.
>
> Q- When you say "to the offices", you're referring to?
>
> A- To Castor's offices in Montreal.
>
> (...)

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[657] Ford, September 6. 1996, p. 182
[658] Ford, December 10, 2009, pp. 87–91 (namely on page 91).
[659] Ford, December 8, 2009, p. 171
[660] Ford, December 9, 2009, pp. 127-128
[661] Ford, December 8, 2009, 186-188; Ford, December 10, 2009, pp. 16-32
[662] Ford, December 7, 2009, pp. 186-226; Ford, December 8, 2009, pp.80-98

A- (...) I had discussions with respect to Socrates Goulakos, with respect to the financial statement presentation of the statements that had been issued in draft to Herr Stolzenberg on February fifteenth (15th), nineteen eighty-nine (1989), a draft set of financial statements was sent to the client.

Subsequent to that, Herr Stolzenberg and Herr Baenziger had requested some changes that would be required or would be requested with respect to respect to those financial statements and for me to follow up on the presentation that was being requested, I had to sit down with Socrates Goulakos, discuss those changes and also be provided with suppor ting evidence for those changes.

Q- And did they relate to areas such as maturities?

A- Yes, they do. (...)

Q- And with respect to Mr. Dragonas, did you have any dealings or interactions with Mr. Dragonas?

A- Not with Mr. Dragonas directly, no.

Q- During any of those three years?

A- No, I did not.

Extracts of December 8, 2009

Q-(...) and I'd like you to explain to the Court, the manner in which you proceeded to deal with these changes that appear in the letter of February twenty-second (22nd), twenty-third (23rd) and twenty-seventh (27th). (...)

A- I would have had my working paper files that I had prepared in Europe with me. I would have looked at and we had the information that was being proposed as potential changes to classifications of the financial statements. I would have then looked and seen and gone through the various confirmations that I would have received from Geneva to see if any of those changes had been confirmed on a confirmation, yes or no, and then I would have sat down with this letter and George... Socrates Goulakos, and sat down with him in the offices of Castor in Montreal, to go through the proposed changes to the maturities, and there he would have had either documentation available to me at the time that I went on my first meeting, or he would have had to ask Herr Baenziger and Herr Stolzenberg for support with respect to those changes.

Some of the evidence was provided with the original document that was sent by Herr Baenziger to Mr. Dragonas and Mr. Goulakos at the time, and some of that information would have been sufficient for my purposes and some of the points, I would have had to have followed up with Goulakos at the end of the... with each individual memo.

Q- Okay. Now, when you're saying that some of the information was found in the communication that you received, you're referring to what?

A- There are sequential pages that continue on from the original letter from Edwin Baenziger, 44, 45, 46, 47, 48, 49, all the way through to, I believe, 58, and those... and I believe Edwin Baenziger also mentions in his letter that he's included certain documents with that letter.

(...)

Q-... these are confirmations that emanate from CH International Overseas.

A- That's correct.

Q- And these are the type of confirmations that were not generated by a computer?

A- They were typed by the client representative, yes.

(...)

Q-Are you able to read it, because on the copies, they don't...

A- It's under point 7.2, and it says: "*The facility shall terminate on April 30, 1990.*"

(...)

Q- Yes, I believe it's Bayerische Vereinsbank (inaudible).

A- Yes. What it's stating is that the original confirmation that went out and contained a date that showed in nineteen eighty-nine (1989) as being the due date. However, he's showing evidence that the actual true maturity date is in nineteen ninety (1990), by showing... providing a copy of the actual loan agreement with respect to that particular facility.

Q- Okay. And with respect to the Berliner Bank, which is sequential page 58, I note that the content is... the language used is German and this particular matter was being addressed to... First of all, is this a confirmation which is sequential page 58, or it's...

A- No, this is correspondence with respect to... from the Berliner Bank to CHI International NV, with respect to a particular loan position, and he's basically sending them a signed copy of the changes made to the original agreement which was dated nineteen eighty-six (1986).

Q- Okay. So, based on this, what is your understanding with respect to the maturity of the facility?

A- On page number 59, sequential page 59, again, there's a highlighted before point number 8, "Representations", it says that for a period ending later than six (6) months at the end of the (inaudible) period, i.e. March fifth (5th), nineteen ninety (1990).

Q- And this is again also... it's the full agreement between... Yes. These are changes, these is a supplemental agreement number 2, so that's the full supplemental agreement number 2 with respect to that particular loan facility. So, these ones, he provided at the time that he sent the original fax to Mr. Dragonas and that was given to me at the time as a copy, so I have photocopied and maintained the whole package intact in the file.

Q- And with respect to the remaining items that are dealt with on pages 1 or 2, which are sequential pages 41 and 42, as well as the following exhibits which are sequential page 39 and sequential page 38, how did you proceed and on what documentary evidence did you rely upon in order to accept the changes that appear on these documents?

A- I would have been at the offices of Castor in Montreal discussing these with Socrates Goulakos and he would have provided me with on-site documents relating to the specific recommendations for changes and classification that Herr Baenziger was proposing, and I would have reviewed those documents on site with Socrates Goulakos and noted that the changes were appropriate and therefore, made the changes to the notes 2, 3 and 4 of the financial statements.

Q- Now, could you explain to the Court why you did not include in the audit working paper the documentary evidence that you consulted that allowed you to accept the changes shown on the documents that we have reviewed, the three (3) separate... the two (2) letters and one (1) memo?

A- It would be similar to when I was reviewing appraisals, where I didn't photocopy all the appraisals to support the numbers that I had inserted on the pages we looked at yesterday, I had seen the documents in front of me, I had read them, I was happy with the representations and the documents that were there, therefore I was comfortable to make the changes, and I also, if I ever needed to refer back to them, they were going to be maintained with the client, so if I ever needed further reference, they would be there for me to look at.

Relevant evidence - Other elements

[623] Ron Smith testified that neither he nor any members of his mortgage department ever met with any C&L representatives with respect to the loans to the DT Smith companies, nor was he ever asked to provide them with any information[663].

[624] Ron Smith described Castor's involvement in the financing of Wood Ranch[664]. He mentioned that the original commitment letter "*included a cash flow which projected*

[663] Ron Smith, June 10, 2008, pp.39-40
[664] Ron Smith, June 11, 2008, pp.39 and following

a sell-out date by July of nineteen ninety (1990), this is a typical twenty-four (24) month sales scenario"[665] and he mentioned the delays in construction[666].

[625] Ron Smith confirmed that the maturity dates (for the purpose of Castor's 1988 audit) had never changed[667].

[626] Ron Smith explained that there had been no closings as at February 12, 1990 in the Wood Ranch project[668] and that the Tennis Court Villas project was paid back out of the process of the auction that took place in 1990[669].

[627] David Smith testified that while such a topic would have been part of his functions and responsibilities, he had never discussed maturity dates, extension of maturity dates or advancing any maturity dates with anyone at Castor[670].

[628] David Smith confirmed that the project Wood Ranch II was also known as "Village on the greens"[671]. So did Moscowitz and Ron Smith.[672]

[629] Moscowitz described the Wood Ranch project[673] looking at the compendium PW-1118 relating thereto.

[630] Moscowitz described his functions and responsibilities with DT Smith as follows : *for each of the construction loans and land loans, developmental loans that DT Smith had with Castor, I would generally put together all of the information within the company about that property, which is where it was located, some marketing information, getting ready to do an appraisal and talk to an appraiser, and put that package together, and then meet with Ron Smith or Matt Hendel, and discuss the cash flows and the market, and together as a group we would put together a cash flow or projection*[674].

[631] Moscowitz explained that DT Smith refinanced the Wood Ranch project with Castor after delays in construction and a demand from their construction lenders, Security Pacific Bank, that DT Smith finance the cost overruns they had to face[675].

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[665] Ron Smith, June 11, 2008, p.42
[666] Ron Smith, September 24, 2008, p.101; Ron Smith, March 27, 2009, pp.188-189
[667] Ron Smith, June 11, 2008, pp.46-47
[668] Ron Smith, June 11, 2008, pp.62-63
[669] Ron Smith, June 10, 2008, p.63
[670] David Smith, March 13, 2000, pp.72-73
[671] David Smith, March 17, 2000, p.742; David Smith, October 27, 2000, p.1507, 1552
[672] Moscowitz, December 14, 1999, p. 386-387; Moscowitz, December 17, 1999, p.1045; Ron Smith, June 11, 2008, p.44
[673] Moscowitz, March 8, 2000, pp.1663 and following
[674] Moscowitz, December 13, 1999, pp 29-30
[675] Moscowitz, December 13, 1999, p.34,; Moscowitz, December 14, 1999, p.239; Moscowitz, December 17, 1999, p.1043; Moscowitz, March 9, 2000, p.2063-2064

[632] Moscowitz recognized David Smith's signatures on the confirmations sent to CHIO for the 1988 audit[676] and he confirmed that there had been no changes in the maturity date[677]. Moscowitz also recognised the confirmations from DT Smith that had been sent to CHIO for the purpose of the audit of the DT Smith companies[678].

Credibility issue –Ford's testimony

[633] Given the striking difference between her testimony at discovery and her testimony at trial, Ford's uncorroborated testimony at trial is neither credible, nor reliable.

[634] Ford was examined extensively on her work in recording maturities of loans during discovery in 1996. She was unable then to remember what she relied on or reviewed when making the changes, and it never came up that she would have had meetings with Goulakos in that respect.

[635] At trial, in 2010, almost 15 years later, and more than 20 years after the audit work was conducted, Ford asserted that Goulakos showed her documents, which justified these changes.

[636] Other examples of Ford's credibility deficit are discussed later in the present judgment.

[637] Moreover, the evidence shows abundantly the poor quality of the Ford's work– said evidence is discussed, hereinafter, under the GAAS sections of the present judgment.

Credibility issue – Selman's propositions

[638] Vance's positions on the issue of maturity matching are accepted and those of Selman are rejected when they are different from Vance's and here are the main reasons why.

[639] With respect to Wood Ranch and Tennis Court Villas, the propositions of Selman rest upon the following assumption:

> the projects were at the point, the stage, the point of sale, would be at the stage of point of sale in nineteen eighty-nine (1989), sufficiently... that would sufficiently support an expectation that the accelerati on clauses would be tri ggered.[679]

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[676] Moscowitz, December 13, 1999, p.103
[677] Moscowitz, December 14, 1999, p.385
[678] Moscowitz, December 14, 1999, pp.386-389
[679] Selman, June 10, 2009, p.149

[640] Selman relied on the acceleration clause in the loan agreements to opine that there could be a "*plausible explanation*" for the changes made to the maturity dates although Bänziger did not make reference to this clause in his letter to Ford.[680]

[641] With respect to Wood Ranch and Tennis Court Villas, as with all situations relating to Castor's overseas subsidiaries, Selman's propositions are reliant on Ford's testimony and on assessment of credibility and reliability of same.

[642] Cross-examination illustrated that Selman's comment in his written report ""*I will deal with the issues that this raises under Tennis Court Villas. My general comment there have equal application here*"[681] was likely to mislead. If Selman could rely on evidence in the Tennis Court Villas situation[682], no similar evidence was ever seen by him on Wood Ranch[683] and, as the Court noted earlier in the present judgment, Selman did not testify *viva voce*, in direct examination, on the Wood Ranch situation[684].

[643] In cross-examination, with respect to the change made for Wood Ranch, Selman was asked what audit evidence he had seen that did not support the change and he answered he had not seen any:

> A- I didn't see any audit evidence that did not sup port the change[685].

[644] His answer "*didn't see any audit evidence that did not support the change*" was followed by the following exchange :

> Q- (...) when you were doing your work, did you attempt to identify audit evidence that would be for a change, an audit evidence that would be against the change, or did you only look for audit evidence for a change?
>
> A- Well, obviously, I looked for all of the audit evidence that was available. I have not been selective about looking at audit evidence in this section or in any other section of this report. This isn't, you know, I'm trying to provide the Court with a balanced view of the situation[686] (...)

[645] Selman was asked if he had looked at the confirmations and his answer was "*Well, the audit confirmation requests are not very good evidence of maturity dates in this circumstance*"[687].

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[680] Selman, June 10, 2009, p.159
[681] D-1295, p. 283, para. 6.9.23
[682] D-169
[683] Selman, June 10, 2009, pp.148 and following
[684] Selman, May 20, 2009 and Selman, May 21, 2009
[685] Selman, June 10, 2009, p.179
[686] Selman, June 10, 2009, pp.179-180
[687] Selman, June 10, 2009, p.181

[646] He was asked if he had looked at Moscowitz's testimony and his answer was "*I don't think so. I didn't get that deeply into the D.T. Smith stuff, so I didn't read Moscowitz or David Smith's testimony with respect to all these projects, so I can't say* (...)"[688]

[647] Selman was shown exhibit PW-1118-2B and was asked if he had looked at the mortgage loan summary section which stipulated "*The maturity date shall be the later of October 31, 1990 or the 27th month from the date of closing*"[689].

[648] Selman was asked what steps the auditor should take when faced with a request to change the maturity date and his answer was "*to make enquiry of the client as to the status of the development and to establish that the client had a reasonable ground for expectation that there would be a triggering of the acceleration clause in nineteen eighty-nine (1989)*",- i.e. to ascertain from the client the stage of development of the project[690].

[649] Selman acknowledged that it would be based on the stage of development of the project that the auditor would be able to determine the likelihood of closings taking place during 1989[691]. He also acknowledged that appraisal reports would constitute audit evidence if they contained an estimate of when the properties would be completed and sold[692].

[650] Selman was presented with appraisal report PW-1118-5 dated September 26, 1988, showing that the project consisted then of rough-graded land and that construction had not even commenced except for model units. He was asked if that was a factor that made it less likely that there would be actual closings during 1989 (to trigger the acceleration clause). His answer was:

> I view it as neutral, totally neutral. That doesn't tell you anything one way or the other. You've got fifteen (15) months from the date of that appraisal to build out and complete a hundred and fifty-six (156) units townhouse project. That's, in my experience in construction, a relatively long period of time to do it[693].

[651] Selman was presented with exhibit PW-1114-10 dated March 1989, which contains a section entitled "*Construction status*" (item 3) stating ""*Foundations will start in approximately 45 to 60 days*". He was asked if this piece of information would have affected his determination as to whether or not it was reasonable that there would be closings taking place in 1989. His answer was :

> I don't know. Somebody has written in here "When will first closings take place? August, 10 September?". I mean, this is California, there's no building season,

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[688] Selman, June 10, 2009, pp.181-182
[689] Selman, June 10, 2009, pp. 183-184
[690] Selman, June 10, 2009, p 186
[691] Selman, June 10, 2009, p.186
[692] Selman, June 10, 2009, p.186
[693] Selman, June 10, 2009, p.188

> things start and progress in a straight line, because there's no weather issues, unlike here, for example, or Canada generally. So, could they have completed these or not completed these, I can't tell you from this document[694].

[652] Selman was presented with exhibit PW-1118-8, a document dated February 12 1990 establishing that 33 units had been sold but that none had closed (as of that date). He was asked whether he had taken that information into account in the course of his work to determine the plausibility of payments being made on the Wood Ranch II loans during 1989 in application of the acceleration clause. His answer was:

> And I'll give you the same answer that the documents I took into account did not include a detailed review of all the documents that existed in the D.T. Smith file of documents
>
> (...) I wasn't aware of that, that is correct. I wasn't aware of it when I wrote this portion of the report.[695]

[653] With respect to the Tennis Court Villas project, to support his views that the application of the acceleration stipulation should be considered, Selman referred to a memo dated September 11, 1989[696] and made reference to units sold (46) notwithstanding that only closings would trigger a repayment. As noted in that memo, only 3 units had closed. When Selman was asked why he had not mentioned in his report that only 3 units had closed, he said:

> My Lady, I looked at the document, there's a limit to how much detail about every exhibit I can put in a report, you know, if I tried to do that with every exhibit, pros and cons of an exhibit, I'd end up with a report that I couldn't possibly have prepared for you in the very busy time during the last summer when there was a strong amount of pressure from counsel to get a report to you because you wanted to read it over the summer. There's a limit to how much detail I can put in it[697].

[654] In both cases (Wood Ranch and Tennis Court Villas), Selman downplayed the importance of third party evidence such as audit confirmations[698] and failed to consider the testimony of Moscowitz and David Smith who were unaware of changes to the maturity dates[699].

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[694] Selman, June 10, 2009, p.202
[695] Selman, June 10, 2009, pp.202-205
[696] D-169
[697] Selman, June 10, 2009, pp.157-158
[698] Selman, June 10, 2009, p.181
[699] Selman, June 10, 2009, pp.181-182, 189, 204 and following

Conclusions

[655] Maturity dates, on both sides of the balance sheet - assets and liabilities- had to be the contractual due dates at year-end, not some random dates of expected future payment made after likely rollovers.

[656] Maturity dates on loans payable to Castor could not be changed unilaterally by Castor – Castor's debtor had to agree. Ron Smith could not change the contractual rights and obligations of Skyeboat and 321351 Alberta, namely the maturity date, by simply sending letters to those debtors[700].

[657] Castor could not reasonably expect Lambert to repay the interests in 1989 given the history of that file – as a matter of fact, evidence shows (as discussed later in the present judgment) that the payments that were made on the Lambert file in 1989 were a cash circle.

[658] Selman acknowledged that the changes requested by Bänziger required corroboration[701] : C&L neither looked for nor obtained corroboration.

[659] In case of contradictory evidence, C&L had to resolve the inconsistency[702]. C&L did not; C&L ignored its own audit evidence and acquiesced to management's requests.

[660] The preponderance of evidence supports the conclusion that changes made by C&L to maturity dates were solely based on representations made by management, even in situations where management representations contradicted management's previous representations[703] and the documentary evidence, including third party evidence gathered by C&L such as audit confirmations.

[661] By extending the due date of various liabilities beyond their actual due dates and advancing the due date of various receivables before their actual due dates, Castor improved its apparent liquidity position and this was falsely reflected in the audited financial statements for each of the relevant years.

[662] Castor intended Notes 2, 3 and 4 of the audited consolidated financial statements to provide information on the matching of current assets and current liabilities, which is critical to assess the liquidity and the solvency of a company.

[663] The assessment of liquidity focuses on the short-term, i.e., the year following the financial statements, and evaluates the ability of the company to meet its obligations as they become due and in the normal course of business.

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[700] D-573 and D-574
[701] Selman, June 10, 2009, pp. 170-172.
[702] PW-1419-1A, section 5300.20
[703] Bänziger's comment to Janet Cameron noted in the AWPs.

[664] The effect of these changes was to further improve the liquidity position as shown in Notes 2, 3 and 4 to the financial statements.

Liquidity improvements (100 million debentures)

Positions (in a nutshell)

Plaintiff

[665] Plaintiff submits that:

- Castor's audited consolidated financial statements for the year ending December 31, 1988 were materially misleading and false as a result of the $100 million debenture transaction entered into by Castor in 1987. This transaction was a circular transaction that had no commercial purpose and was simply a movement of Castor's own money.

- The $100 million debenture transaction enhanced the information disclosed in Castor's financial statements and artificially improved Castor's liquidity and solvency: the loans made by CHIF to Foxfire (Liacon) and Morocco were shown as current loans receivables in the notes to the financial statements while the $100 million of debentures were shown as long-term liabilities not coming due in the following year.

- This transaction led readers of the financial statements to believe that Castor had the ability to raise significant funds from arm's length sources, when in fact this was simply a circular transaction employing Castor's own funds.

Defendants

[666] Defendants submit that:

- The sale of the $100 million debentures occurred in 1987. Although Castor's obligation to repay the debentures when they fell due remained as a long-term liability on its financial statements thereafter, the transaction would be expected to be subject to audit tests in 1987. There are no allegations that the 1987 audit work was inappropriate. Defendants therefore submit that the Court must assume that the work was correct.

- In 1987, Castor issued two series of $50 million of debentures, one maturing in 1997 and the other in 2002, to a group of offshore entities. The funds raised were used to pay down an inter-company debt owed to CHIFNV, and reduce the withholding tax. Also in 1987, CHIFNV made a $75 million loan to Morocco Holdings ("**Morocco**") and a $25 million loan to Foxfire. The actual transactions required a total of 43 cash movements, of which Castor itself was involved in 13,

CHIFNV in 13, Castor Finanz in 8 and CHI (Cyprus) in 9. The evidence now shows that Gambazzi and his office were heavily involved in all aspects of this series of transactions, as well as subsequent transactions related to them. Gambazzi charged Castor $4 million for sourcing the funds. Plaintiffs' experts now characterize this as a sham, asserting that there was no new money and that Castor's funds were being circled. The $4 million fee was further circled within Castor, and $1.3 million of it was diverted to purchase a house for Stolzenberg.

- In 1988, before the year-end, the Foxfire loan was retired and the Morocco loan was reduced to $50 million. A new $50 million loan was granted by CHIFNV to Liacon, secured by a Gambazzi-in-trust back-to-back agreement. In 1991, the Liacon back-to-back security was replaced with a pledge of $50 million of debentures.

- The 1987 working papers indicate that the debentures secured these two loans. The loan agreements have not been produced by the Plaintiffs. Although this demonstrates a relationship of some kind between the debenture-holders on the one hand and Morocco and Foxfire on the other, it does not imply, and C&L did not know (assuming that it is true) that all of these companies were related to Castor. In fact, in order for the tax planning to be effective, this could not have been the case. Moreover, by the time of the 1988 audit, only $50 million of debentures were pledged, for the Morocco loan. As far as C&L knew, the Foxfire loan had been paid out and Liacon was otherwise secured.

- The Court must determine what impact the above facts would have on the financial statements. As only some of the facts were known to C&L, to the extent that the Court determines that the financial statements would be materially different, the subsequent question arises as to whether C&L should have discovered additional facts through the application of ordinary GAAS.

- Vance provided two inconsistent options as to how this transaction should have been presented on the financial statements: on the one hand, he stated that Notes 2-4 should have been affected; on the other hand, he states that the transactions should have been eliminated entirely as they were shams.

Evidence – The 100 million debentures

The transaction

[667] In a memo to Wolfgang Stolzenberg dated April 13, 1987, C&L responded to questions that Simon and Christa Karl, Castor's employees, asked in relation to tax advice regarding withholding taxes on interest paid on debentures[704].

[704] PW-1493

[668] Further to the reception of this memo, Castor proceeded to issue 100 million of debentures.

[669] On June 25, 1987, CHIFNV transferred a total of $75 million out of its accounts, charging this to Morocco Holding[705].

[670] Castor issued 100 million of debentures to the following entities[706]:

- Anstalt fur Montanbedarf, Vaduz (15 million)
- Anstalt Tomura, Vaduz (10 million)
- AG fur Buchprufungen und Treuhandwesen, Vaduz (6 million)
- Fondation Letor, Vaduz (6.5 million)
- Overnome Handels - Finanz-anstalt, Schaan (25 million)
- Mova Inc., Panama (12.5 million)
- Coeval Co. Inc., Panama (15 million)
- Mireta Ltd. Inc., Panama (10 million)

[671] Castor received $75 million from the debenture holders other than Overnome between June 25 and June 29, 1987[707].

[672] Castor Holdings Ltd. made three transfers to CFAG totalling $72.5 million as follows[708]:

- June 26, 1987: $25 million
- June 29, 1987: $27.5 million
- July 7, 1987 : $20 million

[673] The above amounts were recorded in CHL's general ledger account number 358 as a reduction of "*Advance Payable - ZUG*"[709].

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[705] PW-791 (bates #44420, 44626 to 44633); PW-789 and PW-790
[706] Marcinski, January 10, 1996, pp.152 and following; PW-1053-29, sequential page 84 (FF34)
[707] PW-94 (bates #250, 251)
[708] PW-1484-9-3-87, PW-1999 and PW-2000
[709] Part of PW-78

[674] CFAG concurrently transferred the exact amounts it received from CHL to CHI (Cyprus) which, again concurrently, transferred the exact amounts it received to CHIFNV[710].

[675] CHIFNV made a payment to Foxfire Investments of $25 million on November 27, 1987[711]. Also on November 27, 1987, CHL received $25 million which was recorded in its books as having come from Overnome[712].

[676] On November 30, 1987, CHL transferred $18 million to CFAG and $2 million to CHI (Cyprus)[713]. The former amount was recorded in CHL's general ledger account number 358 as a reduction of "*Advance Payable - ZUG*" and the latter amount in account number 360 as a reduction of "*Advance Payable CH (Cyprus)*[714].

[677] CFAG transferred the $18 million to CHI (Cyprus) on November 30, 1987[715].

[678] CHI (Cyprus) transferred the $20 million to CHIFNV[716].

[679] CHL retained $7.5 million of the funds and CHIFNV disbursed $7.5 million more than it received, but, at the end of the day and on a consolidated basis, 100 million of current liabilities of Castor were moved to long-term debt.

[680] Gambazzi received $4 million in commission related to this transaction[717] without having done any work as no new money was raised. These fees ended up being circulated back to CHI (Cyprus) and CHIFNV and ultimately, in part, to Stolzenberg for the purchase of a Westmount home[718].

The transaction and the 1988 financial statements

[681] Under the heading "*Investments in mortgages, secured debentures and advances (notes 2, 3, 4 and 10)*" of the assets section, the balance sheet included 100 million of loans made by CHIF to Morocco and Liacon maturing within the year and therefore presented as current assets[719]. The total amount of the consolidated assets was $1,163,047 million.

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[710] PW-1484-9-3-87, PW-1999 and PW-2000
[711] PW-791 (bates #44420, 44626 to 44633), PW-789 , PW-790
[712] PW-94 (bates #240, 241)
[713] PW-2001
[714] Part of PW-78
[715] PW-1484-9-3-87, PW-1999, PW-2000 and PW-2001
[716] PW-2001
[717] D-324-1, D-323-1, D-323-2, D-323-3, PW-791 (bates #44447)
[718] PW-1053-85 (page 35), PW-2304, D-325-1, PW-1199, PW-791, (bates #44780), PW-253, PW-253A, PW-791 (bates #44604, 44315)
[719] PW-5, tab 10

[682] Under the heading "*Debentures*" of the liabilities section, the balance sheet included $100 million of long-term debt since, as written under note 6, $50 million of those debentures were maturing on June 30, 1997 and $50 million were maturing on June 30, 2002[720].

Experts' opinions

[683] Vance and Rosen opined that this was a circular transaction that had no commercial purpose and was simply a movement of Castor's own money[721]. Defendants' expert Levi opined likewise[722].

[684] Defendants' expert Selman admitted that, if the $100 million transaction was a circular transaction, the financial statements were materially misleading[723].

Conclusion

[685] The 100 million debentures transaction was a circular transaction. The financial statements were materially misleading.

Undisclosed restricted cash

[686] Castor had an unclassified balance sheet in its 1988 financial statements which included the heading "*Cash in bank and short-term deposits*".

[687] Section 3000.01 of the Handbook, an italicized recommendation, provided:

> The following should be excluded from current assets:
>
> (a) Cash subject to restrictions that prevent its use for current purposes;
>
> (b) Cash appropriated for other than current purposes unless such cash offsets a current liability.[724]

[688] Without any note disclosure, a reader of the financial statements would assume that the amount shown under the heading "*Cash in bank and short-term deposits*" was all available and usable for general purposes[725].

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[720] PW-5, tab 10
[721] Vance, March 12, 2008, p. 166; PW-3033, Vol. 1, pp. 70–71.
[722] D-1347, pp. 60-66.
[723] Selman, May 25, 2009, pp. 28-29.
[724] PW-1419-1, section 3000 "cash"
[725] Vance, March 13, 2008, p.29.

Positions (in a nutshell)

Plaintiff

[689] Plaintiff argues :

- Vance opined that USD $20 million were pledged to secure loans made by Credit Suisse Canada to Castor, in existence since 1985 and merely rolled forward in subsequent years[726]. Even if he could not refer to an actual pledge or other guarantee signed by Castor in favour of Credit Suisse with respect to 1988, since none could be located, Vance assumed such a pledge existed in light of the content of the written confirmations signed.

- Castor's 1988 audited consolidated financial statements were materially misstated and misleading as a result of the non-disclosure of such restricted cash[727].

Defendants

[690] Defendants argue:

- Selman opined that the returned confirmation of Credit Suisse Canada indicated that the collateral was a "*Payment Obligation from CS London in the amount of $US 20,000,000*", indicating only that a guarantee was in place. He could not say that Vance was wrong in assuming that the pledge continued. In his report, he also wrote:

  > If an error was made in that there was a pledge in 1988, it appears that its genesis lay in miscommunication by Credit Suisse to C&L in 1987 and in the possibility that there was not a completion of a request in respect of 1987 for information on what appeared to be a relatively immaterial matter. Another possible explanation is that Credit Suisse London had, in fact, unblocked the deposit. The existence in 1988 of a pledge may be just an allegation[728].

- There was no evidence of any such pledge, that the confirmations said no such thing and therefore Plaintiff had not discharged his burden of proof.

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[726] Vance, March 13, 2008, p. 46.
[727] Vance, March 13, 2008, pp.28-29; PW-2908A.
[728] D-1295-1, p. 326

Evidence

[691] Prior to 1988, the audit evidence indicated that the deposits were pledged[729].

1985

PW-1053-37-3 (...) sequential number 62 (...) the bank confirmation in nineteen eighty-five (1985) shows the loans again, there's one ten (10) million dollar loan and two (2) five (5) million dollar loans, and the nature of collateral lodged is described in this case as guarantee.

And then the confirmation that was received by CH International Finance NV in the same year, nineteen eighty-five (1985), is PW-1053-97-2, at sequential page 199. And in this case, it's in the form of a letter, (...) that the balances are shown, again the one ten (10) million dollars and two (2) five (5) million dollars, with a description as being fixed deposits blocked in favour of Credit Suisse Canada Toronto[730].

(...)

1986

Q-Between nineteen eighty-five (1985) and nineteen eighty eight (1988), was there any changes in the situation of these funds?

A- There were not insofar as nineteen eighty-six (1986) was concerned. (...)

Eighty-six ('86) is PW-1053-32-1 (...)

And for the twenty (20) million US of loans in Castor Holdings Limited, the collateral is shown is: "*Pledge of funds US 20 million held at Credit Suisse London in the name of CH International*".[731]

1987

And then in nineteen eighty-seven (1987), there is a slight difference in that the bank confirmation with respect to the Montreal audit is PW- 1053-30-5, sequential page 28, and it refers to (...)

And then in nineteen eighty-seven (1987), as I inadvertently had mentioned for nineteen eighty-six (1986), it is nineteen eighty-seven (1987), PW-1053-30-5, sequential page 28, working paper 821, says: "Letter of guarantee for US 20 million dollars until May 31st,1990."

And then I say in nineteen eighty-seven (1987), there is an issue with respect to the confirmation that came in from CH International Finance... to CH International

[729] PW-1053-97, seq. p. 199; PW-1053-32, seq. p. 90; PW-1053-75, seq. p. 33
[730] Vance, March 13, 2008, pp.38-40
[731] Vance, March 13, 2008, pp.41-43

> Finance from Credit Suisse, it's PW-1053-75-3, sequential page 33, in the form of a letter. (...)
>
> and it's in letter form again, it confirms that there's a nil balance in the current account. And number 2 is US two (2) million dollars: "*Guarantee facility valid until 31st May, 1990, duly pledged by cash deposits*."
>
> And in this instance, the auditors noted the difference. And on PW-1053-75-4, which is sequential page 11, again there's a letter from Mr. Bruce Wilson, the audit manager, to Mr. Edwin Baenziger, item 3, reading: "*Bank confirmation from Credit Suisse, point 2, US dollars 2 million. According to our records, there are three deposits totalling US 20 millions, please advise*."
>
> So he... the auditor's understanding, of course, was that there was... the twenty (20) million that was continued to be pledged. And then on P... the response from Mr. Baenziger to that request is PW-1053-75-5, sequential pages 24 and 25[732].

[692] The CHIFNV deposits with Credit Suisse London were confirmed for the purposes of the 1987 audit[733] and a confirmation letter was received from Credit Suisse London in respect of CHIFNV[734] by C&L's Geneva office. Geneva confirmed such reception to C&L Montreal prior to their finalization of the audit[735].

[693] The 1987 AWPs include a confirmation for a US $2 million guarantee facility - an obvious mistake since it should have been a $20 million guarantee facility -supported by pledged deposits[736], received however by C&L Montreal after the audit was finalized and the consolidated audited financial statements for the year ending on December 31, 1987 were issued.[737] C&L sent a follow-up request for information to Bänziger but the AWPs do not indicate if and how the matter was resolved.

[694] Restricted cash was not disclosed in the 1987 consolidated audited financial statements.

[695] Prior to 1988, Credit Suisse London had been sent a standard confirmation form (banking relationships form) but, in 1988, it only received a statement of open positions form[738].

[696] In 1988, the bank confirmation from Credit Suisse Canada indicated that loans to Castor totalling US$ 20 million were subject to a «*payment obligation from CS London in the amount of $US 20M*»[739] -

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[732] Vance, March 13, 2008, pp.43-45 (see also Vance, June 5, 2008, p.242)
[733] PW-1132A, bates 881, 883 and 884
[734] PW-1132B, bates 1101
[735] PW-1053-93, sequential pages 47-48
[736] PW-1053-75-3; see also D-1295-1, p. 323, para 6.12.02
[737] PW-1053-75, sequential page 35
[738] Vance, June 5, 2008, p. 246; see also PW-1133A, bates 1420

> under "*Loans, Other Direct Liabilities and Collateral Security*", it lists three (3) loans of US amounts ten (10) million, and then two (2) loans of five (5) million, and it shows the collateral as being "Payment Obligation from CS London" in the amount of US twenty (20) million dollars[740].

[697] Vance explained that "*payment obligation*" meant that Credit Suisse London had made an obligation to pay Credit Suisse Canada 20 million dollars to secure the loan[741].

[698] The confirmation received in Europe from Credit Suisse London with respect to the deposits did not contain information relating to the guarantee.

- The confirmation was a statement of open positions[742] rather than a standard bank form as Bänziger, who had control of the confirmation process, elected to send such a form (a statement of open position) to Credit Suisse London.

- Levi testified that an auditor would expect a bank to disclose restrictions where they exist[743].

- However, as Vance explained, through a statement of open positions, a bank is asked to confirm the amounts on deposit and the terms and the interest, but it is not requested to confirm collateral security, guarantees, contingent liabilities or any of the other information that auditors routinely expect banks to confirm or turn their minds to[744].

[699] The 20 million loans that were still in existence at 1988 year-end were repaid by Castor during 1989[745].

[700] Wightman neither saw nor looked at the above various confirmations during the relevant years – he saw them, or some of them, for the first time during examination in 1995 or 1996[746].

Conclusions

[701] The 3 loans, totalling twenty million dollars, existed from 1985 to 1989: this credit facility was valid until May 31, 1990.

[702] The 1985, 1986 and 1987 situations are not in dispute. The Court does not give credit to the suggestion made by counsel for the Defendants, based on propensity or

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[739] PW-1053-23, seq. p. 27.; Vance, June 5, 2008, pp.228-229
[740] Vance, March 13, 2008, p. 37
[741] Vance, June 5, 2008, p. 245
[742] PW-1133A, bates number 1420
[743] Levi, January 13, 2010, pp. 24-26
[744] Vance, March 13, 2008, p.46
[745] Vance, March 13, 2008, p.47
[746] Vance, June 5, 2008, pp. 253-254

possibility of human error by the bankers who were responding to these confirmations, that Credit Suisse Canada and Credit Suisse London got it wrong three years in a row[747].

[703] In their written submission of July 8, 2010, Defendants wrote "*The 1987 situation is not in dispute and the existence of a pledge can change from year to year*", an assertion supported by a reference to Selman's testimony[748] concerning sections 6.12.01 to 6.12.06 of his written report[749].

[704] The Court accepts the general proposition that the existence of a pledge can change from year to year. The Court acknowledges that the language used in the confirmations for 1988 was not identical to that of prior years.

[705] Nevertheless, since the loans totalling 20 million had not been repaid by Castor at year-end 1988, the Court finds that the proper interpretation of "*payment obligation from Credit Suisse London in the amount of US twenty (20) million*" in the 1988 confirmation of Credit Suisse Canada (same amount and same bank as in the previous years), is that it had merely been rolled forward and the 20 million of cash was still restricted. Backstopping that payment obligation was a pending collateral security.

[706] Selman acknowledged that he could not say that the above conclusion was wrong.

> So Mr. Vance assumes that the nineteen eighty-seven (1987) pledge which he concluded existed continued, and as I said, I can't tell you he's wrong, but it's necessarily just an assumption on his part.
>
> So I guess the answer is left to you, My Lady, to decide whether the words "payment obligation" means there was a pledge or just means that there was a guarantee[750].

[707] In the overseas file, a standard confirmation form was not sent, which explains that C&L only got partial confirmation (only confirmation of what was asked for in the statement of open positions). Had C&L asked about any restrictions or contingent liability, it would have received a confirmation of such restrictions or contingent liability.

[708] In the Pineridge litigation, Selman opined:

> «1.14 The points to be raised in the confirmation request of a bank are well known to auditors. (...) the **bank should be asked to confirm not only deposit**

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[747] Vance, June 5, 2008, pp.231-232
[748] Selman, May 14, 2009 pp.65 to 67
[749] D-1295-1
[750] Selman, May 14, 2009 pp. 68-69

balances but whether there was any contingent liability under the guarantee.»[751] (emphasis added)

[709] Knowledge and understanding gained in prior years clearly indicated that twenty million of deposits with Credit Suisse London had been pledged to secure the guarantee facility granted to Castor by Credit Suisse Canada valid until May 31, 1990.

[710] In those circumstances, the Court concludes that, at year-end 1988, US$20 million of restricted cash on deposit with Credit Suisse London was not disclosed on Castor's audited financial statements.

Undisclosed Capitalised interest and inappropriate revenue recognition

General context

[711] Capitalized interest is interest earned on loans but not received in cash by Castor from its borrowers.

[712] Depending on the borrower and on the borrower's situation, capitalization was done through a process of granting new loans, through drawdowns of amounts available under existing loan agreements, or simply through a process of increasing existing loans.

[713] In 1988, all capitalized interests (100%) were recognized as revenue in Castor's audited financial statements.

[714] Defendants admit that a significant amount of Castor's interest income was capitalized and that they knew it[752].

Issue

[715] Did GAAP require that the amount of capitalized interest revenue be separately identified in the financial statements, either as:

- a result of a specific Handbook recommendation;
- a result of general practice; or
- a result of an overriding principle of "fairness"?

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[751] PW-3052

[752] Defendants 'plea, par. 103 and 139; Rosen, February 27, 2009 p. 209-210.

Positions (in a nutshell)

Plaintiff

[716] Plaintiff says that there is a distinction between planned and unplanned capitalized interest. Capitalization of interest, especially the unplanned ones, is a "*red flag*" – a "*warning signal*" – something an auditor has to look at very carefully.

[717] Plaintiff reiterates that in Castor's situation, in 1988, C&L had to deal with a material amount of unplanned capitalized interest, with multiple situations of non-compliance with loan covenants.

[718] Plaintiff argues that Castor's practice and quantum of capitalized interest should have been disclosed – it was material information. A number of provisions of the Handbook expressly or implicitly required or called for such disclosure:

- Section 1505, since the capitalization of interest was a significant accounting policy, particularly with respect to revenue recognition[753];
- Sections 1500.05 and 3850.03 combined, since the amount of capitalized interest was material and failure to disclose the amount resulted in misleading statements and did not constitute fair presentation[754];
- Section 1540, since a SCFP that disclosed the cash generated from operations was required while such a proper SCFP would have disclosed, at least, that Castor was generating virtually no cash from operations (i.e., the consequences of capitalized interest);
- Section 3020.10, since the assets were overstated because no provisions were taken to reduce the non-performing loans to estimated realizable value;
- Section 3400.06, since revenues were grossly overstated because they included interest receivable that was unpaid of which there was no reasonable assurance of collectability; and
- Section 3850, since the italicized recommendation (3850.03) reads as follows: "*The amount of interests capitalized in the period should be disclosed*".

[719] Plaintiff concludes that there was no reasonable assurance of the collectability of the interest and fees accrued for the loans connected to the projects that Plaintiff's

[753] PW-2908, Vol. 1, p. 4-D-3 to 4-D-5.
[754] PW-2908, Vol. 1, p. 4-D-5 to 4-D-8; PW-2370

experts reviewed[755] and the minimum overstatements of revenue for 1988 was $56.8 million[756].

Defendants

[720] Defendants say that there was no obligation to disclose the practice and quantum of capitalized interest.

[721] Defendants reiterate that an auditor could not oblige a client to make a disclosure that was not required by GAAP.

[722] Defendants submit that no separate fairness standard overrides GAAP. At best, in 1988, there was some debate in the profession and the majority of practitioners would have reasonably concluded that the debate had been resolved in favour of there not being such a separate standard. When the debate was resurrected by the MacDonald commission report and then again, after the Kripps[757] decision, the CICA's views were made very clear: no such separate fairness standard overrides GAAP.

- Prior to 1976, auditors had to give two opinions or what was commonly referred to as a "two-part" opinion: that the financial statements were in accordance with GAAP and that the financial statements were fair.
- After 1976, auditors had only a single opinion to give - there was no longer a separate "fairness" standard.
- Therefore, in 1988, C&L was not giving an opinion on fairness or truth in any absolute sense, but only giving an opinion on fairness in accordance with GAAP.

[723] Defendants mention that although certain Canadian jurisdictions had "caught up" with the change made to the content of the audit report in 1976 and most company legislation had adopted the "*present fairly in accordance with GAAP*", the one part opinion, by 1988 not all legislatures had done so. British Columbia had not– its legislation still required a two-part opinion. As the audit client in the Kripps[758] case was organized under British Columbia law[759], this case had to be looked at accordingly taking into account that the applicable New Brunswick law under which Castor was incorporated did not contain a similar provision for a two part opinion.

[724] Defendants assert that section 3850 of the Handbook only addressed capitalized interest expense.

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[755] PW-2941, Vol. 1, p. 25, para. 2.4; PW-2908, Vol. 2, pp. A-6, B-1, G-17.
[756] PW-2908, Vol. 1, S-7 to S-10.
[757] *Kripps v. Touche Ross & Co.*, 1997 CanLII [2007] (BC C.A.)
[758] *Kripps v. Touche Ross & Co.*, 1997 CanLII [2007] (BC C.A.)
[759] PW-2370-3 p. 32 starting at line 22

[725] Defendants argue that the words "*Generally Accepted*" in the acronym "GAAP" are meaningful. The Handbook states that where it is silent, GAAP includes, among other things, other accounting principles that are generally accepted by virtue of their use in similar circumstances by a significant number of entities in Canada. Looking at what others did during 1988 is therefore relevant.

[726] Defendants say that the distinction between planned and unplanned capitalized interest is artificial: nothing in the Handbook even hints at a requirement for a pre-existing contractual agreement to defer interest[760].

[727] Defendants mention that Castor fully intended to capitalize the interest while the developer's operations were generating operating losses on the basis that the underlying property values could be realized upon completion of their development and refurbishment. In Castor's case, payments of interest (monthly or quarterly) were called for in some loan contracts simply to permit Castor to put the borrower in default if it determined that to do so was in its best interests, and to allow for appropriate compounding of the interest.

[728] Defendants assert that capitalized and accrued interests in 1988 were ultimately collectible, but had it been determined that they would not be, Castor would have had a choice to either reverse them or to set up a compensating loan loss provision.

Evidence

Exhibits and lay witness' evidence

[729] In a brochure of 1988, Castor was describing its business as follows[761]:

> Since its inception, Castor has focused on short and medium term loans in the North American mortgage market. These investments have been for its own account, as well as on behalf of a growing international clientele.
>
> Castor's preferred investments are first and second mortgage interim loans on income producing properties (i.e. office, commercial, hotels, industrial and apartment buildings), well located in major urban areas, Castor's primary investment activities include:
>
> - Purchase and placement of first and second mortgages for terms between six months and two years;
> - Interim financing for construction and development secured by mortgages and take-out commitments.
>
> (...)

[760] Selman, May 8, 2009 p.161-163
[761] PW-1057-1

> During 1987, the Company placed mortgage loans of about $250 million in Canada and the United States, which were refinanced in Europe and Canada. Castor currently administers directly or in trust for its clients, mortgage loans in excess of $800 million. All proposed investments are reviewed and thoroughly evaluated by Castor's experienced personnel, prior to commitment. Underwriting standards are high and, in addition, particular attention is given to the Company's policy that loans are not to exceed 75% to 80% of the estimated market value. Careful attention is also paid to asset and liability matching and maturities in order to provide funding stability[762].

[730] In reality, Castor's business was quite different:

- A significant amount of loans were not secured by mortgage on real estate;[763]
- Castor was renewing loans year after year since it had no other choice but to do that - in fact, Castor had slowly but clearly moved from short and medium-term loans to long-term loans;
- The income producing properties were not making their own costs and Castor had to finance them[764];
- "Interim financing" was not really taking place;
- Unplanned capitalized interest represented a significant amount of the $250 million of loans placed by Castor in 1987 – such loans were not made as the result of proposed investments reviewed and thoroughly evaluated through high underwriting standards before commitment – Castor had no choice but to make them since its debtors could not pay their debts;
- Castor had no underwriting standards;
- In fact, and in many instances, Castor did not comply with its advertised lending policy – Castor's loans did exceed the 75% to 80% of the estimated market value.

[731] The books and records provided to C&L, in Montreal and overseas, disclosed the nature of Castor's loans and the fact that very little cash – if virtually no cash- was being paid by Castor's borrowers.

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[762] PW-1057-1, page 4

[763] PW-2893-24; Gourdeau, January 17, 2008, pp.164 and following ; Gourdeau, February, 20, 2008, pp. 74 and following

[764] MLV, CSH, TSH, OSH, Meadowlark

Planned and unplanned capitalization

[732] The distinction between planned and unplanned capitalization of interest and the characterization of the latter as a "warning signal" was made as follows in the Estey Report in 1986 under the heading "*Significant Bank Accounting Principles*".

> Capitalization of interest refers to the advance of money by the bank to the borrower to enable him to pay the interest on his loan from the bank. **Interest may be capitalized pursuant to the original loan agreement, or on an unplanned basis**. Capitalization is planned where the bank and customer do not expect a revenue stream sufficient to service the loan to develop immediately. The most common example is the real estate development loan. It is common and acceptable practice to include in such loan contracts provision for funds sufficient to pay interest during a defined period. **Unplanned capitalization of interest, on the other hand, is considered to be a warning signal, because it indicates the borrower's inability to meet its loan obligations, perhaps in the long term**[765]. (our emphasis)

[733] In various situations[766], Castor and the borrower intended the interest to be paid upon completion, refinancing or sale: then, the agreements indicated a common intent between the two contracting parties to capitalize the interest[767] - the capitalization was planned[768]. It was the case for the certain loans relating to the MEC project, a fairly substantial real estate project that could take some time to complete.

- The Bank of Montreal, the first mortgage creditor, did not tolerate interest capitalization on its loan but it had required that the interest on Castor's loans to YHDL and MEC be capitalized[769].

- Castor's MEC loan documents called for capitalization, including simple capitalization or the establishment of an interest reserve as part of the loan facility[770].

[734] However, huge amounts of Castor's capitalized interest were unplanned capitalized interest further to non-compliance with loan covenants; they were, nevertheless, recognized as revenue.

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[765] PW-1422A, p. 607 (OSR #15 dismissed);.

[766] Vance, May 28, 2008 p. 127-142. These included: CSH - PW-1087-4 and PW-1087-5; the back-to-back loans; the Skyline loans - PW-1053-12-1 sequential p. 90, D-575, p. 1 items 3a and 3b (the pricing was based on a 5-year term) PW-167x, PW-167v ; MLV(interest was capitalized via loans in Europe); see also TWDC - PW167cc – p. 2; TWTC – PW-1053-23-7 p. E-107; Ron Smith, September. 17, 2008, p. 19-20, 24, 98-100

[767] Vance, May 28, 2008, p.143-144

[768] Vance, May 28, 2008, pp. 125-127

[769] PW-1102A-5, see definition of Development Costs (p. 7), Articles 2.02, 2.07 and 12.01(d)

[770] Vance, April 10, 2008 p.19-23, re loans 1100, 1101/03 and loan 1109

C&L internal material

[735] In its internal policies, C&L directed its professionals to take into account the recommendations of the MacDonald Commission[771].

[736] As well, in its permanent files for the Castor audit, C&L maintained a copy of US case law (predating the relevant years) that questions «*whether the [audit] report fairly presents the true financial position...*» and cited the following principle: «*Fair presentation is the touchstone for determining the adequacy of disclosure and financial statements. While adherence to generally accepted accounting principles is a tool to help achieve that end, it is not necessarily a guarantee of fairness*»[772].

C&L's peer review (Castor's 1987 audit)

[737] C&L's peer review of the 1987 Castor audit was done internally by Higgins and Carvell, partners of C&L[773] who wrote in their report:

> From the loan review sheets it is not clear that C&L has checked the information gathered to supporting documentation. The sheets also do not address the question of whether the client is up to date with their review of the debtors' financial position or has complied with all loan covenants[774].

[738] In the same report, peer reviewers Higgins and Carvell made the following recommendation "*Consideration should be given to revising the loan review sheets used in conjunction with those currently in use on bank audits*"[775].

[739] Even though Wightman wrote to Higgins and Carvell that he would consider it for the 1988 audit[776] ("*should be done for 1988*"), the recommendation was not implemented.

Capitalized interest and the audit teams

[740] The issue of capitalized interest was a "hot topic" for the audit[777] and an area of risk for the audits[778], and C&L staff brought forward to Wightman the fact that very material amounts of interest were being capitalized[779].

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[771] PW-1420, Tab 28, re: T&T 125, pp. 1-2.
[772] PW-1053-63C, seq. pp. 53-71, at p. 57.
[773] PW-1420-1A, TPS-A-213
[774] PW-2590, page 3, paragraph 5h (also in PW-1053-21, sequential pages 352-355 and PW-1426)
[775] PW-1053-21, sequential pages 352-355; PW-1426 and PW-2590
[776] PW-2590, page 3, paragraph 5h (also in PW-1053-21, sequential pages 352-355 and PW-1426)
[777] Mitchell, April 24, 1996, pp.81-82
[778] PW-1053-13, sequential page 180
[779] Mitchell, April 24, 1996, pp.130-132: PW-1053-17, sequential page 10; PW-1053-3, sequential page 476

[741] Remarkably Wightman testified that he had no idea whether the percentage of the reported figure of revenue represented 10% or 90% of capitalized interest[780].

Section 1500.05

[742] In the October 1972 CA Magazine issue, auditors can read as part of an article titled "*Research – CICA Handbook – new research recommendations*" edited by Gertrude Mulcahy, FCA, Director of research, CICA:[781]:

> Release No. 8 of Revisions to the CICA handbook will be mailed shortly to members and other subscribers. This release includes a new section in the Research Recommendations division of the Handbook – Section 3050, "long-term Intercorporate Investments" – as well as revisions to a number of other sections necessitated by the new Recommendations. Revisions to two other sections are also provided. (...)[782]
>
> **Other section amendments**
>
> Handbook Revisions – Release No. 8 also included some amendments to existing material which did not arise as a result of the new Section 3050.
>
> **Section 1500- General Standards of Financial Statement Presentation**
>
> A new recommendation has been incorporated in this section to make it clear that information provided outside the financial statements (which includes notes and supporting schedules to which the financial statements are cross-referenced) cannot be considered an integral part of "fair presentation".[783] (*emphasis is part of the original text*)

[743] In "*Principles of auditing*", second Canadian edition 1983, Meigs writes:

> «The meaning of the expression "present fairly" as used in the context of the auditor's report has been much discussed in court cases and in auditing literature. Some accountants believed that financial statements were fair if they conformed to GAAP; others insisted that fairness was a distinct concept, broader than mere compliance with GAAP. This discussion led to an earlier CICA recommendation of a "two-part" opinion; that is, "present fairly" and "in accordance with GAAP" were to be judged separately. However, the CICA subsequently changed its recommendation and now takes the position that the judgment on "present fairly" can be applied "only within the framework of generally accepted accounting principles". In the opinion of the authors, the essence of the CICA position is to equate the quality of **presenting fairly** with that of **not being misleading or not being materially misstated**. Financial statements must not be so presented as to lead users to forecasts or conclusions

[780] Wightman, October 10, 1995, pp. 45–46.
[781] D-519
[782] D-519, p.64
[783] D-519, p.67

> that a company and its independent auditors know are unsound or unlikely».[784] (*emphasis is part of the original text*)

[744] In "*The external audit*", second edition 1984, Anderson's arguments against a separate and abstract standard of fairness include the following:

> 1. Effective communication requires agreement between sender and receiver as to a common language in which the communication will be expressed. GAAP provide that language. The reader can then interpret "fairly" in the non-technical sense of "not misleading", but only in relation to an identifiable standard such as GAAP (...)
>
> 5. Concerns that GAAP represent a set of overly rigid and mechanical rules are exaggerated. Accounting pronouncements in Canada (as compared with the U.S.) are usually expressed in general, rather than very detailed, terms. The Introduction to Accounting Recommendations states:
>
> In issuing Recommendations, the Accounting Research Committee recognizes that no rules of general application can be phrased to suit all circumstances or combination of circumstances that may arise nor is there any substitute for the exercise of professional judgment in the determination of what constitutes fair presentation or good practice in a particular case.
>
> (...)
>
> Furthermore, application of the auditor's professional judgment is also required in assessing compliance with the following very general Recommendation:
>
> Any information required for fair presentation of financial position, results of operations, or changes in financial position, should be presented in the financial statements...
>
> 6. This position is consistent with the present position in the U.S.
>
> The independent auditor's judgment concerning the "fairness" of the overall presentation of financial statements should be applied within the framework of generally accepted accounting principles. Without that framework the auditor would have no uniform standard for judging the presentation...[785]

[745] In the same publication, under the subtitle "*The fairness standard within GAAP*", Anderson writes:

> Attention to fairness in applying GAAP involves the exercise of care and judgment in several critical areas:
>
> (...)

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[784] PW-3053-1, p. 29.
[785] PW-1421-22, pp. 553-554.

> 5. assessing whether disclosure is adequate; that is, whether it includes all information required for fair presentation (...)
>
> 8. identifying circumstances where the spirit, rather than the letter, of the recommendations should prevail[786].

[746] The MacDonald commission's report published in June of 1988 states at paragraph 3.45:

> In an ideal world, the accountability framework and GGAP would be well thought out and comprehensive, so that their application in an honest manner would almost inevitably provide the information that users need to know. But auditor must know that we do not live in a perfect world. There are, and probably always will be, ambiguities and lack of completeness in GAAP. The auditor is expected to have a good sense of the basic concepts of fair presentation. He or she should be aggressive in seeing that they are applied, notwithstanding the absence or lack of clarity of guidance and, if not satisfied, the audit report should be qualified. This is particularly so when accounting is proposed that appears to be unreasonably optimistic. Users of financial information will be much more critical of accounting practices that paint an unwarranted picture of prosperity than of accounting that proves to have been conservative. An auditor needs an acute sense of danger. If the auditor encounters a dubious accounting presentation and has a sense of danger, we are confident that grounds will exist for qualification of the audit report.[787]

[747] The CICA research study entitled "*Professional judgment in financial reporting*", published in 1988, states authors Gibbins and Mason:

> STATEMENTS AS A WHOLE COMPLYING WITH GAAP
>
> Is it possible for each of the transactions comprising a set of statements to be recorded and disclosed in accordance with GAAP, but for the statements as a whole to be deemed not to comply with GAAP? Depending on how one interprets *CICA Handbook* paragraph 1500.05, the answer may be "yes" That paragraph states:
>
> Any information required for fair presentation of financial position, results of operations, or changes in financial position, should be presented in the financial statements...
>
> Since there is no indication as to what is meant by "fair presentation" not any criteria for assessing it, it would be quite possible for the statement preparers or auditors to deem, in their judgment, certain information to be required for it even

[786] PW-1421-22, pp. 554-555
[787] PW-1432A, p. 50, para. 3.45.

> though such information is not required either by the *Handbook* or by other sources of GAAP.[788]

[748] The staff of the Assurance Standards Department at the CICA issue, in September 2001, a non-authoritative bulletin, a practice advice (issue 9), which includes the following comment:

> The AcSB also proposes to reword *CICA Handbook*- Accounting paragraph 1500.05 to clarify its original intent when it was first introduced into the *CICA Handbook – Accounting*. That intent ensures that all information necessary to comply with GAAP is included in the financial statements (including notes to such statements and crossed-reference supporting schedules), rather than other documents. Some parties have misinterpreted current wording to require a separate consideration of fairness[789].

[749] In October 2003, further to an exposure draft and usual proceedings relating thereto, Section 1400 comes into force[790]. It namely provides for the following italicized recommendations (1400.03 and 1400.09) and non-italicized paragraphs (1400.04 and 1400.05)

> 1400.03 Financial statements should present fairly in accordance with Canadian generally accepted accounting principles the financial position, results of operations and cash flows of an entity (that is, represent faithfully the substance of transactions and other events in accordance with the elements of financial statements, and the recognition and measurement criteria set out in FINANCIAL STATEMENT CONCEPTS, Section 1000).
>
> 1400.04 A fair presentation in accordance with generally accepted accounting principles is achieved by:
>
> (a) applying GENERALLY ACCEPTED ACCOUNTING PRINCIPLES, Section 1100;
>
> (b) providing sufficient information about transactions or events having an effect on the entity's financial position, results of operations and cash flows for the periods presented that are of such size, nature and incidence that their disclosure is necessary to understand that effect; and
>
> (c) providing information in a manner that is clear and understandable.
>
> 1400.05 An entity exercises professional judgment to provide sufficient information about the extent and nature of transactions or events having an effect on the entity's financial position, results of operations and cash flows for the periods presented that are of such size, nature and incidence that their disclosure is necessary to understand that effect.

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[788] PW-2917, p. 126.
[789] D-520, pages 3 and 4
[790] D-659-1 (re:4.4.08) B

This information would include the significant terms and conditions of such transactions, as well as the nature of such events and their financial effects on the periods presented.

1400.09 Financial statements, including notes to such statements and supporting schedules to which the financial statements are cross-referenced, should include all information required for a fair presentation in accordance with generally accepted accounting principles.

[750] The CICA publishes a document entitled "*General Standards of Financial Statement Presentation – Background Information and Basis for Conclusions Section 1400*" where one reads:

FAIR PRESENTATION

23 **"Fair presentation"** is difficult to define unless expressed in terms of compliance with standards. Accordingly, the AcSB decided to amend GENERAL STANDARDS OF FINANCIAL PRESENTATION, Section 1500, **to clarify** that "fair presentation" is not a separate consideration from whether financial statements are in accordance with generally accepted accounting principles.

24 A first step in this clarification was taken initially by proposing to reword former GENERAL STANDARDS OF FINANCIAL STATEMENT PRESENTATION, paragraph 1500.05 (now GENERAL STANDARDS OF FINANCIAL STATEMENT PRESENTATION, paragraph 1400.09), **to clarify** its original intent when it was first introduced into the CICA Handbook – Accounting. That Intent ensures that all information required to be disclosed by GAAP is included in the financial statements (including notes to such statements and cross-referenced supporting schedules), rather than other documents. Some had misinterpreted the former wording to require a separate consideration of fairness.

25 After the initial proposals, some questioned how the overall fairness of presentation of financial statements would be assessed. Also, **some additional comment letters expressed the view that it is important to "step back"** and consider whether the financial statements as a whole present fairly in accordance with GAAP the financial position and results of operations of an entity. They proposed that merely complying with the various presentation and disclosure requirements specifically identified in the CICA Handbook – Accounting might not be sufficient. **They believed that the spirit of GAAP also needed to be taken into account.**

26 **The AcSB concurs that it is always necessary, but in some cases not sufficient, to follow the minimum requirements of GAAP and that an entity should "step back"** and consider whether its financial statements are presented in a manner that provides clear and understandable information to users of financial statements. In particular, this applies to the manner in which notes to the financial statements are presented – so as to be informative and

useful, rather than merely providing "boilerplate" information. However, the AcSB believes that this should be restricted to an assessment of whether "fair presentation in accordance with GAAP" has been achieved, rather than whether fundamental recognition or measurement requirements should be compromised.

27 The AcSB proposed **to clarify** this matter by introducing a new paragraph .04, which explained that **a fair presentation in accordance with generally accepted accounting principles requires not only applying** accounting policies that are in accordance with GENERALLY ACCETED ACCOUNTING PRINCIPLES, Section 1100, **but also assessing whether** there are transactions, circumstances or events of such size, nature or incidence that their **disclosure is necessary to** understand the entity's financial position, results of operations and cash flows. (...)

33 Paragraph 1400.09 (former GENERAL STANDARDS OF FINANCIAL STATEMENT PRESENTATION, paragraph 1500.05) continues to require that financial statements are cross-referenced to any notes and supporting schedules. It has been notes that US GAAP does not require such cross-referencing. However, the AcSB believes that this results in better presentation and has retained this requirement.

(*emphasis added by the undersigned*)

Section 3850

[751] The Exposure Draft[791] that preceded the adoption of section 3850 of the Handbook dealt solely with capitalization of interest expense. The underlying research proposal and the Statement of Principles leading to the Exposure Draft similarly dealt solely with such expense. The responses to the Exposure Draft, all part of the public record, centered almost entirely on such expense; only three mentioned an extension of it to interest revenue.

[752] Historically, when there had been a major change between an Exposure Draft and the final wording contemplated, the concerned section had been re-exposed. At the time section 3850 of the Handbook was adopted, Vance was puzzled by the lack of re-exposure[792].

[753] After section 3850 was adopted, CA Magazine published an article describing the process, the responses which had been received and the ultimate resolution of any issues that had been raised. The article contained the following passage under the heading "*Defining terms*":

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[791] PW-1423

[792] Vance, April 16, 2008, p.140-142

> The Committee decided that, for Section 3850's purposes, interest capitalized would simply be the amount not otherwise expensed as interest in the income statement under an enterprise's existing accounting policy[793].

The audit report over the years

[754] Prior to 1976, auditors were required to give two opinions or what was commonly referred to as a "two-part" opinion:

- that the financial statements were in accordance with GAAP; and
- that the financial statements were fair.

[755] The version of the 1988 opinion was introduced in 1976, a change explained in the Handbook as follows[794]:

> "The material now indicates that the auditor formulates his opinion within the framework of generally accepted accounting principles whereas the material which has been replaced – paragraphs 5500.01 to .08 indicates that the auditor expresses his opinions as to whether the financial statements: 1) present fairly and 2) were prepared in accordance with generally accepted accounting principles."

What others did

[756] Vance could not produce and was not aware of any financial statements of any lender from 1988 to 1990 that specifically disclosed the amount of capitalized interest revenue, either as a note or as a separate line item[795].

[757] Selman conducted broad-based research and brought all the results to the Court's attention in Exhibit 1 part C of his report[796].

[758] In testimonies on discovery rendered in 1995 and 1996, Wightman said:

<u>On October 11, 1995</u>

> First of all Castor wasn't a bank so the comparison is perhaps not valid[797].

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[793] D-487-2, bates # 000063
[794] PW-1419-13
[795] Vance, May 28, 2008, p.248
[796] D-1295-1
[797] Wightman, October 11, 1995, p. 131

On August 13, 1996

In answer to the following question "*Did you indicate to your valuations Department that the business of Castor was comparable to the business of major Canadian public trust companies?*"

No, As a matter of fact I recall discussing whether in fact that was a good basis to compare with or not to compare with because I said it wasn't comparable to a trust company...[798]

And further, on page 70

I had to agree that I couldn't name any company that I felt – any companies or company that was more closely related to Castor's activities[799]

On September 13, 1996

In answer to a question relating to the format of SCNIA that was used between 1986 and 1990 for Castor

We had great difficulty in finding companies that we felt were comparable to CASTOR and so that in itself would not lead me to compare them to all other financial institutions[800].

In answer to a question relating to the use of the SCFP

First of all I don't know of any industry that CASTOR was in specifically that is public information. As I told you, the trust companies were regulated companies, they were – insurance companies were regulated companies, banks were regulated companies and they all had particular reporting requirements. CASTOR was not a regulated company as such and that's where we always had difficulty finding what you would call companies in the same industry. And so I don't think to compare CASTOR,s – because it was making mortgage loans to compare it to the trust companies in Canada is a fair comparison for purposes of Financial Statement presentation[801].

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[798] Wightman, August 13, 1996, p. 68
[799] Wightman, August 13, 1996, p.70
[800] Wightman, September 13, 1996, p. 40
[801] Wightman, September 13, 1996, pp. 52-53

[759] Marcinski, another partner of C&L, when questioned on discovery about Castor and its business, testified as follows:

> I'm unaware of any other clients in our practice that would have had a socalled mortgage reserve for example, which was an unusual income tax complication (...)[802]
>
> As well, I'm unaware of any other client in the Montreal practice that would have been characterized as a so-called trust and loan corporation for purposes of the Quebec Taxation Act, (...)[803]
>
> At the time, in 1989, I'd had ten (10) years of work experience, to be fair, in my experience this was a new client, a unique client as I mentioned, (...)[804]

[760] In a letter dated April 3, 1989, in reply to an exposure draft, the Superintendent of financial institutions Canada wrote to the CICA:

> My fundamental problem at the moment is that, until a great deal of work is done, my office will not accept the inclusion of banks within the scope of the handbook. In taking this position I have the general support of the banking industry and those chartered accountants most familiar with banking auditing and accounting[805].

[761] In C&L's technical policy statement TPS-A-400, revised December 29, 1989, one reads at paragraph 4:

> Except where otherwise stated in a particular Recommendation, the Accounting Recommendations of the Handbook are applicable to all types of profit-oriented enterprises other than banks and to most non-profit organizations.[806]

[762] On cross-examination on June 1, 2009, Selman explained that the Bank Act did not require a SCFP and he acknowledged the following:

> The superintendant had never mandated that the banks prepare a statement of changes in financial position. Some banks chose to do so and some banks chose not to do so[807].
>
> (...) the statement of changes in financial position had not been mandated as a requirement by the superintendant and (...)
>
> So in one sense, I would accept that you could say that the banks were exempt from the handbook (...)[808]

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[802] Marcinski, January 10, 1996, p. 40
[803] Marcinski, January 10, 1996, p. 41
[804] Marcinski, January 10, 1996, p. 220
[805] D-742
[806] PW-1420-1B, TPS-A-400
[807] Selman, June 1, 2009, p. 117

Experts' evidence

[763] Both experts, Vance and Selman, agreed that «*the standards cannot set a rule of general application applicable to all circumstances so you have to be able to understand the spirit of the rule and how to use it*»[809].

[764] There is no dispute that the standard audit opinion uses the phrase "*present fairly in accordance to GAAP*".

[765] There is no dispute between the experts that, where a loan agreement provides for planned capitalization of interest and/or fees, the accrued interest and fees are recognized as revenue provided that there is reasonable assurance of collectability[810].

Plaintiff's experts

[766] Vance opined that Castor was required to disclose the amount of its capitalized interest revenue. In support of this position, Vance invited the Court to take account of any combination of the following requirements, the strongest being the requirement for a SCFP (given the factual situation)[811]:

- Section 1500.05 and the duty to present fairly, such duty being part of GAAP[812] in that "when you finish the audit, and you've done all the bits and pieces, you have to stand back and make sure that what you've done results in fair presentation"[813];
- Section 1540 relating to the SCFP[814]; and
- Section 3850 relating to the disclosure of capitalized interests[815].

[767] Vance opined that section 1500.05 of the Handbook was setting "*an omnibus standard of fairness that had to prevail through the financial statements*"[816].

[768] As authoritative support for his interpretation of section 1500.05, Vance[817] referred to the MacDonald Commission Report, to its recommendation that there be a "*stand back look*" of financial statements[818]. He explained that the recommendation did not lead to a change in the Handbook because the CICA Committee, of which he was

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[808] Selman, June 1, 2009, p.118
[809] D-1295, p. 242.
[810] PW-2941, Vol. 2, p. 125, para. 2.247.
[811] Vance, May 28, 2008, pp.196-197
[812] PW-1419-2, s.1500.05; Vance, April 12, 2010, p. 96.
[813] Vance, May 28, 2008, p.194
[814] See the section of the present judgment relating to the SCFP
[815] Vance, March 6, 2008 p.152-154
[816] Vance, May 28, 2008, p.195
[817] PW-2908,p. 4-D-6 to 4-D-7 and Vance, March 6, 2008 p.179-180
[818] PW-1432A R-20 on p. 60

an active member, felt that such a requirement was already part of GAAP[819]. However, Vance acknowledged having been made aware later that some practitioners held different views[820].

[769] Rosen also opined that Castor was required to disclose the amount of its capitalized interest revenue.

[770] As he explained, to differentiate fantasy from reality, planned and unplanned capitalization has to be looked at in a precise factual context, from a practical point of view rather than a theoretical one[821].

[771] Rosen relied on section 1000 of the Handbook to support his testimony that there was a separate fairness standard.

[772] Rosen stated that, in 1988, 1989 and 1990, the bulk of the people interpreting section 3850 were saying that section 3850 was applicable to disclosure of capitalized interest revenue, but he acknowledged that it was possible to find people who did not interpret it that way[822].

[773] Froese was not asked to opine on this topic but in his report, he wrote:

> 11.11 We were not asked to provide our opinion as to whether Castor complied with GAAP in relation to its failure to prepare a statement of changes in financial position or otherwise disclose the extent of capitalized interest in the notes to its consolidated financial statements.
>
> 11.12 However, due to the extent of interest capitalization and C&L's awareness, at least in part, of the extent of interest capitalization, in our opinion Castor and C&L should have considered whether interest capitalization was occurring to such an extent that it required disclosure[823].

[774] In cross-examination on December 12, 2008, Froese testified as follows:

> A- GAAP had no specific provisions that required you to disclose the extent of non-accrual loans. But GAAP does require you to disclose information that's material to the financial statement readers in relation to financial... the financial statements. And when you look at the extent of non-accrual loans over those three (3) years, in my opinion, the extent of non-accrual loans is material.
>
> Q- And would you agree that a reasonably competent professional during the relevant years could differ with you on that disclosure issue, given their

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[819] Vance, May 28, 2008, pp.210-211
[820] Vance, Mai 28, 2008, pp.199-200
[821] Rosen, March 30, 2009, pp. 37-56
[822] Rosen, March 26, 2009, p. 182
[823] PW-2941, volume 1, p. 191

> interpretation of the requirements of GAAP and the debate that was ongoing in respect to fairness?
>
> A- **That's possible. It depends on whether they have the same fundamental assumptions or facts that you're basing it on.** So if you look at the full extent of non-accrual loans as set out in Volume 1 that, in my view, are nonperforming and should be on a non-accrual basis, and you compare that to the total financial statements. **If they have the same information, in my view, most - and I can't say all - but I would think most professionals would agree it requires disclosure.**
>
> If it was a much smaller amount or had a different framework underlying, it is a non-accrual loans where five percent (5%) or two percent (2%) of total loans, I would agree disclosure is likely not required[824]. (our emphasis)

Defendants' expert

[775] Selman opined that the issue of materiality of capitalized interest was irrelevant unless the Handbook specifically required disclosure of an item and therefore, even if 100% of the interest income was made up of capitalized interest, there was no disclosure requirement[825].

[776] Selman referred to section 1000.03, which states clearly that section 1000 does not set disclosure standards and concluded that, as a result, any auditor who attempted to impose additional disclosure on his client by appealing to section 1000 would be met with resistance that, in his view, would be legitimate[826].

[777] Selman opined that section 1500.05 was intended to ensure that all information to see, as part of fair presentation, would be included within the financial statements, including notes and other schedules to which the financial statements were cross-referenced. Selman explained that the issue was purely a matter of location of the information - the goal was to make it clear that an assessment of whether the financial statements presented the financial position fairly in accordance with GAAP should not include consideration of whether the reporting entity had provided information required under GAAP in some other document, such as a management discussion and analysis. In other words, the financial statements had to provide all the information required by GAAP within themselves. [827]

[778] Selman opined that section 3850 of the Handbook had to be interpreted and applied as referring to capitalized interest expense only[828] based on the contents of the Exposure Draft that preceded its adoption and the discussion in the Public Record[829].

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[824] Froese, December 12, 2008, p.19
[825] Selman, June 11, 2009, pp. 58–59.
[826] Selman, May 7, 2009, p.161
[827] Selman, May 7, 2009 p.86-94
[828] Selman, May 8, 2009, p.119-120

[779] Selman pointed out[830] that the statement included in the CA Magazine, by its nature, referred only to capitalized interest expense.

[780] Selman concluded that reading all of these materials made it clear that section 3850 was not dealing with the accounting disclosures of the lender and did not require disclosure of capitalized interest revenue.

[781] Selman referred to the research he had done and highlighted that he had listed seventy-four financial companies that did not disclose the amount of their capitalized interest revenue – that six of these indicated that they had a capitalization policy and that one said it had no capitalized interest. Selman added that some of these lenders were known to lend to developers and some of them were lending to Castor[831].

[782] Selman could not opine as to the ultimate collectability of the capitalized interest but he did opine that preparers had a choice to reverse capitalized or accrued interest that was determined not to be ultimately collectible, or to set up a compensating loan loss provision ("**LLP**").[832].

Conclusions

[783] Revenue is recognized when "*ultimate collection is reasonably assured*"[833]. Revenue should not be recognized unless there is reasonable assurance of collectability and measurement.

[784] Capitalization of interest was not in itself unusual.

[785] Financial statements are by their very nature summaries of financial events, including transactions and commitments and it is not possible to convey all financial information that might be of interest to all readers. However, material information must be disclosed.

[786] Provided a client's financial statements were not misleading nor materially misstated and met GAAP, an auditor was powerless to insist on fuller disclosure even where he knew that the financial statements would not meet the information needs of certain types of users. Such auditor had however to apply an overall fairness standard within GAAP. The Handbook's primary directive is to reasonably ensure that financial statements are presented fairly and are not materially misstated.

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[829] D-487-2 and PW-1423
[830] Selman, May 8, 2009, pp.119-120
[831] Selman, May 8, 2009, pp.135 -148
[832] Selman, May 8, 2009 p.103-109
[833] PW-1419-1, section 3400.06; Rosen, February 3, 2009 p.50-54; Selman, May 8, 2009 p.103

[787] As Anderson wrote:

- "*The concept of fairness should not be interpreted as imposing a subjective set of standards that would prevail over GAAP*"; but,
- "*there is thus considerable scope within GAAP to apply an overall fairness standard in the preparation of financial statements. This may logically be interpreted as calling for compliance with the spirit rather than with the letter of the accounting recommendations*". [834]

[788] The amount of capitalized interest was indisputably material and C&L knew that interest was not being collected in cash, but was being routinely capitalized.

[789] The concern that the Castor audits were characterized by overreliance on valuations of collateral without considering the financial condition of the borrower, deemed "*collateral myopia*", being the «*failure to see beyond collateral values to a financial weakness...*»[835], appears to have driven Higgins and Carvell, the peer reviewers, to recommend on November 10, 1988 the use of bank questionnaires for the Castor audits in the future. Those questionnaires put a much greater focus on the assessment of both the value of the collateral and the financial condition of the borrower[836].

[790] Wightman testified that he could not tell if 10% or 90 % of revenue was capitalized interest. Only two possible conclusions can be drawn from such testimony:

- Wightman was being untruthful; or
- Wightman was acknowledging his ignorance of a very critical feature of Castor's business as a lender.

[791] Whatever conclusion the Court may come to, a fact remains: at the end of the day, Defendants ignored this very critical feature of Castor's situation in the exercise of professional judgment.

[792] According to the Handbook the objective of financial statements is to communicate material information to users and its overarching purpose is to ensure disclosure if necessary to avoid a material misstatement. Although the auditor does not give an opinion on "fairness" as such, fairness still remains part of the equation. In his report, the auditor does not say that the financial statements present the situation in accordance to GAAP but he says that the financial statements present fairly in accordance to GAAP.

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[834] PW-1421-9 and PW-1421-22
[835] PW-2942
[836] PW-2590, para. 5h.

[793] This issue of undisclosed capitalized interest was considered by the British Columbia Court of Appeal in a case known as the Kripps case.

[794] The factual context of the Kripps case is similar to the present case: it involves a lender who, in the early 80s, disclosed its policy of permitting capitalized interest, but not the quantum of capitalized interest on its audited financial statements (although the amount was available in a public document) and who was seeking, in 1983-1984, investments in debentures through a prospectus into which its audited financial statements and its auditor's report were included.

[795] Defendants have urged this Court to disregard the Kripps decision alleging that it had been rendered in a context of a two-part opinion. This argument has no merit: except for the fact that in Kripps, there is a SCFP, while in Castor, there is a SCNIA, the auditor's report in litigation in the Kripps case and the C&L's audit report of 1988 in litigation are "*twins*".

Audit report in the Kripps case[837]	C&L report (1988 audited financial statements)[838]
We have examined the balance sheet of Victoria Mortgage Corporation Ltd. as at December 31, 1983 and 1982 and the statements of operations and retained earnings and changes in financial position for the year then ended; and the consolidated statements of operations, retained earnings and changes in financial position of the year ended December 31, 1981, the four months ended December 31, 1980 and the year ended August 31, 1980. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures as we considered necessary in the circumstances.	We have examined the consolidated balance sheet of Castor Holdings ltd. as at December 31, 1988 and the consolidated statements of earnings, retained earnings and changes in net invested assets for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures as we considered necessary in the circumstances.

[837] *Kripps v. Touche Ross & Co.*, [1997] CanLII 2007 (BC C.A.), paragraph 113 (in the dissenting opinion) [1997] 6 W.W.R. 421 • (1997), 33 B.C.L.R. (3d) 254

[838] PW-5, tab 10 (see also tab 11 and tab 12 for 1989 and 1990)

In our opinion, these financial statements present fairly the financial position of the Company as at December 31, 1983 and 1982, and the results of its operations and the changes of financial position of the years ended December 31, 1983, 1982, and 1981, the four months period ended December 31, 1980 and the year ended August 31, 1980 in accordance with generally accepted accounting principles applied on a consistent basis.	In our opinion, these consolidated financial statements present fairly the financial position of the company as at December 31, 1988 and the results of its operations and the changes in its net invested assets for the year then ended in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

[796] The British Columbia Court of Appeal did not accept Selman's opinion that disclosure of material capitalized interest was not required under GAAP. Leave to appeal was refused by the Supreme Court of Canada[839].

[797] The British Columbia Court of Appeal held that in 1984, the CICA was moving towards a requirement that the failure to disclose explicitly the amount of unpaid interest (if material) was contrary to the goal of presenting fairly the financial position of the company and, in 1985, the CICA formally changed GAAP in this regard. There is no doubt that the Court is referencing here the modifications to the SCFP that were introduced in 1985 by the CICA and the understanding that the modifications would facilitate the disclosure of unpaid interest (i.e., non-cash) to the reader.

> 56. Although capitalizing unpaid interest was part of GAAP at the time Touche prepared its auditor's report, the accounting profession had begun to recognize the failings inherent in this approach. The Canadian Institute of Chartered Accountants (CICA) appears in retrospect to have been moving towards a recognition that failing to disclose explicitly the amount of unpaid interest made it difficult for financial statements to fulfill the broad aim of presenting fairly the financial position of the company, and that GAAP had to be changed so as to fulfill the broader aim. The financial statements prepared for VMCL the next year (1985) did disclose accrued and unpaid interest, although the CICA did not formally change GAAP until later in 1985[840].

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[839] SCC News release of November 6, 1997 , file 26118

[840] *Kripps v. Touche Ross & Co.*, [1997] CanLII 2007 (BC C.A.), paragraph 56; [1997] 6 W.W.R. 421 • [1997], 33 B.C.L.R. (3d) 254

[798] The British Columbia Court of Appeal wrote:

> 65 (...) It is clear from the Handbook that the paramount aim in auditing and in providing an unqualified audit is to ensure that the financial statements "present fairly" the financial position of the company being audited. GAAP is a tool to achieve that fair presentation. (...) The tool used – GAAP – is intended to result in such fair presentation and when it does not the tool is revised, as it was **in 1985 when it became clear that the practice of capitalizing unpaid interest could be misleading.**
>
> 66. Given the aim in auditing, the understanding of audits that those who might rely on them have, and that auditors know of this understanding, **auditors cannot hide behind the qualification to their reports ("according to GAAP")** where the financial statements nevertheless misrepresent the financial position of the company. (our emphasis)

[799] As to the judicial attitude towards standards, the British Columbia Court of Appeal cited Sopinka J., writing for the majority of the Supreme Court in *Ter Neuzen v. Korn*:

> I conclude from the foregoing, as a general rule, where a procedure involves difficult or uncertain questions of medical treatment or complex, scientific or highly technical matters that are beyond the ordinary experience and understanding of a judge or jury, it will not be open to find a standard medical practice negligent. On the other hand, as an exception to the general rule, if a standard practice fails to adopt obvious and reasonable precautions which are readily apparent to the ordinary finder of fact, then it is no excuse for a practitioner to claim that he or she was merely conforming to such a negligent common practice.[841]

[800] Thereafter, the British Columbia Court of Appeal concluded that it "*respectfully disagree with the learned trial judge that it is appropriate for auditors to sign unqualified auditor's reports if the financial statements are prepared in accordance with GAAP, if the auditors know or ought to know that the financial statements are misleading*".

[801] The standard opinion in 1988 clearly called for a single opinion that tied "fairness" to GAAP, GAAP calling for any information required for fair presentation of financial position, results of operations, or changes in financial position, to be presented in the financial statements including notes to such statements and supporting schedules to which the financial statements are cross-referenced.

[802] Taking into account the evidence summarized in the section "What others did" of the present judgment, the way banks and other regulated entities presented their financial statements during the relevant years is not conclusive.

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[841] *Ter Neuzen v. Korn* [1995] CanLII 72 (S.C.C.) cited in *Kripps v. Touche Ross & Co.*, [1997] CanLII 2007 (BC C.A.), paragraph 69; [1997] 6 W.W.R. 421 • [1997], 33 B.C.L.R. (3d) 254

[803] In the normal course of business, financial institutions do not recognize a disproportionate percentage of their revenue in the form of capitalized interests. Not only does a 90 day rule for recognition of revenue prevent such inappropriate recognition, it is simply not normal in Canada for a bank or other financial institutions not to receive interests on a monthly basis from its borrowers when contractual provisions so provide. Banks do not tolerate, as Castor did, that close to 90% of their recorded revenue from loans results from capitalization of interest and fees.

[804] In Castor's unique situation, not applying GAAP in a vacuum, disclosure of the capitalization of interest and of the quantum of such capitalized interests had to be done.

[805] In 1988, given all the discussed sections of the Handbook in force, taking account of the knowledge of C&L as to the uses that they themselves, and other users would have for their audit work and audit report, the capitalization of interest and the quantum of such capitalized interests was mandatory to prevent materially misstated and misleading audited financial statements from circulating. Reasonableness leads to conclude accordingly.

Understatement of Loan loss provisions and overstatement of carrying value of Castor's loan portfolio and equity

[806] Section 3020 of the Handbook concerns the carrying value of loans and requires the preparer to value these assets at the lower of estimated realizable value and cost. As a result, the amount of the loan balances on Castor's books (inclusive of capitalized interest) has to be used as a starting point – it represents the cost of the assets.

[807] In 1988, Castor represented a carrying value of loans (investments in mortgages, secured debentures and advances) of $1 005,992 in its audited financial statements[842] : it represented that the figure of $1 005,992 was the lower of estimated realizable value and cost.

[808] The next three subheadings that deal with the question and answer at the heart of the matter, with the positions of the parties, in a nutshell, and with the experts' assessment of the loan loss provisions, as exposed in three different grids, serve as an introduction to detailed analysis of various loans and projects that were financed by Castor, which starts thereafter.

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[842] PW-5, tab 10

Question and answer at the heart of the matter

Question

[809] To try to assess the exact quantum of any LLP that might have been required for 1988 is neither achievable nor necessary. This litigation is not about what should have been the precise content of Castor's financial statements for 1988. It is about whether or not C&L's 1988 audited financial statements of Castor presented fairly the financial position of Castor in accordance with GAAP, as they purported to do.

[810] At December 31, 1988, could the carrying value of loans, at the lower of estimated realizable value and cost, be $1 005,992 or an amount close enough to $1 005,992 to avoid a material misstatement?

Answer

[811] Taking into account the facts as they unfolded, viewed and analysed in the context of the relationship that existed between Castor and YH, the obvious conclusion is that the carrying value of loans could not be $1 005,992 or an amount close enough to $1 005,992 to avoid a material misstatement.

[812] In the absence of a significant LLP, the 1988 Castor audited financial statements were materially misstated.

Positions in a nutshell

Plaintiff

[813] Plaintiff argues that, for 1988, the loans were largely overstated by at least $123.6 million.

- Plaintiff's experts each only reviewed about half of the loan portfolio for purposes of establishing required loan loss provisions. For the most part and to give C&L the "*benefit of the doubt*", Plaintiff's experts used appraisal values even though it was apparent that such values were overstated and relied on assumptions that were not and could not be attained.

- Had all of the loans in the portfolio been examined and valued in accordance with GAAP, the loan losses would have been far greater.

[814] Because the determined losses were so huge, Plaintiff pleads that it was not necessary for experts to ascertain all of the overstatements; in either event, the audited financial statements were manifestly misstated and misleading.

[815] Hopes and dreams cannot be employed to artificially create value under GAAP because there is no reasonable certainty that such future events will ever occur.

[816] Plaintiff maintains:

- That Goodman's values and assumptions (factual premises) are often unsustainable or inaccurate;
- That Goodman relies on security enforcement scenarios which are totally unrealistic, never considered by Castor and never relied upon by C&L for purposes of valuing the loans; and
- That Goodman applies a theory of offset that has no basis either in law or in accounting to overcome deficiencies.

[817] «*GAAP cannot be used to fool people and distort financial statements*»[843], says Plaintiff.

Defendants

[818] Defendants say GAAP requires that very specific evidentiary requirements be fulfilled in order to allow a departure from the known precision of contractually owed amounts to the subjective realm of "*best estimates*".

[819] As the preparer moves from the certainty of cost, he must ensure his estimate is reliable; he is required to follow specific GAAP evidentiary rules to support that adjustment.

[820] Defendants argue that a loan loss had to be both probable and estimable to be recorded under GAAP; absent one of these two elements, the only acceptable GAAP amount was "cost". GAAP did not permit speculation: GAAP required a loss to be probable rather than merely possible, before a provision was taken.

[821] Defendants insist that in determining whether a loss was probable, GAAP required that the lender's options be considered, but they recognize it has to be done within realistic assumptions, which are consistent with the lender's intentions and his financial and contractual ability.

[822] Defendants say that any analysis that fails to take into consideration Castor's business model, such as the Plaintiff expert's analysis, does not meet GAAP.

Experts' figures

[823] All Plaintiff's experts opine that LLP should have been taken in 1988, the lowest minimum LLP assessment being in the amount of $123.6 million as per calculations of Froese.

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[843] Vance, April 12, 2010, p.181

[824] Vance proposes a total minimum LLP of $184 million breaking down as follows:

Project/Category	Vance's proposed minimum LLP
MLV	54 million
YH Corporate loans	77.665 million
MEC	11 million
TSH	20.4 million
CHS	9.4 million
OSH	10.9 million

[825] Rosen proposes that LLP ranged between $182 to $271 million breaking down as follows[844]:

Project/Category	Approach A - Low	Approach A- High	Approach B- Low	Approach B- High
MLV	46.3 million	52.9 million	46.3 million	52.9 million
YH Corporate loans	79 million	91 million	87 million	99 million
MEC	3 million	13 million	3 million	13 million
TSH	18 million	20 million	33 million	35 million
CSH	3.8 million	14.4 million	12.8 million	23.4 million
TWTC	25 million	40 million	25 million	40 million
Meadowlark	7 million	7.6 million	7 million	7.6 million

[844] PW-3033, volume 2

[826] Froese proposes that LLP ranged between $123.6 to $152.9 million breaking down as follows[845]:

Project/Category	Low	High
MLV	43 million	43 million
YH Corporate loans	52,3 million	68,4 million
CHS	3,9 million	17,1 million
THS	24,4 million	24,4 million

[827] Goodman opines that no LLPs were needed.

[828] Goodman outlined a five step methodology and alleged that all his calculations had been made accordingly. Those five steps are:

- Step #1: Make a best estimate of the market value of the collateral security, deducting net liabilities that would be payable, which is "Castor's Value of Collateral Security";
- Step #2: Identify prior-ranking debt, property taxes payable and construction payables, to arrive at the "Value Available to Castor";
- Step #3: Compute the outstanding loans owing to Castor as at December 31 of each year (their cost);
- Step #4: Deduct the amounts in steps 2 and 3 from the amount in step 1, to determine whether there is a collateral surplus or deficiency, and its amount;
- Step #5: Determine whether a deficiency identified in step 4 indicates that it was probable that Castor would suffer a loss, or whether, after considering the options, intent and business arrangements, a loss was not estimable and probable.

[829] The more serious dispute between Plaintiff's' experts and Goodman is with respect to the value used for step 1 and the proper application of step 5 under GAAP given Castor's reality and Castor's borrowers' realities.

[845] PW-2941-4; PW-2941, volume 1, p. 33

Discussion

[830] The loans looked at by experts are largely the same, but Plaintiff's experts and Goodman used different groupings depending on the conclusions they reached as to the ownership of some properties or entities.

[831] The discussion of the LLP issue is done, in light of the burden of proof that rests on Plaintiff, by using Plaintiff experts' groupings and the following sub-headings: MLV, YH Corporate loans, MEC, TSH, CSH, OSH, TWTC and Meadowlark.

MLV

Experts' positions

[832] Plaintiff's experts opined that LLPs were required for MLV, the proposed minimum LLPs being:

- 54 million, according to Vance.
- 43 million, according to Froese.
- 46.3 million, according to Rosen.

[833] Goodman opined that no LLPs were needed for MLV.

Additional evidence specific to MLV

Prior to 1988

[834] In 1983, R.B. Mullins ("**Mullins**") of Mullins Realty Limited had been retained by Castor to appraise MLV as of March 1, 1983[846]. Using the Income Approach, Mullins had estimated the value of the property at 129 million (mid-point) and concluded that MLV had an estimated market value of 130 million, including all furniture, fixtures and equipment[847].

[835] In fact, between 1984 and 1987, MLV's income before interest, depreciation and income taxes was significantly less than that projected in the 1983 Mullins Report[848].

[836] In 1986, repeated statements of claim were filed by Great-West Life Assurance Company against MLVII for payment in relation to MLVII's default on payments under the terms of an $11 million mortgage loan[849].

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[846] PW-493
[847] PW-493, page 94
[848] Froese, PW-2941, volume 3, p.25

[837] Amounts due and payable to debenture holders on April 1, 1987 and October 1, 1987, totalling more than $6 million, were not paid[850].

[838] In 1987, MLVII received demands for payment of overdue property taxes from the City of Niagara Falls.

[839] Interest continued to be capitalized on the CHIF loans to MLV Investors.

[840] Statements made to Wightman during the year-end wrap-up meeting in the 1986 audit regarding reduction of the MLV loans[851] had failed to materialize, but the topic was not brought up at the year-end wrap-up meeting of the 1987 audit.

[841] Audited financial statements for MLV for the year ended September 30, 1987 were not available until early 1989. These audited financial statements for the year ended September 30, 1987 included a going concern note that highlighted an outstanding renegotiation of indebtedness, outstanding property taxes, and the need for continued financial support from related parties[852].

> Note 3 a
>
> (...) At September 30, 1987 accounts payable and accrued liabilities include property taxes of $3,172,709 (1986, $2,759,697) which were in arrears. The City of Niagara Falls filed a tax arrears certificate against the Company in the amount of $2,800,000.
>
> Note 3b
>
> The first mortgage due on demand was to have been renegotiated in January 1988. This renegotiation has not yet been achieved and as a result the full amount is now due.
>
> Term bank loan principal of $2,225,000 remained unpaid.
>
> The property tax arrears were paid in full on January 3, 1989 using the proceeds of a loan of $5 million. The loan matures March 31, 1989.
>
> Note 11
>
> The Company has received substantial financial support from related parties as more fully described in notes 4 and 9. As set out in notes 3 and 5, at January 3, 1989 the first mortgage bank loan has not been renegotiated and certain required payments on a term bank loan and the subordinated debentures had not been made.

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[849] PW-483 A to PW-483D
[850] PW-1070H-2
[851] PW-1053-3, p.474
[852] PW-478D.

> The Company is negotiating financing of $50 million to refinance existing mortgages and loans as well as providing approximately $15 million for refurbishment and new construction. At January 3, 1989 this financing, which will require the agreement of the holders of the subordinated debentures, had not been finalized.
>
> The successful negotiation of such financing and/or the continuance of the financial support noted above, which the related parties have agreed to continue, are required in order to ensure continued operations."

1988 Events

[842] The operations of MLV continued to encounter serious financial difficulties in 1988.

[843] In April 1988, Castor advanced its first direct loan to MLVII, beginning with a $2.75 million unsecured credit facility (loan 1105). A promissory note was provided by MLVII and guaranteed by YHDL. Castor's representatives were to sign all cheques on the bank account to which the loan proceeds were being advanced, along with YHHL personnel. The loan terms also gave Castor the ability to take control of MLVII's bank accounts at its discretion, as follows:

> "Castor Holdings Ltd. will receive and hold, undated, executed, revised banking resolutions for all bank accounts of Maple Leaf Village. In the interim, Castor reserves the right to control all cash flow of Maple Leaf Village until full repayment of the Grid Promissory Note."[853]

[844] This credit note facility (loan 1105) was to be used to fund MLVII's short term cash flow requirements and was to be repaid from cash flow over the summer of 1988 and "*the balance, if any, will be due and payable on September 15, 1988.*" Instead of being repaid by September 15, 1988, the loan balance increased to $3.1 million by December 31, 1988[854].

[845] From June to October 1988, negotiations took place to sell the hotel properties owned or managed by YHHL.[855]

[846] On August 18, 1988, further to the various discussions that had taken place, a conditional offer of $190 million was presented to YHHL. Said offer included the TSH, the CSH, the OSH, the Skyline Triumph Hotel, and the MLV Hotels[856].

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[853] PW-486 and PW-486A.
[854] PW-1053-23-10, sequential page 80
[855] Prychidny, November 4, 2008, pp. 229 and following; D-1034, D-1035, PW-499, PW-499A, PW-499B, PW-499D, PW-499E, PW-499F and PW-2928
[856] PW-499

[847] YHHL made a counter-offer[857], excluding the Skyline Triumph Hotel, and proposed to increase the price to $215 million, net of commissions, based on the following values[858]:

Property	Amount
TSH	$93 million
CSH	$50 million
MLV (Foxhead, Brock, Village Inn)	$70 million
OSH	$10 million

[848] In the Niagara Falls Review newspaper dated July 30, 1988, an article entitled "*Only five months remain before city takes hotels*" stated that MLVII had been given one year from January 1988 to pay the overdue taxes or the City would take over and sell the properties to make up for unpaid taxes.[859]

[849] On September 2, 1988, First Interstate Bank ("**FICAN**") demanded payment further to MLVII's default under its loan agreement[860]. Defaults disclosed in the letter included the failure to pay principal and interest punctually, the failure to pay Worker's Compensation Board assessments and the failure to advise FICAN of defaults under loan covenants. FICAN namely wrote to MLVII:

> Over the course of the past year, you have made several representations and promises to us with respect to repayment of our loan facilities through alternate financing. The bank is not satisfied that reasonable progress has been made by you to fulfil your representations and meet your continuing obligations to the bank[861].
>
> (...)
>
> As you know, the bank is required to advise Castor Holdings (Quebec) Ltd. of any default under the priorities agreement dated April 17, 1984, as amended, to which you are a party. Accordingly, we have given Castor Holdings formal written notice that there are defaults under the provisions of the original loan agreement, as amended[862].

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[857] PW-499B; D-1035.
[858] PW-499B and PW-499F
[859] PW-1070G-3.
[860] PW-481 and PW-1077.
[861] PW-481, p.1
[862] PW-481, p.3

[850] In September 1988, Great-West Life introduced a court claim against MLVII before the Supreme Court of Ontario for reimbursement of its mortgage[863].

[851] On October 20, 1988, National Bank sent a demand letter stating its loan had been in default since January 1988 and requesting MLVII to make payments to bring the interest current[864]. National Bank namely wrote:

> As you are aware, despite our repeated requests for payment, interest of $157,087.10 for August 1988 and $165,927.97 for September 1988 are currently overdue and on October 25, 1988, interest for October 1988 will be due.
>
> The Bank is not prepared to tolerate this situation any longer.

[852] From September to December 1988, National Bank and FICAN exerted substantial pressure on MLVII to bring current MLVII's outstanding debt. During the same period, YHHL attempted to obtain further payment postponements, the reason being to complete a proposed refinancing with Mellon Bank Canada ("**Mellon**")[865].

[853] On December 5, 1988, Mellon proposed to MLVII its terms for a syndicated mortgage loan: Mellon would fund $50 million, with no more than $25 million syndicated to other lenders, to refinance existing first and second mortgage loans and finance improvements for the hotel complex. Those terms and conditions required that MLVII achieve stabilized net funds available for debt servicing of $5.5 million ($4.1 million from hotel operations and $1.4 million from non-hotel operations) before $44.8 million of the loans would be advanced. The preconditions for the Mellon financing also included Mellon's request that the collateral valuation of the land and improvements, as at completion of improvements, be in excess of $80 million[866].

[854] Castor provided a $5 million standby loan to MLVII[867] to "bridge finance" MLVII's obligation to pay the property taxes pending the closing of the Mellon commitment for a first mortgage financing[868]. As per Castor's request, the 5 million was paid to McLean & Kerr in Trust to pay property arrears to the City of Niagara Falls by certified cheque.[869]

[855] On January 4, 1989, the Globe & Mail published an article disclosing that MLVII's overdue property taxes of $4.2 million had been paid one day before the property would have been seized by the City of Niagara Falls, an article which was included in Castor's loan files for MLVII[870].

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[863] PW-1070F, tab 4 (also - PW-483E-1)
[864] PW-482.
[865] PW-481A to PW-481F.
[866] PW-492.
[867] PW-485B
[868] PW-1450-6
[869] PW-1070G-5; PW-1070G-6
[870] PW-1070G-8

[856] MLVII's revenue for the year ended September 30, 1988 declined from $19.4 million in 1987 to $18.3 million in 1988 and its income before depreciation declined from $825,755 to a loss before depreciation of $6.7 million. A footnote to the financial statements stated "*The above does not include management agreements for 1988 year end*"[871].

[857] The December 1988 Month End Report dated December 31, 1988 for MLVII included the following in its Executive Commentary:[872]

> Our cash position is at an intolerable level. We do not have the funds to meet current requirements and therefore maintenance and marketing programs will suffer.

[858] The said report also included occupancy statistics for the year ended December 31, 1988, summarized as follows[873]:

- Occupancy rate of 40.3% versus a budgeted occupancy rate of 44.3%;
- Average room rate of $79.78 versus a budgeted average room rate of $81.80; and
- Total room revenue of $9,889,118 versus budgeted room revenue of $11,145,592.

[859] Interest due to the debenture holders by MLVII was funded by Castor, through Account 046 or by bank transfer, and amounted to more than 6 million.[874]

[860] The hotels were incapable of meeting their obligations and would have been lost without Castor's support[875]. The MLV project did not generate sufficient operating income to meet its first mortgage payments. In 1988, the project generated $4 million of net income before debt, but its annual interest obligations alone represented $20.4 million. Real estate taxes were paid one day before the City of Niagara would have sold the property for taxes[876]. No money was available from YH to support the MLV project[877].

[861] MLVII no longer produced audited financial statements.

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[871] PW-478E
[872] PW-478-F, bates 000140
[873] PW-478F, bates 000162
[874] PW-1070H-1
[875] Prychidny, October 14, 2008, pp. 44-48
[876] Prychidny, October 15, 2008, pp. 50-52; PW-1053-23, seq. p. 163 (note 3a).
[877] Prychidny, October 15, 2008, p. 111; October 14, 2008, pp. 49-52, 72-75, 83-85. 88-90.

[862] As at December 31, 1988, MLVII's 1988 unaudited financial statements disclosed the following information[878]:

- Mortgages and loans of $30.7 million[879];
- bank indebtedness of $7 million[880];
- accounts payable and accrued liabilities of $8.8 million;
- a payable to YHLP of $32.4 million, accrued interest on debentures payable to shareholders of $218,372 and a receivable from shareholder (YHLP) of $33.4 million[881].

Loans as of December 31, 1988

[863] At December 31, 1988, $96 million were owed to Castor in relation to MLV (some to CHL and some to CHIF):

Loans owed to CHL

- Loan 1105 to MLVII[882] – 3.1 million
- Loan 1048 to YHLP[883] – 14 million secured by a pledge of shares
- Loan 1125 to KVW investment ("**KVWI**") [884] – 7.2 million
- Loan 1011 to Harling International[885] – 3 million
- Loan 1012 to Runaldri S.A.[886] – 2 million
- Loan 1013 to Charbocean Trading[887] – 4 million
- Loan 1014 to Harling Finance[888] – 7.5 million
- Loan 1015 to Gebeau Overseas[889] – 5 million

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[878] PW-478G
[879] PW-478G, note 3
[880] PW-478G, note 3
[881] PW-478G, note 4
[882] PW-1053-23-17
[883] PW-1072-4A; PW-1053-23-8; PW-1053-23-17; PW-1053-23-10 (sequential page 80).
[884] PW-1073-5A; PW-1073-5; PW-1053-23-8; PW-1053-23-17; PW-1053-23-10 (sequential page 81).
[885] PW-1053-23-8; PW-1053-23-1 PW-1053-23-10 (sequential page 80).
[886] PW-1071-6-8; PW-1053-23-1 PW-1053-23-10 (sequential page 80).
[887] PW-1071-5-1; PW-1071-5-8; PW-1053-23-1
[888] PW-1053-23-8; PW-1053-23-1; PW-1053-23-10 (sequential page 80).

- Loan 1016 to Gebeau Holding[890] – 2.420 million
- Loan 1017 to Harling International[891] – 3 million
- Loan 1018 to Trade Retriever[892] – 2.280 million
- Loan 1019 to Trade Retriever [893]– 2.220 million

Loans owed to CHIF[894]

- Loan 770001/0009 to Runaldri – 3.678 million
- Loan 26100/0004 to Charbocean Trading – 7.297 million
- Loan 385005/3010 to Gebau Overseas - 8.349 million
- Loan 385009/3005 to Gebau Overseas – 3.320 million
- Loan 385009/0003 to Gebau Overseas – 1.895 million
- Loan 38500/0008 to Gebau Overseas – 0.850 million
- Loan 38500/0004 to Gebau Overseas – 3.704 million
- Loan 441004/3010 to Harling International – 4.5 million
- Loan 441004/0008 to Harling International – 6.697 million
- Loan 890000/0010 to Trade Retriever – 4.617 million

[864] Loan 1048 to YHLP was secured by a pledge of 190,200 common shares of MLVII and 6,019 preferred shares of MLVII owned by YHLP.

[865] Loan 1125 to KVWI was secured by a pledge of 500,000 common shares of YHLP and a guarantee provided by YHLP.

[866] Loan 1105 was an unsecured loan.

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[889] PW-1071-7-9; PW-1053-23-8; PW-1053-23-1; PW-1053-23-10 (sequential page 80).
[890] PW-1071-4-14; PW-1053-23-8; PW-1053-23-1; PW-1053-23-10 (sequential page 80).
[891] PW-1071-2-10; PW-1071-2-11; PW-1053-23-8; PW-1053-23-1; PW-1053-23-10 (sequential page 80).
[892] PW-1071-8-11; PW-1053-23-1; PW-1053-23-10 (sequential page 80).
[893] PW-1071-9-6; PW-1053-23-1; PW-1053-23-10 (sequential page 80).
[894] PW-1076A-1

[867] Loans 1011 to 1019 made by CHL were secured by a pledge of all debentures of MLVII owned by the borrowers and the debentures were themselves secured by mortgages against the property as well as other assets of MLVII.

[868] Loans owed to CHIF, all owed by MLV investors (debenture holders), were secured by a pledge of all debentures, all common shares and all preferred shares of MLVII owed by the borrower, and the debentures were themselves secured by mortgages against the property as well as other assets of MLVII.

Interests recognized as revenue

[869] In 1988, Castor recognized interests totalling $7,195,291.88 as revenue on MLV related loans[895].

Loans and commitment letters

[870] The terms and conditions of the commitment letters and extension letters as well as the loan documentation in connection therewith called for the payment of monthly interest, annual fees and the supply of financial information[896]. The borrowers were in chronic breach of all such covenants.

MLV appraisals

[871] No 1988 Mullins appraisal existed[897]: the Mullins appraisal was dated 1983[898].

[872] A valuation of the hotel portion of Maple Leaf Village, dated July 1988, was prepared by R.W. Hughes & Associates Inc. (the "**Hughes report**").[899] The hotel portion of MLV, as defined by the Hughes report, included: Foxhead Hotel, Brock Hotel, Village Inn, the parking area, and Tussaud's Wax Museum. It excluded the Shopping Mall and the Amusement Park[900].

[873] The Hughes report concluded that the estimated current value of the hotel portion of MLV, as at July 31, 1988, was in the range of 66.4 to 70.4 million and that the most probable single value was 67.7 million[901].

[874] The Hughes report also included an evaluation of the property's future potential estimated at 104 million[902] on the following basis:

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[895] PW-1075A
[896] For example, see: PW-1071-1 to PW-1071-9; PW-1072 (series); PW-1073 (series) and PW-1074 (series)
[897] Ron Smith, May 16, 2008, pp.53-54
[898] PW-493
[899] PW-494
[900] PW-494, bates 000043
[901] PW-494, bates 000008
[902] PW-494, bates 000009

> "(...) on the owner effectively completing enhancements to the hotels in the amount of $4,000,000 to $6,000,000. This is in addition to the $7,300,000 of Basic Upgrading required to meet the Pannell Kerr Forster income forecast. In addition, this estimate of the property's future potential includes the owner's proposed new 37,600 square foot retail corridor between Clifton Hill and the existing Maple Leaf Village Mall."

[875] In providing a future potential estimated value, the authors of the Hughes report included the following disclaimer "*There are no guarantees that this level of value will be achieved.*"

[876] The appraisal conclusions of the Hughes report were intended to be read in conjunction with a June 1988 Pannell Kerr Forster Market Position Study (the "**1988 PKF Report**")[903] which included the assumed increases in revenue of the hotel portion of MLV which themselves were based on the properties being upgraded, such upgrading being a critical factor.

[877] The Hughes report and the 1988 PKF Report were sent to Ron Smith of Castor on September 21, 1988[904].

[878] There was no appraisal available in 1988 for the Shopping Mall and the Amusement Park. However, an appraisal for the Shopping Mall which indicated a value of 26 million was obtained in March of 1989[905].

Other information

[879] The renovations which were to be implemented were never completed and the hotels were never upgraded[906].

[880] In Prychidny's words, *YH was an absentee owner of what the locals called the "Make Believe Village".*[907]

[881] The operations of the MLV project were seasonal: its peak occupancy period was in July and August; its minimum occupancy period, in winter.

[882] MLV's operations were problematic.[908] Castor not only funded operating deficits,[909] but had to make systematic and ongoing support payments to lenders in an attempt to counter foreclosure proceedings[910].

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[903] PW-495
[904] PW-494-1
[905] PW-496
[906] R. Smith, May 15, 2008, pp. 135-149; Prychidny, October 14, 2008, pp.217 and following
[907] Prychidny, October 15, 2008, pp. 50-51.
[908] See, for example, PW-1070G-2, PW-1070G-3, PW-1070G-4.
[909] PW-1070H.
[910] See, for example, PW-1070F-2, PW-1070F-4, PW-1070F-5.

[883] Prychidny testified that as a result of serious efforts to try to sell, only one offer was received: it was in the amount of $90-100 million, and for the entire MLV project[911] .

> an offer not just for the hotels but an offer for the whole complex, which included the three (3) hotels, the shopping mall and the amusement park assets, the whole seventeen (17) acres site[912].

[884] Prychidny added "*That was the top and I thought a very reasonable and fair price.*" [913]

[885] Wightman never saw the appraisals relating to the MLV project[914].

[886] In the 1988 working papers, Wightman wrote beside his MLV inscription "for sale at $90-100 million".[915]

Experts' evidence

[887] Plaintiff's experts (Vance, Rosen and Froese) asserted that a LLP was required in respect of Castor's loans that were secured by and associated with the MLV project.

[888] Because of the chronic defaults of Castor's borrowers in connection with the MLV and their obvious inability to service the interest or fees due to Castor, all the capitalized interests and fees recorded by Castor in connection with the MLV loans should have been reversed - had such reversal taken place, the required LLP would have been reduced accordingly[916].

[889] In his computation of the proposed LLP, Vance used the total value figure of 93.7 million: 67.7 million for hotels and museum and 26 million for mall, tower and park. Vance mentioned that he had not taken account of the investment in 705743 Ontario, and he explained why[917].

[890] In his computation of the LLP, Rosen used two approaches taking account of low and high value figures[918]: 104 million and 115 million[919].

[891] In his computation of the proposed LLP, Froese used the total value figure of 102.3 million: 67.7 million for hotels and museum, 26 million for mall, tower and park,

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[911] Prychidny, October 14, 2008, pp. 210-214
[912] Prychidny, October 14, 2008 pp.211-212
[913] Prychidny, October 14, 2008, p.214
[914] Wightman, February 25, 2010, p. 42.
[915] PW-1053-23-16, sequential page 117
[916] Vance, PW-2908, Vol. 1, pp. S-8 to S-10.
[917] Vance, PW-2908, Vol. 2, pp. A-3 to A-5 and Vol. 3, section on MLV.
[918] PW-3033, volume 2, tab D, p. 6-7
[919] Rosen, PW-3033, Vol.2, section D, pp.34-38

1.355 million for current assets, $773,000 for a net receivable from shareholder and 6.460 million for an investment in 705743 Ontario[920].

[892] In his report, Goodman namely wrote that:

- *the MLV properties were distressed properties that were performing poorly, and certainly far below the financial projections that were set out in the various appraisals, whether with or without the financial support arrangements offered by the YH Group;*
- *Castor had to continually "bail out" the YH North American Group in order to keep the MLV properties in operation as going concerns;*
- *Castor capitalized significant interest over the 1988 to 1990 period and that as a result, MLV's loans from Castor increased materially;*
- *The YH Group of companies were insolvent during the 1988 to 1990 period.*[921]

[893] In his computation of the proposed LLP, Goodman used the total value figure of 124.2 million: 117.7 million for hotels, Tussaud's wax museum, Mall and Amusement Park (26 million for Mall and Amusement Park plus 104 million for Hotels, less 12.3 million for the cost of enhancements and upgrades) plus 6.5 million for the investment in 705743 (amusement park assets)[922].

[894] Concerning any possible sale of MLV during 1988, Goodman said:

> Q.-So during that period of time, isn't it a fact that neither Castor or York-Hannover were able to obtain any offer for the entire MLV complex that was higher than the ninety (90) to one hundred (100) million dollars that Mr. Prychidny testified about from the Okabi group?
>
> A- I'm not aware of any... any other offer other than the one that Mr. Prychidny talked about (...)[923]

[895] Goodman agreed there was a shortfall in MLV[924]. He assessed the deficiency at $21.6 million[925]. He wrote:

> I am of the view that the best estimate of Castor's security value supporting its loans amounted to $75.1 million as at December 31, 1988. After deducting the

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[920] Froese, PW-2941, Vol.3, pp.55-56 and PW-2941-4
[921] D-1312, p. 363
[922] Goodman, D-1312, p. 347
[923] Goodman, November 30, 2009, p.91
[924] Goodman, November 30, 2009, pp.67-68
[925] D-1312, p. 347

> balances outstanding on Castor's loans, there was a deficiency of $21.6 million which would have been recovered from the application of surplus Gambazzi, in Trust deposits or from the WOS/KvW guarantees. According to the C&L audit working papers, the surplus of Gambazzi, in Trust deposits over Gambazzi, in Trust loans was more than sufficient to cover the $21.6 million deficiency[926].

[896] Goodman concluded that Castor's assertion that no LLP was required on this group of loans was reasonable under GAAP despite the existence of a loan security deficiency when considering the property values alone. He opined that two other sources allowed him to conclude accordingly: Wersebe and Stolzenberg's guarantees to debenture holders and Gambazzi in Trust deposits.

[897] Goodman described Wersebe and Stolzenberg's guarantees as follows:

> the guarantees that are... that I'm noting as the KVW and WOS guarantees are guarantees that were made to the MLV investors that would allow the MLV investors to put their loans back to WOS and KVW in the event that the syndication of the MLV investor positions did not proceed in accordance with the plans they had in nineteen eighty-one (1981), eighty-two ('82) and nineteen eighty-three (1983)[927].
>
> Trade Retriever, under this agreement, is allowed at any time to tender its interest in Maple Leaf Village to the guarantors, being Karston Von Wersebe and Mr. Stolzenberg, and those two individuals have agreed they will assume all the obligations and repay any and all outstanding principal and interest on a promissory note on its final maturity, provided that any amounts collected are offset against it.[928]

[898] Goodman acknowledged that Wersebe and Stolzenberg's guarantees, to which he was referring, concerned only some of the debenture holders and had nothing to do with CHL loans to MLVII, YHLP or KVWI.

> I am not suggesting at all that Mr. Von Wersebe guaranteed any of the Castor Holdings Limited indebtedness, and just so that we're all on the same page, so no, there would not... I'm not suggesting that there was a guarantee by KVW of loans 1105, 1126, 1136, 1048 or 1125[929].

[899] Had MLV been sold and the proceeds been distributed, according to Goodman the various debts would have ranked in the following order:

- Great-West, FICAN and National Bank (34.6 million)[930]

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[926] D-1312, p. 348
[927] Goodman, November 30, 2009, p. 110
[928] Goodman, November 30, 2009, p.115
[929] Goodman, November 30, 2009, p.57
[930] Goodman, November 30, 2009, p.75-76

- CHL debenture holders loans (31.6 million)[931]
- CHIF debenture holders loans (40.3 million)[932]
- CHL loans to MLVII (loan 1105)[933]
- CHL loan to YHLP (loan 1048) and CHL loan to KVWI (loan 1125)[934].

[900] When Goodman was asked whether it was consistent with Castor's intent to sue Stolzenberg and Wersebe to collect loans made to debenture holders, he answered: *It's consistent with Castor's option; I couldn't tell you whether Castor had the intent to sue Mr. Von Wersebe or Mr. Stolzenberg on this amount. I didn't see anything that indicated that they intended to do that, all I say is they have the option*[935].

[901] In his cross-examination, Goodman acknowledged the Court should not infer that each of the CHIF debenture holder loans was guaranteed by Wersebe and Stolzenberg, or that each of those loans was pledged by deposits (Gambazzi in Trust deposits).

> I do the same in respect of Gambazzi, and then I stand back and I say, okay, I have all of this in front of me, what do I do, do I have a probable loss, yes or no? And so...
>
> Q- But...
>
> A- ... that's the way I'm looking at it, it's not sort of A plus B plus C plus D.
>
> Q- Okay. Well, I'm going to ask you, then, again, are you suggesting to the Court that the Court should infer that each one of the CHIF debenture holder loans in the box MLV.9 were guaranteed by KVW and WOS, even though you don't have agreements for those other loans, and are you asking the Court to infer that each one of the loans in the box MLV.9 was pledged by deposits? That's my simple question.
>
> A- No.
>
> Q- Not whether you should take a loss or not.
>
> A- No.
>
> Q- So the Court... you're not asking the Court to infer documents that don't exist?

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[931] Goodman, November 30, 2009, p.76-77
[932] Goodman, November 30, 2009, pp.77-78
[933] Goodman, November 30, 2009, p.78
[934] Goodman, November 30, 2009, p.78-79
[935] Goodman, November 30, 2009, p. 118

A- No. No[936].

[902] Goodman acknowledged that options totally unrealistic could not and should not be taken into account[937] – as, for example, an enforcement option that Castor would never exercise.

[903] All experts used the same two appraisals,[938] but they applied GAAP differently to them, and they differed in their consideration of the value of security available to Castor.

[904] Goodman's analysis[939] valued the amusement park rides, which were held by 705743 Ontario Ltd., a wholly owned subsidiary of MLV, at 6.5 million, as described in note 10 of MLV's financial statements. Froese[940] also included a 6.5 million loan security value in respect of these rides. Neither Vance nor Rosen asserted value to this asset in their computations.

[905] Two main factors make up for the difference of 54 million between Vance's and Goodman's conclusions on the LLP: 30.5 million in value figures and 21.6 million in possible recovery through other sources[941].

[906] The same two factors make up for the difference of 43 million[942] between Froese's minimum LLP and Goodman's conclusions on LLP: 21 million in value figures and 21.6 million in possible recovery through other sources[943].

[907] At least 9.2 million in value figures and 21.6 million in possible recovery through other sources make up for the difference of 46.3 million between Rosen's minimum LLP and Goodman's LLP conclusions[944].

Conclusions

Value and minimum deficiency before other recovery sources

[908] In the specific factual circumstances of MLV as herein above described, in light of the disclaimer clause of the appraisal report regarding the 104 million value and since the hotels were nowhere close to satisfying the basic assumptions used by the

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[936] Goodman, November 30, 2009, p. 131
[937] Goodman, November 30, 2009, p.106-107
[938] PW-494, PW-494-1 and PW-496
[939] Goodman, October 5, 2009, pp.126-160
[940] Froese, January 6, 2009, pp.244-246
[941] D-1312, p. 360
[942] Froese, January 27, 2009, pp. 95 and following and PW-2941-4, Schedules 1 and 2
[943] D-1312, p. 375
[944] D-1312, p. 383

appraisers (renovations and projected earnings), this 104 million figure cannot reasonably be used to value the hotels.

[909] Evidence shows that the 1988 market value for the entire MLV project was in the range of 90 to 100 million. The offer that was made in August 1988 and the figures used in preparation of the counter-offer[945] constitute highly relevant value indicators in light of Prychidny's testimony relating thereto, a testimony that the Court finds credible and reliable[946]. Moreover, said figures were noted by Wightman in the 1988 working papers. The Court does not believe Wightman's testimony that he would have been told that these figures represented only part of the project[947].

[910] Based on a 100 million total value, the minimum deficiency on MLV is $48.3 million.

Other possible sources of recovery

[911] Goodman's suggestion that there would have been other possible sources of recovery to be taken into account by Castor in preparation of its financial statements does not hold water. Had it been the case, Castor would not have taken, as it did, a 5 million LLP on MLV in 1990.

[912] The available value to Castor based on Goodman's figures would have been sufficient to cover Castor's loans ranking in 2nd and 3rd place, had MLV been sold, but it would not have covered Castor's loans ranking in 4th and 5th places.

[913] Those loans which would have ranked in 4th and 5th places have nothing to do with any of Wersebe's or Stolzenberg's possible guarantee or Gambazzi's deposits in Trust, as Goodman acknowledged.

[914] Needless to say that, in all circumstances, suing Stolzenberg or Wersebe is unrealistic – it is an enforcement option that Castor never contemplated and would not have exercised.

Required LLP

[915] A minimum LLP of at least $40 million was required for MLV in 1988.

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[945] PW-499 B
[946] Prychidny, October 14, 2008, pp. 210-214
[947] Wightman, February 11, 2010, pp. 201-202

YH Corporate loans

[916] The following loans were looked at by all Plaintiffs' experts under the grouping "YH Corporate loans". They are loans made by Castor and CFAG to YH entities to reallocate, on an annual basis, unpaid interest, fees and support payments due to Castor by various members of the YH Group. These loans totalling 74.4 million do not relate to advances made for completion of a specific project.

- Loan 1123 to KVWIL
- Loan 1081 to YHDHL
- Loan 1092 to YHDL
- The CFAG Loans to YH

[917] Vance also looked at Loan 1091 by CHL to YHDL in the amount of 29 million[948]. Therefore, he discusses 103 million of YH Corporate loans for 1988.

[918] Rosen discusses 124.3 million of "YH Corporate loans" since he looked also at the following loans under this grouping:

- Loan 1090 to YHDL (Options) – 3.3 million
- Loan 1091 by CHL to YHDL in the amount of 29 million[949]
- Various loans made by CHIF to Harling and to KVWIL, for a total of 17.6 million[950]

[919] Froese also looked at "G/L Account[951] 046/loan 1153" in the amount of 1.8 million and at Loan 1090 to YHDL (Options) in the amount of 3.3 million. Therefore, he has 79.5 million of YH Corporate loans for 1988[952].

[920] KVWIL and YHDHL were holding companies, and YHDL, an operating company.

Additional evidence specific to the YH corporate loans

CFAG loans (20 million) prior to 1988

[921] In 1981, CFAG made 20 million of unsecured loans to YH by way of five separate promissory notes, each bearing interest at prime plus 6% and having a term of five years and four days from its signature date[953].

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[948] PW-1059-6 and PW-1053-23-3, sequential pages 180-182 and 270
[949] PW-3033, Vol. 2, Section C, p.4; PW-1059-6 and PW-1053-23-3, sequential pages 180-182 and 270
[950] PW-3033, Vol. 2, Section C, p.4
[951] General ledger account
[952] PW-2941, vol. 4 p. 15

[922] These five unsecured loans of 20 million represent virtually the totality of the CFAG loan portfolio through the years.

[923] On December 16, 1982, an agreement was signed between YHDL, YHHL and Investamar in relation to 20 million of debts[954] resulting from five promissory notes apparently issued in 1981 and maturing at various dates in 1986.

[924] In its 1984 audit working papers ("**AWPs**"), C&L added a handwritten inscription on a confirmation letter drafted on Investamar's letterhead: "*After receipt of these conf. Investamar SA will confirm to Castor Finanz AG that these confirm were received on AG's behalf*"[955]. The AWPs indicated that the amounts had been agreed to the general ledger ("**G/L**") in relation to loans 158004, 158104, 158204, 158304 and 158404 of CFAG to YH. The 5 loans were maturing at various dates during 1986, as per inscriptions appearing on the unsigned confirmations[956].

[925] In its 1985 AWPs, C&L listed the five loans of CFAG to YH (loans 158004, 158104, 158204, 158304 and 158404). C&L noted that loan 158004 was maturing in 1987 while the other four were maturing at various dates in 1988[957] - those maturity dates match perfectly the maturity dates agreed to in the 1982 agreement between Investamar, YHDL and YHHL[958]. Confirmations on Investamar letterhead were again included in the AWPs[959] with a handwritten note at the bottom of one of those confirmations similar to the one made the previous year but for the following words which were added: "*Practice consistent with prior years (Loans I to V)*"[960].

[926] In its 1986 AWPs, C&L listed the 5 loans of CFAG to YH (loans 158004, 158104, 158204, 158304 and 158404) with confirmation numbers 5003 to 5007 in the margin and maturity dates (1987 for loan 158004 and various dates in 1988 for the other four loans)[961].

[927] In its 1987 AWPs, C&L listed those 5 loans of CFAG to YH (loans 158004, 158104, 158204, 158304 and 158404) all maturing in 1988[962].

[928] G/L account 046 was used over the years to capitalize interests in CHL on these 20 million loans of CFAG[963].

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[953] PW-1177-1.
[954] PW-1178
[955] PW-1053-99,sequential page 260
[956] PW-1053-99, sequential pages 259 to 264
[957] PW-1053-97, sequential page 287
[958] PW-1178
[959] PW-1053-97, sequential pages 290 to 294
[960] PW-1053-97, sequential page 290
[961] PW-1053-95, sequential page 261
[962] PW-1053-93, sequential page 197

Account 046 (Before 1988)

[929] The YH account (G/L account 046 ("**account 046**")) is explained as follows in C&L 1985 AWP:

> "YH's account gets built up from interest accruing on YH loans, and drawn down by being reclassified to new mortgage loans." "Advance to YH @ P + 6% unsecured"[964]

[930] C&L's 1986 AWPs include the following explanation of G/L account 046:

> "This account though gets built up from interest accruing on YH loans & down by being reclassified to new mortgages."[965]

[931] Each month, journal entry number 6 ("**JE# 6**") was recorded to reallocate interest income receivable for various YH loans to account 046. Most of the time, JE # 6 was supported by detailed memos.

[932] By journal entry number 12 ("**JE#12**"), CHL recorded transactions relating to "Zug" and, namely, interest income receivable of CFAG on its 20 million loans to account 046. Most of the time, JE#12 was supported by detailed memos.

[933] At year-end, account 046 was reduced by re-allocating the indebtedness to YH projects (existing or new loans).

Castor and YH : "equity partners" prior to 1988

[934] Whiting explained that Wersebe considered Castor «*to be an equity partner*»[966]. The YH group and representatives surely acted accordingly.

[935] Smith explained that the genesis of this unfortunate "*partnership*" was that from the beginning, Castor was the "*financing arm*" and YH was the "*investment arm*". Rather than acting as a lender, Castor effectively assumed and inherited all of YH's risks:

> «All of the projects that we were involved with, we were basically supplying the equity to their positions or secondary mortgage positions, or else we gradually took over the first mortgage positions. So, it was always Castor's... Castor was at risk, so all of that leverage that York-Hannover had in their own system, they effectively transferred over to Castor and it became our risk, and as a result of it, there just wasn't enough cash flow coming in to satisfy all of that debt we required, all of the debt service that was required on that risk. So, effectively, we

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[963] PW-88; For example see the following exhibits - for 1986, PW-82 bates 000130, 000287 and 000289; for 1987, PW-83, bates 000188, 000189, 000261 and 000263; for 1988, PW-84, bates 000183, 000185, 000396 and 000508

[964] PW-1053-83-5

[965] PW-1053-35-6

[966] Whiting, November 16, 1999, pp. 130-136.

> inherited York-Hannover's leverage and we just kept adding to it to support it, but they never corrected the situation, they couldn't sell off their projects fast enough, they couldn't generate from their own operations to pay us down, and Castor's interest just snowballed and grew, so our own leverage position then got to a point where we had to finance interest on interest on interest year after year, and what we're doing is basically increasing our own leverage position, and you can't live with that forever, you're going to get caught at some point in time.[967]»

[936] No underwriting standards whatsoever were associated with the granting of loans or the systematic renewal of such loans at each maturity date. These loans were made because that was the only manner in which Castor could recognize interest and fee income on outstanding non-performing loans[968].

[937] Between 1982 and 1987, CHL assets grew from 111 million to 388 million[969]. Significant portions of the increase of assets were loans to the YH group, many of which were created pursuant to capitalization of interest and year-end re-allocation through account 046[970]. CHL's growth significantly depended on lending to YH[971].

1986 year-end re-allocation

[938] By 1986, Castor had run out of YH projects on which to re-allocate the ever increasing (snowballing[972]) YH indebtedness. At year-end 1986, Castor's loans to YH moved primarily from mortgage lending to unsecured equity financing and «*further and further away from the projects*»[973].

Loan 1081 prior to 1988

[939] The purpose of this loan of CHL to YHDL (at the time) was described in a commitment letter dated December 23, 1986 as follows: "*To provide a blanket Fixed and Floating Charge Debenture financing on the assets of the Borrower for the purpose of bridge financing the sale and refinancing of the various assets of the Borrower*"[974]. This commitment letter was for a $25 million loan at an interest rate of prime plus 6%, a factor that an auditor would consider indicative of a high risk loan, according to Froese.

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[967] R. Smith, October 2, 2008, p. 62.
[968] R. Smith, May 14, 2008, p. 137.
[969] PW-5A, tab 6 (1982) and tab 11 (1987) (unconsolidated audited financial statements of CHL)
[970] PW-88A
[971] Froese, November 26, 2008, pp.125-130
[972] Vance, April 9, 2008, p. 178; R. Smith, September 3, 2008, pp. 88-89, R. Smith, October 2, 2008, p. 62
[973] R. Smith, May 14, 2008, p. 56-63 (extract from page 60)
[974] PW-1054-1

[940] Castor and YH had agreed that this loan to YHDL was to be put in place on an interim basis only; they intended to substitute later YHDHL for YHDL, as the borrower[975].

[941] At year-end 1986, loan 1081 was used to transfer 25 million from account 046. After such transfer, the balance left in account 046 was 2.2 million[976].

[942] Consistent with the plan agreed upon earlier, a commitment letter dated April 14, 1987 transferred the 25 million loan from YHDL to YHDHL. The security listed in the loan summary included an unconditional guarantee of Wersebe in the amount of 12.5 million. The loan was also secured by a pledge of YHDHL's shares, a pledge of YHDL's shares owned by YHDHL and a specific assignment of 30 million of YHDHL's loan receivables. Payments were to be made quarterly, consisting of $375,000 of principal plus accrued interest, with the first payment to be made on November 1st 1987.

[943] Payment was not made on November 1st 1987, notwithstanding a specific demand for payment[977]. Whiting had informed Castor that "*the only way York-Hannover could make the payment would be if Castor lent them the money.*"[978]

[944] Castor considered calling its loan to YHDHL (loan 1081) as early as 1987[979], but it never pursued any enforcement actions on any of its YH corporate loans.

[945] A commitment letter dated December 15, 1987 increased loan 1081 from 25 to 30 million[980].

Loan 1092 prior to 1988

[946] A commitment letter dated December 15, 1987 described the purpose of a new 10 million loan to YHDL as follows: "*To provide interim financing of $10 million secured by specific assignment of various loan receivables of the Borrower*"[981].

[947] The receivables provided as security consisted of receivables from YH Greenwich Inc., Skyline (1980) and Triumph Hotel limited Partnership[982].

[948] The commitment letter also contemplated a 5 million personal guarantee from Wersebe but the item was crossed out in the loan summary attached to the commitment letter[983].

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[975] PW-1054-2
[976] PW-77 (account 046)
[977] PW-1054-6-1 and PW-1054-6-2
[978] PW-1054-7
[979] PW-1054-6-1, PW-1054-6-2, PW-1054-7; PW-1054-8, PW-1054-11
[980] PW-1054-10
[981] PW-1060-1, page 2
[982] PW-1060-1A, Tab 4
[983] PW-1060-1

[949] The closing documents included an acknowledgement that the 10 million had been advanced by way of a reduction of the inter-company indebtedness of YHDL to Castor on December 31, 1987[984] (a reduction of the balance in account 046[985]).

[950] At December 31, 1987, the unaudited financial statements for Skyline (1980) disclosed a deficit of $10 million and suggested that the receivables from Skyline (1980) provided as security to Castor on loan 1092 would not be repaid in the short-term from normal operations and might be impaired[986].

Loan 1090 prior to 1988

[951] A new loan of 3.3 million to YHDL *"to provide interim financing secured by the pledge of the Borrower's options to repurchase a 6.25% interest in the Toronto World Trade Center Inc. ("TWTCI") and repurchase the Skyline Triumph Hotel ("Hotel") together known as the "Options"* was granted by a commitment letter dated December 15, 1987[987].

[952] On exercise of the TWTCI option, YHDL would be required to pay $5.9 million, subject to certain adjustments[988].

[953] On exercise of the Triumph option, YHDL would have amounts to pay – these amounts would vary depending on the time period, and failure to exercise the option by a certain date would entail consequences (discharge of mortgages and other financial penalties)[989].

Financial situation - 1987 year-end

[954] The 1987 AWPs included the September 30, 1986 audited financial statements of YHDL[990]. No subsequent financial statements of YHDL were ever sought or reviewed by C&L.

[955] By the end of 1987, the YH group of companies was experiencing serious financial difficulties. Throughout the year, Castor had continued to accumulate unpaid interests on a monthly basis into account 046 and the balance in account 046 had to be reduced at year-end.

[956] Since YH could not meet Castor's demand at year-end 1987, Castor had no choice but to resort to circular transactions (cash circles) to clear account 046 and recognize interest revenue on YH loans. Castor delivered two checks payable to

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[984] PW-1060-1A, Tab 3
[985] PW-1056A, page 2
[986] PW-449
[987] PW-1061-1
[988] PW-1061-3
[989] PW-1060-1B
[990] PW-1053-27, seq. pp. 164-172.

McLean &Kerr in trust in the amounts of $3.3 and $5 million[991] and of these funds, $8.28 million were returned to Castor and recorded as payments of principal, interests and fees on loans[992].

[957] Castor did not record any specific LLP for the YH corporate loans in 1987.

Loan 1092 (during 1988)

[958] In January 1988, The Triumph Hotel Limited Partnership receivables were replaced with two mortgages (3rd and 4th positions) between The Triumph Hotel Limited Partnership and YHDL[993].

[959] At the maturity date, in December 1988, loan 1092 was extended for a year (to December 1989)[994]. YHDL provided an additional security – a pledge of its limited partnership interest in CHR Realty Equities Limited Partnership[995].

Loan 1123 (during 1988)

[960] By a commitment loan dated June 15, 1988, Castor agreed to provide a 35 million loan to KVWIL. The purpose of the loan was "*To bridge finance the Borrower's holdings of various subsidiaries and related companies*". The interest rate was prime plus 6%[996].

[961] The 35 million loan was to be secured by an unconditional guarantee of Wersebe for the full amount. However, by addendum, the guarantee was reduced to 12.5 million.

[962] This loan resulted from a reallocation of account 046[997].

[963] 20 million of this 35 million loan were reallocated to YHDL, in relation to the Hazelton Lanes loan 1091, and 20 million of personal guarantees of Wersebe were released.

Loan 1091 (Hazelton Lanes) during 1988

[964] In a letter to Castor, addressed to Ron Smith and dated May 6, 1988, McLean & Kerr had written about the Hazelton Lanes loan 1091 and its security[998]:

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[991] PW-1056A-1
[992] PW-1056A-6 and PW-1056A-7
[993] PW-1060-1B, Tab 2
[994] PW-1060-3A-1
[995] PW-1060-3A-5
[996] PW-1058-1
[997] PW-1056B
[998] PW-1059-2

- *Until the agreement dealing with the delivery of title deeds is terminated, York-Hannover Developments Ltd. and its related nominee companies do not have the ability to pledge any part of the Hazelton Lanes project to you to secure any financing;*

- *An unregistered pledge of the interest of York-Hannover Developments Ltd. or its nominee companies in either Hazelton Lanes site or development site will be subject to any intervening interests given by York-Hannover Developments Ltd. whether in compliance with the Co-Owner's Agreement and the financing documents or not which is registered prior to registration of the pledge to you. Notice and registration of the pledges to you will, of course, be an event of default with a likely result that the construction lender Confederation Life Insurance Company will require that the existing loans will be immediately repaid.*

[965] Castor held no security interest in any part of the property known as Hazelton Lanes, as confirmed in an acknowledgement signed by Stolzenberg on May 31, 1988[999].

CFAG loans (20 million) in 1988

[966] In C&L's AWPs, the five loans of CFAG to YH totalling 20 million appeared again[1000].

YH borrowers' insolvency - 1988

[967] The YH borrowers were insolvent[1001]. YH could only meet its obligations to Castor if Castor gave them the money[1002].

[968] YHDL and the other YH borrowers were incapable of meeting their own obligations, even in respect of their overhead expenses, and their survival became totally dependent upon Castor's continued support. The YH Hotels group looked to Castor as an owner or equity investor supplying the equity to keep the doors open, not as the lender whom it was supposed to be, or should have been[1003]. When YHHL needed funding, it did not approach Castor in the manner that it would have a normal lender:

> «Q- Okay. So when you are going to Castor to ask for money, you were basically trying to obtain moneys, be it short term or long term, to meet the needs that you were faced with.

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[999] PW-1059-4
[1000] PW-1053-91-9, p. BC-1, sequential page 257
[1001] R. Smith, May 14, 2008, p. 183; PW-1153; Prychidny, October 14, 2008, pp. 83-85; D-1312, ES-25, 154
[1002] R. Smith, May 14, 2008, p. 196.
[1003] Prychidny, October 14, 2008, p. 74.

A- Yes, I was approaching them not as a lender, I was approaching them as the owner's representative, depending on which property we're talking about. (...)

Q- So it's in that context that Mr. Von Wersebe told you, like a parent telling his child "Go see your mother or your father".

A- "Go see your uncle, I have no money"»[1004].

[969] YH borrowers did not and could not provide Castor with audited financial statements.

[970] C&L did not request to see audited or unaudited financial statements of YHDL, YHDHL, KVWIL or other YH entities or net worth statements of Wersebe. In fact, C&L did not consider financial statements a necessary tool to perform their audit work and did not consider the borrowers' capacity to pay[1005].

[971] YHDL's auditors refused to accept a personal guarantee of Wersebe as satisfactory evidence supporting the value of inter-company receivables for the purposes of the 1988 aborted audit[1006] and Whiting was surprised that the draft adverse opinion did not disclose even greater write-offs[1007].

YHDL – 1988 financial statements - adverse audit opinion

[972] A draft auditors' report expressing an adverse opinion on the 1988 financial statements of YHDL was prepared by Thorne Ernst & Whinney (YHDL's auditors)[1008], but it was never issued as Thorne Ernst & Whinney were dismissed as YHDL's auditors.

[973] The draft audit report proposed a going concern disclosure, provisions for reductions in value and a provision for future losses that together totalled $99.6 million, a deficiency in shareholders' equity of $70.7 million and an adverse audit opinion (*that the financial statements do not present fairly in accordance to GAAP*)[1009].

[1004] Prychidny, October 16, 2008, 100-101
[1005] Quintal, February 19, 1997, pp. 39-44; December 1, 1995, pp. 85-95; Belliveau, April 1, 1996, pp. 98-103; Quesnel, November 24, 1995, pp. 147-155; Wightman, September 27, 1995, pp. 36-38
[1006] Whiting, June 7, 2000, p. 17-21
[1007] PW-1148A; Whiting, March 28, 2000, pp. 76-77
[1008] PW-1148A
[1009] PW-1148A

Account 046 (1988)

[974] C&L 1988 AWPs included the following comment regarding account 046, similar to comments written in the previous years[1010]:

> "This account gets built up from interest accruing on YH loans and down by being reclassified to new mortgage loan"[1011].

[975] In 1988, account 046 had built up to approximately 30 million. By using journal entries, management reallocated approximately 29 million of account 046 to create a new loan to KVWIL (loan 1123). Later, other loans were readjusted and loan 1123 was reduced to 14.3 million while the Hazelton Lanes loan to YHDL (loan 1091) was increased to 29 million.

1988 Year-end "cash circle"

[976] Circular movement of funds occurred again in 1988.

[977] On December 22, 1988, CHL advanced $10,073,425 to its attorneys, McLean & Kerr, which it recorded as a loan to TWTCI (loan 1120). Those funds were used to pay various amounts owed to CHL, who received them from McLean & Kerr and recorded them in its cash receipt journal, on December 22, 1988, as follows[1012]:

Debtor	Nature	Amount	Relating to
223356 Alberta	interest & fees	$ 104,877	Southview
Serel	interest & fees	274,487	Serel
Skyline 80	interest and fees	995,586	Ottawa Skyline
YHDL	interest and principal	3,665,502	Corporate Loan
KVW Investments	principal	3,250,000	Corporate Loan
YHDL	interest, fees & A/C046	708,050	Accrued Interest
TOTAL		$8,998,502.	

[978] Castor did not record any specific allowances for LLP for any YH corporate loans in 1988.

[1010] PW-1053-83-5; PW-1053-35-6
[1011] PW-1053-23-20
[1012] PW-95, bates #000212 & #000213

Loans as of December 31, 1988

[979] At least 108.5 million of "YH Corporate loans", specifically reviewed by Plaintiff's experts, was owed to Castor as of December 31, 1988:

- Loan 1123 to KVWIL – 14.4 million[1013]
- Loan 1081 to YHDHL – 30 million[1014]
- Loan 1092 to YHDL – 10 million[1015]
- Loan 1091 to YHDL - 29 million[1016]
- Loan 1090 to YHDL – 3.3 million
- Account 046/Loan 1153 – 1.8 million
- CFAG loans to YH – 20 million[1017].

Interests recognized as revenue (1988)

[980] In 1988, $19,113,196.38 of interest was recognised on loans used for year-end reallocations of the YH group indebtedness.[1018]

Loans and commitment letters

[981] The commitment letters and loan agreements which C&L supposedly reviewed called for audited and unaudited financial statements of the borrowers to be provided to Castor[1019].

[982] The YH borrowers did not pay interests or fees to Castor on their loans as called for in the loan covenants. If it was not all the interest due to Castor that was capitalized or funded by Castor, it was certainly close to 100%[1020].

[1013] PW-1053-23-2, sequential pages 248-250 and 272; PW-1058-1
[1014] PW-1053-23-1, sequential pages 211-212; PW-1054-3 and PW-1054-10
[1015] PW-1053-23-4, sequential pages 209-210-279; PW-1060-1 and PW-1060-3
[1016] PW-1059-6 and PW-1053-23-3, sequential pages 180-182 and 270
[1017] PW-1053-91-9, p. BC-1, sequential page 257
[1018] PW-1056F Namely, on the YH Corporate loans discussed in the present section, the following amounts : for loan 1123, $3,006.156.71 ; for loan 1081 - $5,292,584.77; for loan 1092 - $1,327,534.27; for loan 1091 - $1 ,278,787.67; for loan 1090 -$553,902.75
[1019] For example, PW-1058-1, PW-1063-1, PW-1054-3-1, PW-1059-6
[1020] R. Smith, May 14, 2008, pp. 138-139

Books and records

[983] The books of original entry disclosed that the interest and fees on the YH corporate loans were not being paid in cash, but were being systematically capitalized[1021].

[984] The General Journal disclosed that interest on a series of loans to YHDL was being capitalized each month to account 046[1022]. It also disclosed that interest on the YHDL portion of the Meadowlark loan was being similarly capitalized until 1990 and that YHDL's guarantee of the MLV debenture holders' obligations to CHIF was being satisfied in a similar fashion through the inter-company Zug/Enar account (JE#12)[1023].

[985] The cash receipts journals disclosed that virtually no interest was being collected in cash on a monthly basis notwithstanding the loan covenants that called for monthly payments of interests. The General Journal disclosed, in December of each year, the year-end reallocations from account 046 to existing or new YH loans[1024].

[986] In 1988, CFAG's accounting ledger did not specify the names of the borrowers of what were then five loans totalling 20 million although the working papers[1025] showed that the loans were due by "York-Hannover".

Wersebe's guarantees

[987] At December 31, 1988, Wersebe had given the following guarantees relating to YH Corporate loans:

- 15 million relating to YHDHL loan 1081[1026]
- 12.5 million relating to KVWIL loan 1123[1027]

[988] The draft auditor's report of the 1988 YHDL financial statements indicates a shareholder's deficiency of $70.7 million[1028].

[989] Castor's ability to realize on Wersebe's guarantee was limited[1029]. In a letter dated February 9, 1989 Whiting wrote to Stolzenberg that "*the express agreement between the parties was that Mr. von Wersebe's European holdings not be brought in under the share pledge provisions of the guarantee*"[1030]. Through a document entitled

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[1021] PW-2908, Vol. 1, p. 5-12; PW-1485R; Vance, March 6, 2008, pp. 147-155.
[1022] PW-87.
[1023] PW-100, pp. 41, 47.
[1024] PW-84, bates p. 000573
[1025] PW-1053-91-9, p. BC-1
[1026] PW-1054-3 and PW-1054-10
[1027] PW-1058-1
[1028] PW-1148A
[1029] Whiting, November 16, 1999, pp.118 and following
[1030] PW-1058-2

"acknowledgment", Stolzenberg agreed that Wersebe's European holdings were not included in the share pledge provisions of the guarantees given relating to loans 1081 and 1123[1031].

[990] C&L did not review information on the net worth of Wersebe or on the legal enforceability of his personal guarantees.

Other information

[991] Mackay testified that he understood that Castor could not consider taking a loan loss provision on one YH loan because a provision would then have to be taken on all of them[1032]. Smith said he was not permitted to take loan loss provisions on any YH loans[1033].

[992] Prychidny testified that YH European entities made it clear they were not prepared or able to support loans made by Castor to the YH North American group;[1034] they were rather hoping for those entities to provide them with the financial support they needed[1035].

[993] Interest owing on the YH corporate loans was recognized through the vehicle of capitalization of interests or year-end circles of funds[1036].

[994] YH never produced consolidated financial statements.

Experts' evidence

[995] The minimum LLP required according to Plaintiff's experts was:

Expert	Minimum LLP
Vance	77.7 million[1037]
Froese	60.4 million [1038]
Rosen	79 to 91million[1039]

[1031] PW-1058-4
[1032] Mackay, August 24, 2009, pp. 173-175.
[1033] R. Smith, May 14, 2008, pp. 124-126.
[1034] Prychidny, October 14, 2008, pp. 50-51.
[1035] Prychidny, October 14, 2008, pp. 50-52
[1036] PW-1056F
[1037] PW-2908, Vol. 1, S-8
[1038] Froese, January 27, 2009, pp.95 and following and PW-2941-4, schedules 3 and 4;
[1039] PW-3033, Vol. 2, Appendix C, p. 3, Approach A (unadjusted).

[996] In his analysis of the YH Corporate loans for 1988, Froese did not include loan 1091 related to Hazelton (in the sum of 29 million). Rosen, on the other hand, included 17.7 million of CHIF loans, which were not addressed by the other experts. When adjusted for purposes of comparison, taking account of those differences, the estimates of Plaintiff's experts all fall within a reasonable and consistent range.

[997] Plaintiff's experts also opined that all of such loans should have been placed on a non-accrual basis, since there was no reasonable assurance of collectability. The revenue on the YH corporate loans that should have been reversed to comply with GAAP amounted to $14.7 million according to Vance[1040]. Experts added that had such revenue been reversed as required under GAAP, the loan loss provisions referred to above would have been reduced accordingly (to avoid double counting).

Vance

[998] Vance calculated that Castor's exposure to YH Corporate loans in 1988 was 103.4 million[1041] and he described the methodology he had followed to assess the required LLP at 77.7 million[1042].

[999] Vance included the Hazelton Lanes loan in his YH Corporate loans because Castor could not register its security against the project; he did consider that Castor could recover some amount from this project and he accounted for that recovery[1043].

[1000] Vance looked at Wersebe's personal guarantees and concluded they had no value[1044].

- In examination in chief, he explained his conclusion as follows:

  With respect to the working papers and the personal guarantee of Karsten Von Wersebe, I'm aware that a personal balance sheet has been filed at D-848[1045] and that included Canadian assets, primarily Canadian assets and European assets. The Canadian assets were basically the York-Hannover Developments Ltd. group and York-Hannover Developments being the prime operating company, and as we've just seen in my calculations with respect to York-Hannover Developments Ltd., well firstly, it was subject in nineteen eighty-eight (1988) to an adverse opinion, a draft adverse opinion by the auditors who never them complete it, but that adverse opinion had indicated that there was approximately one hundred (100) million of write-offs or additional expenses that should be taken, so that would in effect in my view eliminate any value to York-

[1040] PW-2908, Vol. 1, S-8, S-9 and S-10. The revenue reversals calculated by Dr. Rosen were of a similar magnitude, see PW-3033, Vol. 2, pp. 6-7. See PW-2941, Vol. 4, pp. 26, 82; See also PW-1056F
[1041] Vance, April 14, 2008, p.18
[1042] Vance, April 14, 2008, pp.68 to 141
[1043] Vance, April 14. 2008. p. 23 and 141-142
[1044] Vance, April 14, 2008, pp.142
[1045] The objection to the production of this exhibit (OSR # 126) has been maintained by judgment of this day

> Hannover Developments Ltd., and also, in my own calculations, there was no value to the equity in that company. It could only make a partial payment to its unsecured creditors.
>
> And with respect to the European assets, PW-1058-4 is an acknowledgement that is signed by Castor, by Mr. Stolzenberg, it's dated nineteen eighty-nine (1989), but it indicates that the European, in effect the European assets of Mr. Von Wersebe would not be available to honour the guarantee.
>
> And lastly, the auditors had not carried out any work with respect to that guarantee and didn't undertake to try and give it value, although when I did look at it, in my opinion, the other thing that has to be borne in mind, you're dealing with a sophisticated businessman, who's knowledgeable of secrecy jurisdictions and a creditor proofing, and before you would accept the personal balance sheet, you would want to make sure that you... there was a way you could get your hands on that collateral, it wouldn't be sheltered in some way, shape or form.
>
> And lastly, Coopers did not do anything with respect to that guarantee at all[1046].

- In cross-examination, he added:

> But I think the comment I'm trying to make is he was an individual, certainly of foreign extraction, well-versed in the use of foreign jurisdictions and secrecy jurisdictions and creditor proofing, and if you have another... And the point further down, if the amount of assets in other foreign jurisdictions are material, I think that's regardless of whether it's a Canadian resident or foreign resident, you would have to be able to seek a legal opinion as to the ability to enforce the guarantee over those assets[1047].

[1001] Vance acknowledged that he had not conducted an investigation of Wersebe, whether he owned European companies that owned assets in North America or whether he was carrying on business in North America other than that which concerned the North American YH group of companies. According to Vance, Wersebe's Canadian assets had all been used for the reorganization of KVWIL, and Wersebe conducted his Canadian or North American operations through YH or KVWIL, and his European operations through KVW Holding AG in Zurich, and those operations were kept apart[1048].

[1046] Vance, April 14, 2008, pp.142-144
[1047] Vance, July 7, 2008, pp.208-209
[1048] Vance, July 7. 2008, pp.281-221

Froese

[1002] The following financial statements have been used by Froese in his YH Corporate loans section:

- for KVWIL : PW-1136-4 (1987), PW-1136-5C (1988), PW-1138-1 (1989) and PW-1136-5A (1990)
- for YHHHL : PW-1140 (1986)
- for YHLP : PW-1139 (1988 including comparative for 1987)
- for YHDHL : PW-1138-2 (1990)
- for YHDL: PW-1148 (1988), PW-1148a (1988) and PW-1149 (1989)

[1003] Froese prepared a schedule of combined *pro forma* balance sheets of the holding companies of YH (KVWIL and YHDHL) and an overview of their situation, as of December 31, 1988[1049]. He included also YHLP's assets. The result showed a deficit of 124.9 million[1050]. Even if some adjustments had to be made (due to surpluses from projects like MEC, for example), Froese opined that a huge part of said deficit would never be eliminated[1051]. In such a situation, Froese concluded that KVWIL and YHDHL could not reimburse all of their debts, and that LLPs were needed on loans 1123 and 1081($44.4 million)[1052].

[1004] Froese looked at YHDL's capacity to reimburse loans 1090, 1092, account046/loan 1153 and the CFAG loans and concluded that YHDL was not able to do so. Froese mentioned that, even if 1987 and 1988 had been very good years for real estate, YHDL was barely making enough money to cover its interests[1053]. The difficulties, identified in the draft adverse audit opinion, were very serious[1054]. Froese concluded that YHDL's shares had no value throughout the 1988-1990 periods[1055].

[1005] Froese added that placing the loans on a non-accrual basis together with the magnitude of the increase in LLPs created uncertainty as to Castor's ability to continue as a going concern.

[1049] PW-2945; Froese, November 26, 2008, pp. 143 and following
[1050] PW-2945
[1051] Froese, November 26, 2008, pp. 155-156; see also Froese, January 8, 2009, pp.209 – 222 and Froese, January 9, 2009, pp.31-59
[1052] Froese, November 26, 2008, pp. 157-158
[1053] Froese, November 26, 2008, pp.163
[1054] PW-1148A
[1055] Froese, November 28, 2008, pp.65-66

[1006] Froese opined that Wersebe's personal guarantee had no value in 1988.[1056] In his cross-examination, Froese emphasized the fact that Wersebe had never pitched in even though YH had very serious financial difficulties, and he concluded that it was a significant indicia[1057]. Froese also explained:

> A- (...) over the eighty-eight ('88) to ninety ('90) period, whenever additional cash was required for one of the York-Hannover groups, or not whenever but many of the times, Castor funded it. So even back in nineteen eighty-seven (1987), when the first payment is due on York-Hannover Development Holdings Limited loan to Castor, the comment comes back, York- Hannover can't pay it, Castor has to fund the payment.
>
> And throughout the eighty-eight ('88) to ninety ('90) period, there was no demonstrated ability of York- Hannover to pay its liabilities as they came due, and normal prudent lenders look to the owners to contribute funds in those times, so if you do have a valid personal guarantee, you've got an ability to force an injection of capital, normally you would use that as a lender, and over that period, it didn't appear that Castor was able to access any of Mr. Von Wersebe's personal assets in that period. So I've also considered that in my opinion of the value.
>
> Q- Was able to access or decided not to access those personal assets?
>
> A- Either one would be similar, because when you look at the... I mean, if both the ability to enforce it and the motivation to enforce it, so you need both[1058].

Rosen

[1007] Rosen described the relationship between Wersebe and Stolzenberg and opined that Wersebe had a significant influence on Castor.

> if we go to PW-1054, tab 7, and you look at some of that correspondence, and it's around the time of selling the shares, so he makes a statement something along the lines that "the only way I can pay you is if you give me a loan".
>
> So in that type of arrangement, what else you're going to say other than, if Castor does not keep York -Hannover alive through giving more money and the whole thing goes down, then Castor is going to have to report losses on its financial statements and that's going to end Castor as a... in my opinion, anyway, as a vehicle to use the financial statements to attract money and, therefore, it won't survive.
>
> So you can call it a stranglehold if you want, but I just can't, from that type of comment, and then we can go through other arrangements where the transactions are going back and forth, the nine (9) loans at the end of nineteen

[1056] Froese, December 5, 2008, pp.14 -18; Froese, January 12, 2009, pp. 47-50
[1057] Froese, January 12, 2009, p.71
[1058] Froese, January 12, 2009, p.39

> ninety (1990), that's another consideration, just steps that were taken to curtail Mr. Von Wersebe's spending of Castor money, so certain reorganizations that took place.
>
> I think the evidence piles up to me to say that the influence was very high and the cost to Castor of not bending to what Mr. Von Wersebe wanted was just too drastic to consider[1059].

[1008] Rosen explained why, in his opinion, Wersebe had such influence on Castor while Castor had not that much influence of YH. Moreover, he enunciated that Wersebe's influence negatively impacted Castor's ability to continue to operate as a going concern.

> So that Mr. Von Wersebe, I think was very clever or sneaky, dependent on your point of view, of being able to get Mr. Stolzenberg in a position where he had no choice, and when you have no choice, that, to me, is a very significant influence and forcing the decisions to come your way, the York-Hannover and KVW way. So it's... the relationship was, as I mentioned a few minutes ago, virtually a stranglehold in the situation and Mr. Von Wersebe had considerable power as a result.
>
> Q- And so did Castor over York-Hannover, correct, equally?
>
> A- Well, I don't think it had that much in that sense because KVW as a company, sort of the top company itself and all the other parts of that relationship were just in very serious financial conditions. So Castor I don't think had much power, the assets could not, in my opinion, have been sold for very much and, on that basis, it would have been the end of Castor to have called any loans[1060].

[1009] Rosen gave no value to Wersebe's personal guarantee. In his cross-examination and in no uncertain terms, he disagreed that some evidence showed "*fairly extensive or significant net worth of Wersebe*":

> A-If you want to look at the net worth statements and go through them in detail, somebody who's giving some high value, for example the York-Hannover Developments Limited, when the evidence is showing that they're just mass of financial problems in there, you have to look at the net worth statement and say, "This is ridiculous".
>
> Q- All right. So this was not... the value of the personal guarantees is not included in items where you were prepared to give the benefit of the doubt; correct?

[1059] Rosen, April 6, 2009, pp.54-55
[1060] Rosen, April 6, 2009, pp.57-58

A- Well, this would not be given in the benefit of the doubt. That would have to be a massive Santa Claus to...[1061]

Goodman

[1010] Goodman is the only expert who opined that no LLPs were required on the YH Corporate loans: he concluded accordingly opining that Castor was entitled to consider in its aggregation of YH group of loans various surpluses within the group (including MEC) and the guarantees of Wersebe.

[1011] Goodman opined that from 1988-1990, the 20 million loans owing to CFAG were actually owed by Investamar. He concluded that Investamar had acted as a borrower (from CFAG) and as a lender (to YH), as there was no indication in the 1982 agreement[1062] that Investamar was acting merely as an agency.

[1012] Goodman concluded that Investamar was not just a conduit, but an entity acting as a principal in this 20 million loan transaction. Therefore, it was necessary under GAAP to evaluate its financial strength before any LLP be taken. In the absence of information relating thereto, Goodman opined that the loans had to be carried at cost.

Conclusions

[1013] Plaintiff's experts position on the CFAG loans must prevail:

- 20 million were owed by YH to CFAG notwithstanding the agreement signed in 1982 with Investamar[1063] and the confirmations relating to those loans written on Investamar letterhead. Investamar only acted as "a conduit", as evidenced by the handwritten notes in the AWPs of C&L of 1984 and 1985 and the various inscriptions to account 046.

- The confirmation letters onto which the handwritten notations were made in 1984 and in 1985 indicated they had to be returned to the lender's auditors[1064].

- C&L were not Investamar's auditors but CFAG's auditors.

- In its AWPs, C&L described those loans as loans of CFAG owed by YH, never as loans owed by Investamar.

[1014] Castor and YH did not behave as one would expect them to, had their relationship been an arm's length commercial lending one. In fact, Castor and YH were "*equity partners*" developing, operating or managing various properties. Because YHDL

[1061] Rosen, April 8, 2009, p. 34
[1062] PW-1178
[1063] PW-1178
[1064] PW-1053-99, sequential pages 260 to 264

and its related entities became hopelessly insolvent, Castor could not and did not enforce its securities - such a course of action would have led to the collapse of Castor and the crystallization of hundreds of millions of dollars of losses[1065].

[1015] Various agreements and side deals between Castor and Wersebe limited Castor's ability to realize on Wersebe's personal guarantee.

[1016] One of the cornerstones of Goodman's opinion that the YH Group loans were not misstated in accordance with GAAP is that even though there were significant deficiencies on various loans that he reviewed, it was not necessary to take any loan loss provision in respect of such deficiencies because there existed alleged "surplus positions" in other YH loans. Goodman namely overcame deficiencies in connection with the CSH loans (of $11.9 million, $20.2 million and $23.4 million) by resorting to this theory[1066]. For instance, he suggested that surpluses he calculated in relation to the MEC property be taken into account.

[1017] Goodman testified as follows:

> My analysis, as I just pointed out, was that there were surpluses, or loan security surpluses, in each of the years nineteen eighty-eight (1988), nineteen eighty-nine (1989) and nineteen ninety (1990) in respect of Castor's loans, and that those surpluses were important in the overall consideration of the overall York-Hannover position vis à vis Castor[1067].
>
> any GAAP assessment of the overall York- Hannover group, My Lady, required an analysis of at least all of the major loan positions within that grouping and certainly TWTC was a... was a major... TWTC loans were very significant.[1068]

[1018] Vance testified that Goodman's theory regarding offset did not constitute GAAP and that «*no auditor should accept such approach absent of valid, legal cross-collateralization agreement supported by valid security*».[1069]

[1019] To the same effect, Froese testified as follows:

> you do have to consider all the loans to see if you've missed any loans that require an allowance, but unless you have participation agreements that give you... give you the ability to receive more back than the amount of the loan, you don't have to consider all of the loans to determine whether or not you need an allowance on certain loans, you only need to consider all of the loans if you can get paid back more than the amount of the loans on some of the loans and I understand that these loans didn't have participation agreements and there wasn't the ability to get paid back more than the amount of the loan.(...)

[1065] R. Smith, May 14, 2008, pp. 139-140, 206-207
[1066] D-1312, pp. 429-430.
[1067] Goodman, September 23, 2009, p.177
[1068] Goodman, September 24, 2009, p.43
[1069] Vance, April 12, 2010, p. 242.

> All I was commenting on is you're not going to get to a lower number, but considering more loans, you'd get to a higher number for an allowance, unless you have loans that have participations or some way of getting paid back more than the face amount of the loan. (...)
>
> the surplus would be a situation where you could get paid back more than the amount of the loan. (...)[1070]

[1020] The Court shares Vance's and Froese's point of view.

[1021] Goodman acknowledged that he agreed with Vance *"that the York-Hannover Group of companies were insolvent during the 1988 to 1990 period"*.[1071]

[1022] Castor's very own practices, with respect to the loans to the YH Group, did not contemplate the possibility of an offset in situations where security had not been granted or new loans had not been issued by Castor.

[1023] Whenever Castor wished to clear account 046, or other outstanding indebtedness existing at year-end in respect of the YH loans, it negotiated with YH to grant loans and to obtain security. In each case, where new security was granted, the loan agreements clearly stipulated such security.

[1024] When Castor specifically intended to allow for offset as secondary security, it stipulated such right in the loan agreement[1072].

[1025] When Castor acknowledged deficiencies on various YH loans, such as in the case of Airport Corporate Center ("**ACC**")[1073], Meadowlark[1074] and MLV[1075], it recorded loan loss provisions and did not purport to apply alleged security surpluses on other loans in Castor's portfolio.

[1026] Castor looked at the projects (or properties) as separate groupings. For example, in the case of the TSH and the CSH, separate grid notes were set up to capitalize unpaid interest, fees and expenses that accumulated in connection with such projects[1076].

[1070] Froese, January 9, 2009, pp.58-59
[1071] D-1312, p. 363.
[1072] PW-3089.
[1073] Ron Smith, March 27, 2009, pp.62-63
[1074] In 1989- a LLP of $576,436 was taken on Loan 1117 to Leeds; In 1990 – a LLP of $ 2 million was taken on Loan 1030 to Leeds
[1075] A LLP of 5 million was taken in 1990
[1076] See namely – for TSH: Account 066 and Loan 1148 (PW-167D); Ron Smith, June 11, 2008 ; Ron Smith, September 3, 2008; for CSH : PW-1086 A, PW-1086 B, PW-1086C, PW-1087, tab 6; Ron Smith, September 3, 2008; Ron Smith, September 5, 2008; Account 066 and loan 1147

[1027] Castor knew how to enter into agreements with its borrowers that provided it with the right to participate in any potential "surplus" on a project.[1077]

[1028] In its internal document AM-50, C&L acknowledged that the lower of cost and net realizable value test should be applied on a "parcel-by-parcel" basis, unless parcels were interrelated. C&L valued the loans and purported to determine whether LLPs were required during its audits of Castor accordingly, namely those of 1988, 1989 and 1990.

[1029] On one hand, when C&L considered that the loan documentation provided for a right of offset, the auditor specifically documented such right. For example, in the audit working papers of CHIF for 1986, Wightman indicated that there was a right of offset in respect of certain specific loans. [1078] As an example, he referred to a loan by CHIF to First Holdings where he considered that a right of offset existed. C&L presumably relied on the security agreement with such borrower which provided for a pledge of listed assets.[1079]

[1030] On the other hand, C&L never considered, nor did Castor ever advise C&L, that any right of offset existed between, for example, deficiencies in respect of the Skyline Hotels and an alleged security surplus on MEC or deficiencies in respect of KVWIL and YHDHL and the "value" of shares and debentures of Castor held by Raulino.

[1031] Furthermore, although loan loss provisions were recorded during the relevant years, C&L never once purported to apply such alleged surpluses to situations where loans were provided for or written off.

[1032] At trial, on February 9 and 10, 2010, Wightman testified he generally felt that surpluses from other projects were available for other loans,[1080] and that he understood that capitalized interest was being reallocated onto projects with the most security.[1081] However, fifteen years earlier (on discovery in October 1995) while the facts should have been fresh in his memory, he was completely unaware of the details of the process of interest reallocation,[1082] and never mentioned the availability of surpluses on other projects.

[1033] Not one of the C&L audit staff members who testified asserted that he or she believed that alleged security surpluses on one project could be used to offset a deficiency against another project where no cross-collateral guarantee existed.

[1034] In addition to all of the outstanding indebtedness due to Castor, which would be in default and on which interest could no longer be recognized, had Castor

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[1077] For example, see PW-1102A-4 and Ron Smith, September 15, 2008, p. 131.
[1078] PW-1053-3, seq. pp. 473-478.
[1079] D-579
[1080] Wightman, February 10, 2010, pp. 53-55
[1081] Wightman, February 9, 2010, pp. 116-117
[1082] Wightman, October 18, 1995, pp. 47-50.

contemplated a "*dation en paiement*" of the MEC project in any of the relevant years, (1988, 1989 or 1990) Castor would have had:

- to reimburse the first mortgage lenders;
- to fund the costs to complete the construction; and
- to provide new security to its lenders to whom the $50 million second mortgage bonds had been assigned.

[1035] Castor neither had the means nor the intent or the capacity to act accordingly. As Ron Smith said, such a course of action would have caused the immediate demise of YHDL and of Castor.[1083]

[1036] Goodman acknowledged that when an accountant matches one exposure against another, it must be «*based on the facts, it can't just be some invention of facts*».[1084]

[1037] Goodman's theory presupposes that, even in the unlikely event that one of Castor's borrowers would repay its loan to Castor, any potential surpluses associated with the property would still somehow accrue to Castor rather than to the borrower. The Court does not accept such a suggestion.

[1038] The only liability that each borrower of Castor had was to repay its loan. Once that obligation was fulfilled, absent a specific agreement, Castor had no right to share in any potential upside associated with the property.

[1039] Goodman, who purports to rely on "lender's intent", ignores the fact that when Castor and YH "intended" that Castor could participate in any surpluses, they entered into a contract to that effect.

[1040] In all of the situations relied upon by Goodman to apply alleged potential surpluses to other deficiencies, no such contracts existed.

[1041] Finally, Goodman's theory of surpluses relies totally on Goodman's understanding and assessment of Castor's bargaining position or alleged capacity to apply pressure or alleged capacity to enforce a recovery scenario –such as the scenario of "*dation en paiement*" in the case of the MEC project. The Court does not share Goodman's understanding and assessment, which are not in line with the evidence.

[1042] Therefore, huge LLPs, as opined by Plaintiff's experts, where required in relation to the YH Corporate loans in 1988.

[1083] Ron Smith, May 14, 2008, pp.206-207
[1084] Goodman, October 26, 2009, p. 52

MEC

Additional evidence specific to MEC

Loans as of December 31, 1988

[1043] At December 31, 1988, $83 million of loans made in connection to MEC were owed to Castor[1085]:

- Loan 1100 - $ 46,109,129[1086] - loan to YHDL/97872 as joint owners of MEC dated February 19, 1988, secured by second mortgage bond[1087] ;
- Loan 1109 - $ 4,000,000[1088] - standby loan (credit reserve) made to YHDL/97872 as joint owners of MEC, dated February 19, 1988, secured by third mortgage[1089];
- Loans 1101/1103 - $ 3,848,106[1090] - standby loans (fee and interest reserve) to YHDL/97872 as joint owners of MEC, dated February 19, 1988, secured by third mortgage[1091];
- Loan 1042 - $ 14,000,000[1092] - loan to YHDL, as one of the joint owners of MEC, with an unregistered collateral mortgage on YHDL's interest in the project [1093];
- Loan 1095 - $ 7,500,000[1094] - loan to 612044, the parent company of 97872, secured by a pledge of all of the shares of 97872 (preferred and common);
- Loan 066/1146 – $0,8 million- loan to Palace II;[1095]
- Loan 701000/2001 - $ 7,550,000 - loan to Palace II secured by first mortgage on the Palace Theater.[1096]

[1044] There was also Loan 1158 made to the MEC Tenants Association, not related to YHDL, but secured by YHDL and 97872 guarantees.

[1085] Vance - PW-2908,volume 2, chapter C, p.C-7 (figures taken from C&L's working papers); Goodman - D-1312, p.143
[1086] PW-1053-23, E151
[1087] PW-1102A-3 and PW-1102A-7
[1088] PW-1053-23 , E153
[1089] PW-1102A-4
[1090] PW-1053-23 , E155
[1091] PW-1102-4
[1092] PW-1053-23, E126
[1093] PW-1063-4; PW-1063-5A
[1094] PW-1053-23, E128
[1095] PW-1110A
[1096] PW-283; PW-1110A and PW-1110D

Interests recognized as revenue

[1045] In 1988, Castor recognized interests totalling $8,501,253.02 as revenue on the MEC related loans[1097].

Loan documents and commitment letters

[1046] The commitment letter of the second mortgage financing (loan 1100) specifically provided that 97872 and YHDL were each required to provide audited annual financial statements as well as various other financial information regarding the project[1098]. The disbursement of such loan was conditional upon obtaining legal opinions as to the validity of the security[1099]. Other commitment letters relating to MEC's financing by CHL included similar covenants.

[1047] In respect of the equity loan to YHDL, loan 1042, the commitment letters and other legal documents called for annual financial statements of YHDL to be provided to CHL within 120 days of YHDL's fiscal year end, and for various financial information on the Property (MEC), when requested by Castor (with inspection rights)[1100].

[1048] Legal documents relating to CHIF's loan of $7,550 million secured by first mortgage loan to Palace II Development Inc. provided that Palace II Development Inc. had to pay the interests monthly[1101]. Palace II Development Inc. also had to provide to CHIF annually, within 120 days of the end of its fiscal year, its audited year-end financial statements prepared in accordance with Canadian GAAP, and various other financial information (with inspection rights)[1102]. YHDL and 612044 intervened in the deed. They were bound together and severally obliged to one another along with Palace II Development Inc. in favour of CHIF for the fulfillment of all the obligations of Palace II Development Inc.[1103]

Budget, completion date and status reports

[1049] As of February 19, 1988, the closing date of the financing, the estimated cost of completion of the project was $195 million and the completion date was to be no later than January 31, 1990[1104].

[1050] Borrowers had to provide reports from the project monitor with each draw request[1105].

[1097] PW-1105
[1098] PW-1102A-3, pp.8-9
[1099] PW-1102A-3, p.8
[1100] PW-1063
[1101] PW-285, PW-283B article 2(a) and PW-1110D
[1102] PW-283B (see namely paragraph 31.10)
[1103] PW-283B, pages 35-37
[1104] PW-1102A-4.
[1105] PW-1102A-4, pp.6-7

Events taking place during 1988

[1051] In January 1988, alleging that it had not received the comfort that they wanted from the due diligence investigation into the financial affairs of YHDL[1106], because YHDL was too highly leveraged, the Bank of Montreal ("**BMO**") required at least 10 million of additional equity up front to reduce its proposed first mortgage position of 135 million to 125 million. The difference of 10 million was assumed by Castor.

[1052] The refinancing closing took place on February 19, 1988[1107].

[1053] Shortly after the refinancing, in the fall of 1988, BMO issued a series of certificates notifying Castor of defaults under the first mortgage loan agreement. In each case, Castor was compelled to cure the default and make the payments that the owners failed to make[1108].

[1054] On December 8, 1988, BMO wrote that the physical completion of the MEC would not be achieved by January 31, 1990, thereby giving rise to an event of default, and that the banks were actually in the process of assessing their position[1109]. Substantial negotiations ensued and the issue was resolved, as long as the equity funds were put in place.

[1055] Because YHDL did not have other resources to remedy the deficiencies and to meet other requirements of the project, Castor always funded them on its behalf. YHDL was a fifty percent (50%) owner of the MEC project.

[1056] At the end of 1988, there were no outstanding loans made directly to 97872 owed to Castor[1110].

[1057] Castor's borrowers failed to meet their debt service obligations to Castor and to provide financial statements as called for in the loan agreements[1111].

MEC appraisals

[1058] Royal LePage carried an appraisal and submitted an appraisal report dated August 5, 1988[1112] - they described their work and mandate and expressed their final opinion as follows:

- *We have carried out an appraisal and valuation analysis of the above-mentioned property and submit our findings.*

[1106] PW-1102-A-2A
[1107] See the series of exhibits PW-1102
[1108] As examples, see PW-1104-1 and PW-1104-2; Ron Smith, September 15, 2008, pp.153 and following
[1109] PW-1104-3; Ron Smith, September 15, 2008, pp.158 and following
[1110] PW-1101A; Ron Smith, September 15, 2008, p.160, 162
[1111] PW-1054-3-1, p. 6.
[1112] PW-1108

- *The purpose of this appraisal is to estimate the current market value of the subject property assuming it is fully occupied and completed in accordance with the plans and specifications provided to us.*

- *As a result of our investigations and analysis carried out, it is our opinion that the current market value of Phase 1, when completed at May 1st, 1989, is as follows: ONE HUNDRED THIRTY EIGHT MILLION DOLLARS ($138,000,000.) within a probable price selling range of between $133,000,000 and $143,000,000.*

- *The market value of both Phases 1 and 2 when completed, as at May 1st, 1990, is as follows: TWO HUNDRED AND SIXTY ONE MILLION DOLLARS ($261,000,000.) within a probable price selling range of between $252,000,000 and $270,000,000.*

[1059] The figure that C&L relied upon – which is 275 million – comes from a Royal LePage report, also of August 5, 1988,[1113] in which Royal LePage namely wrote:

- *Further to your request, this is to provide you with a preliminary estimate of the market value of the proposed Montreal Eaton Centre assuming a proposed office building of approximately 400,000 sq.ft. is constructed above.*

- *The value estimates contained in this letter are preliminary in nature and are based upon assumptions which have not been substantiated by retail market studies in the downtown Montreal area.*

- *It is our understanding that the office component will be built over the Montreal Eaton Center retail complex and have direct internal linkages.*

- *We have recognized the favourable impact to the Montreal Eaton Centre retail component by the office building as an increase in gross sales for the retail tenants. In turn, the increase in retail sales will result in a greater amount of percentage rents being achieved and a correspondingly higher value.*

[1060] Royal LePage stated that their value range upon completion was between 266 million and 285 million, assuming that completion of an office tower would add more potential shoppers[1114].

[1061] As of December 31, 1988, the assumption on which Royal LePage's additional report was based (scheme C - construction of an office building of approximately 400,000 sq.ft.) was held in abeyance[1115].

[1113] PW-1108A; Ron Smith, September 15, 2008, pp. 207 and following; Ron Smith, September 22, 2008, p.79

[1114] PW-1108

[1115] D-99D; Vance, April 10, 2008, pp. 84-88; Vance, July 7, 2008, pp.234 and following; Ron Smith, September, 24, 2008. pp. 9 and following

Other information

[1062] Between 1987 and 1990, loan 1042 served for YH year-end reallocation[1116] as follows:

- As part of its 1987 YH year-end reallocation, Castor added 2 million to loan 1042[1117].
- Nothing [1118]was added to loan 1042 as part of the 1988 YH year-end reallocation[1119].
- As part of its 1989 YH year-end reallocation, Castor added 10 million to loan 1042[1120].
- As part of its 1990 YH year-end reallocation, Castor added 5 million to loan 1042[1121].

[1063] Ron Smith testified that those reallocations to loan 1042 were done without specific credit analysis:

> There was no credit analysis. York-Hannover maintained that they had fifty percent (50%) equity in the project and that the project was going to be worth, you know, in excess of three hundred (300) million dollars and therefore, they requested that we book it against directly.

[1064] The mortgage and loan ledger cards in Montreal clearly revealed that all interests and fees on the CHIF loan for Palace II Theater were being capitalized to a grid note in Montreal[1122].

Experts' evidence

[1065] Vance and Goodman took account of the MEC and the Palace II Theater loans under their proposed "MEC calculations" based on the market value at the date of projected completion, less estimated remaining costs to complete.

[1066] In all material respects, Vance and Goodman agree on the principal amount of loans and accrued interests owing to Castor in respect of the MEC project.

[1116] Ron Smith, September 15, 2008, pp.171-173
[1117] PW-1056A
[1118] Ron Smith, September 15, 2008, p.173
[1119] PW-1056B
[1120] PW-1056C
[1121] PW-1056D
[1122] PW-167, vol.2: PW-283A-2

[1067] For 1988, Vance opined that there was a deficit of 11.1 million[1123] whereas Goodman opined that there was a surplus of 73.4 million[1124]. The following elements make up for the difference of 84.5 million:

Description	Amount - Difference
Market value at completion (MEC)	32 million
Castor's future interests as costs to complete	20.7 million
Projected operating income	13.1 million
Market value (and indebtedness) – Palace II Theater	8.1 million
Debt to others	6.8 million
Contributions receivable from third parties	2.4 million
Project payables	1.4 million
TOTAL	**84.5 million**

[1068] Vance used a value figure of 261 million, the suggested value in the Royal LePage appraisal PW-1108 dated August 5, 1988[1125]. Goodman used a value figure of 293 million that he derived from the following value indicators: 275 million, as per Royal LePage's report PW-1108A that took account of additional value to be created by the office building to be erected, and 18 million attributed to the office pad component itself[1126]. Goodman opined that since the costs to complete the office pad were included in the 108,076 million figure of costs to complete, value of the office pad had to be accounted for[1127].

[1069] In Vance's calculations, the costs to complete are of 108,076 million. Goodman started with the same figure,[1128] but he subtracted the future interests to be paid to Castor (20.7 million). Goodman opined that "*inclusion of future income was not prevailing GAAP practice at the time in lending institutions*" and that it was "*not Castor's*

[1123] Vance, PW-2908, volume 3, pp. 37-39
[1124] Goodman, D-1312, pp.142-143 (MEC.11)
[1125] PW-1108
[1126] D-1312, p.157 – as per the offer made D-943
[1127] Goodman, September 23, 2009, p.131
[1128] D-1312, p.134 (MEC.6)

established practice at the time and it represents, recording of future losses that have not been incurred"[1129].

[1070] Goodman opined that it was necessary to take account of the contributions of others that would serve to pay some of the costs to complete, since those costs were deducted from value[1130]. Goodman also opined that the operating income (13.1 million) had to be deducted because it would reduce Castor's funding toward the costs to complete[1131]. Vance opined that while these amounts would create equity, they should not be deducted in the calculation, since they had already been taken account of in the value opinion[1132].

[1071] For the Palace II Theater, Vance used a figure of 4.173 million[1133] while Goodman used one of 11 million.

[1072] When Goodman subtracted the project's payables, he excluded all future interests to Castor[1134].

[1073] Vance subtracted 6.8 million of debts payable to others (creditors of 97872[1135] and 612044[1136]). Goodman opined that these debts should not have been subtracted.

[1074] Froese did not opine on MEC for 1988[1137]. In his 1997 report, based on a methodology and an analysis that he considered appropriate, and that he believed reflected a reasonable opinion, he had shown a surplus between 20.4 million and 39.4 million on the MEC project at the end of 1988[1138]. Since 1997, no new documents came to his attention other than the Bedard appraisal on the Palace II Theatre (which shows a higher value than the book value previously available to him)[1139]. However, in his report PW-2941, Froese's calculations on MEC do not include Palace II Theater – Palace II Theater has been looked at separately.

[1075] Rosen's value range for MEC was between 266 and 285 million, but he did not add value for the office pad component, and he used 11 million for Palace II Theater[1140].

[1076] In his written report, further to a calculation methodology based on the percentage of completion, Rosen suggested a minimum loan loss provision of 3 million.

[1129] Goodman, September 23, 2009, pp.123-124
[1130] Goodman, September 23, 2009, pp. 82-85, p.133
[1131] Goodman, September 23, 2009, pp. 82-85, p. 133
[1132] Vance, April 13, 2010, pp.234-238; Vance April 15, 2010, pp. 86-91; Vance, May 4, 2010, pp.212-216
[1133] PW-1137-2, Schedule 1; PW-2908, volume 3 (MEC), p.39
[1134] Goodman, September 23, 2009, pp.87-88
[1135] PW-323
[1136] PW-326
[1137] PW-2941, volume 3 (MEC section), pp.166 and following
[1138] D-1079
[1139] Froese, January 9, 2009, pp.48-53
[1140] PW-3033-3

In testimony[1141], Rosen agreed that it would have been acceptable not to record a LLP on Castor's loans to MEC in 1988 - based on Rosen's corrected calculation[1142] for Approach A resulting largely from his discovery of the Bédard appraisal[1143].

Conclusions

[1077] Without agreeing to any specific components found in the opinions of Froese, Rosen and Goodman on the MEC 1988 situation, the conclusion that it would have been acceptable not to record a LLP on Castor's loans to MEC is the Court's conclusion.

[1078] Therefore, no use going into many more particulars, save to explain two of the reasons why Goodman's proposition that there would have been a surplus of 73.4 million available as at December 31, 1988 is rejected.

- It would not be appropriate to use a total market value of 293 million, as Goodman did, since the increase value could only result from the actual construction of the office tower and since Royal LePage's comments in PW-1108A are of a "preliminary" nature. At best, the market value figure could be 279 million - 261 million as per Royal LePage's appraisal PW-1108 plus 18 million as per the December 22, 1988 offer relating to the pad component, assuming no value was attributed to the pad component in PW-1108[1144] and costs to complete the pad were part of the costs to complete to be deducted[1145].

- Future interests to Castor should not have been deducted from the costs to complete[1146] namely because neither the borrowers of Castor, nor Castor itself (was Castor to take possession of the property and finalize the construction) had the means and the capacity to pursue the project, without incurring that kind of costs as part of the costs to complete.

TSH

Additional evidence specific to TSH

Beneficial ownership

[1079] The shares of Lambert were issued to bearer.

[1141] Rosen, April 7, 2009, pp.186 and following
[1142] PW-3033-3
[1143] D-586
[1144] D-943; Vance, May 4, 2010, pp. 214-215
[1145] D-99D (108,076 million)
[1146] Vance, April 14, 2008, p.10

[1080] Baudet, the president of Lambert, thought Wersebe was the ultimate owner of Lambert but he acknowledged that Stolzenberg gave him instructions and was an authorized bank signatory.[1147]

[1081] Neither Prychidny nor Whiting[1148] believed that the ownership of the TSH resided with the YH group. Prychidny testified that: «*we had no other owner to look to other than Castor Holdings knowing that Mr. Gravenor was a nominee and not a beneficial owner, so we would look to Castor to act as the owner's representative and support the property in that way.*»[1149]

[1082] In letters dated September 14 and September 16, 1988 relating to negotiations to sell the hotels owned or managed by YHHL, including the TSH, Prychidny wrote:

> We have had the opportunity to canvas the **various owners** involved in the transaction in order to provide a counter-proposal acceptable to our principals[1150].
>
> On behalf of **our clients**, York-Hannover Hotels Ltd. agrees to pay (...) since **some of the owners** are involved in the London market, and the properties are not listed for sale, it may be very embarrassing to have you discuss a sale with a party **our owners** may be doing business with (...) **The owners** do not want the properties "shopped"[1151] (our emphasis)

[1083] Smith never saw a financial statement of Lambert and all his instructions with respect to this borrower came from Stolzenberg.[1152]

[1084] All instructions for the Lambert share subscription as well as the financing were provided to the lawyers by Castor.[1153]

[1085] Similarly, all instructions for Gravenor, a lawyer who was the nominee President and Director of both Topven and 594369 were provided by Castor, and Gravenor was indemnified by Castor for assuming these functions[1154].

Loans as of December 31, 1988

[1086] At December 31, 1988, 111 million of loans made in connection to TSH were owed to Castor (CHL and CHIF).

[1147] Baudet, April 28, 1999, pp. 51, 61, 66; April 30, 1999, pp. 83-84.
[1148] Whiting, November 18, 1999, p. 90.
[1149] Prychidny, October 15, 2008, p. 121.
[1150] D-1035
[1151] PW-2928
[1152] R. Smith, June 11, 2008, pp. 177–178, 184-185.
[1153] R. Smith, September 3, 2008, p. 14.
[1154] PW-234, PW-235, PW-236 and PW-236A

Owed to CHL

- Loan 1107 to Topven 88 secured by first mortgage - 40 million[1155]
- Loan GL/AC 66 (loan 1148) - operating line to Topven (or Topven 88), grid note to Topven - 7.6 million[1156]

Owed to CHIF

- Loan 888002/2003 to Topven 88 secured by second mortgage – 20 million[1157]
- Loan 576000/3002 to Lambert secured by a pledge of shares - 35.7 million[1158]
- Loan 576001/3009 to Lambert secured by a pledge of shares - 7.7 million[1159]

Interests recognized as revenue by Castor in 1988 on loans relating to TSH

[1087] $4,791,632.35 of capitalized interests on CHL's loans 1107, 066/1148 and CHIF's loan 8880021/2003 were recognized as revenue in 1988[1160].

Loans and commitment letters

[1088] Loan documents with Castor required the provision of annual financial statements according to GAAP, prepared by a CA, and the payment of interests in cash on a monthly basis.[1161] These covenants were not respected.

Prior to 1988

[1089] CHIF funded the purchase of Topven's shares by Lambert, as Lambert itself had no resources.[1162] Ron Smith was involved in the setting-up of the required loans to Lambert in 1984 and 1985, and he testified that there was no credit analysis made by Castor prior to making the loans to Lambert.

[1155] PW-212-1; PW-211; PW-1053-23-9; PW-1053-23,E-80
[1156] PW-1053-23-9; PW-167
[1157] PW-211-1; PW-1460-8; PW-1460-7; PW-1053- , B-39 and B-40
[1158] PW-1053-91, B-36
[1159] PW-1053-91, B-37
[1160] PW-1081A
[1161] First mortgage loan (#1107): PW-212-1; Second mortgage loan (#888,002/20): PW-2273; Grid note loan (#1148): PW-275C; Lambert Securities loans (#576,000/30 and 576,001/30): PW-136A and PW-2759.
[1162] R. Smith, September 3, 2008, p. 13.

> « I did not do any analysis of it and nobody else, in my mortgage investment group, did either».[1163]

[1090] By the end of 1985, Castor's exposure on the TSH project was approximately $73 million.[1164]

[1091] Topven incurred net losses of $3,425,000 in 1984[1165], of $7,111,000 in 1985[1166] and of $9,857,000 in 1986[1167].

[1092] The auditors of Topven (Peat Marwick) refused to issue its 1985 audited financial statements without having first received confirmation from Lambert that it would provide sufficient funds to meet its operating obligations and other financial engagements.[1168]

[1093] Despite promised support from Lambert, the auditors continued over the next year to be concerned about the collectability of a receivable, of $586,000 from YH, and about the deteriorating performance of the TSH. Peat Marwick also came to the conclusion that there were undisclosed related party transactions between Castor, YHHL and Topven. Those matters could not be resolved sufficiently to satisfy Peat Marwick's concerns and the 1986 financial statements were issued with serious qualifications.[1169]

> Our audit opinion contains two qualifications related to departures from generally accepted accounting principles evidenced firstly by the Company's failure to appropriately provide for the doubtful collection of its receivable from York-Hannover Hotels Ltd. and secondly for the difference of opinion between management and ourselves as to what constitutes a related party transaction under generally accepted accounting principles[1170].

[1094] The Topven 1986 financial statements also contained a "*going concern*" note expressing uncertainty as to the ability of the company to realize its assets and to discharge its liabilities in the normal course of business as a going concern.

[1095] Topven's auditors asked that they not be reappointed as auditors.[1171]

[1096] On June 13, 1986, Smith wrote to Stolzenberg that he had serious issues with YHHL's management of the TSH and with Castor's loans to borrowers connected to the TSH- he said:

[1163] R. Smith, June 11, 2008, p. 177.
[1164] R. Smith, June 11, 2008, pp. 166-169.
[1165] PW-404
[1166] PW-405
[1167] PW-187
[1168] PW-1080-3; R. Smith, September 3, 2008, pp. 52-53.
[1169] PW-411; R. Smith, September 3, 2008, pp. 79-81.
[1170] PW-188, p. 2
[1171] PW-188; PW-187: Audited financial statements of Topven Holdings for the year ended December 31, 1986; R. Smith, September 3, 2008, pp. 85–89.

> "It is imperative that we meet with KVW concerning the following issues. The meeting is long overdue and most of the items have reached the critical stage.
>
> We have bank-rolled these hotel projects and kept them alive for the past years by a combined investment of $100 million from the lenders and equity syndicates with the result that the projects are still seriously floundering and require substantial additional sums of money with no end in sight. York-Hannover Hotels have made no progress on either project. They have provided us with very limited cooperation and information based on instructions from KVW and the hotel personnel are operating without leadership, direction, enthusiasm or commitment...
>
> It is now very critical that alternate solutions be discussed, strategies selected, and the appropriate people selected and delegated the authority to implement the strategic objectives.[1172]"

[1097] In this same memorandum, Smith described as follows his concerns relating to the TSH:

> "Various lenders in the syndicate have requested the 1985 audited statements and a progress report on the hotel, as required under the terms and conditions of the Loan and Co-Lenders Agreement. To date we have provided vague verbal responses which have kept them at bay, however, they keep repeating their requests and they will not let the matter go unanswered much longer. The lack of financial statements and progress report will become a bigger issue and receive more scrutiny the longer it takes to deliver them.
>
> We have been informed that the auditors will not release the 1985 financial statements until they have –
>
> > a) Reviewed and satisfied themselves with the feasibility of the Topven Skyline Business Plan for 1986. They are quite concerned that the hotel has not performed anywhere near the previous forecasts, and that the real problem lies with the managerial capacity and competence of York-Hannover Hotels which may not be corrected in time for the hotel to survive.
> >
> > b) Received a commitment from Lambert to Topven to fund the 1986 anticipated deficiency of approximately $5 million via a preferred share issue or otherwise. This will require a substantial commitment from Lambert which may not end at this point and will be repeated in 1987 although hopefully on a smaller scale.
>
> The auditors are starting to get quite skiddish [skittish] on both hotel projects because of the poor performance of the properties and management, the high leverage, the cash deficiencies and the perceived insolvency of the situations. They are getting quite worried about their own liability and questioning everything

[1172] PW-1080-2

> according to the rules. They are even starting to question the ownership and cash support of the project by offshore share subscriptions and deposits and Castor's involvement as a lender[1173]".

[1098] Concern over the exposure of Castor on loans to Lambert was expressed by Jean-Guy Martin in the 1986 working paper file of CHIF:[1174] he attempted to assess the value of the underlying security and was unable to do so[1175].

[1099] In the 1986 working papers, Martin noted that interests had been capitalized (100%) on the Lambert loans since inception.[1176]

[1100] Martin, moreover, noted the reluctance of Stolzenberg to provide him with information regarding to Lambert and suggested delaying the release of Castor's financial statements until more information was obtained. His notes on the MAPs[1177] included the following:

> 11. CHI-N.V. has approximately $42 million in loan receivables (Lambert Securities Inc.) for which the security could not be obtained in Zug. WOST was apprised of the situation and appeared very reluctant to disclose the information we need. Interest on this loan has been capitalized since the loan was made in 1984 for a total of $8,500,000 of which $2,833,820 was received on January 28, 1987. The loan is secured by the following assets for which we could not ascertain the value (no documents available to us):
>
> i) 600 shares of Lambert Securities Inc. - Panama;
>
> ii) 15,679,315 Class B shares (non-voting) of Topven Holdings Inc. representing an amount of $15,679,315. This company owns and operates the Skyline Hotel in Toronto);
>
> iii) subordinated note receivable from Topven Holdings Ltd.(non-interest bearing) in the amount of $2,239,000;
>
> iv) note receivable from Skyeboat Investments Ltd. in the amount of $7,099,000;
>
> v) 11 common shares of 594639 Ontario Ltd.
>
> We strongly suggest that C&L Montreal (ECW/JG) obtain this information in order to determine the adequacy of the security before releasing financial statements in final form.[1178]"

[1173] PW-1080-2
[1174] PW-1053-95-1
[1175] Jean Guy Martin, January 5, 2010 pp. 137-161
[1176] Jean Guy Martin, January 5, 2010, p. 160
[1177] PW-1053-3-1
[1178] PW-1053-3-1

[1101] Further to those remarks, no financial statements of Lambert were obtained but C&L nevertheless released its 1986 audited financial statements.

[1102] Despite financing from Castor to refurbish the hotel, by 1987, the TSH was still unable to achieve the net operating income that YH had projected.[1179]

[1103] The loans had been made and renewed since the early 80s without any credit review of the borrower.

[1104] Although the TSH was an operating property and should have been able to service its debts, interests were being capitalized on the Topven loans[1180] and on the Lambert loans, at least as early as 1984[1181].

[1105] In October 1987, solicitors for the City of Etobicoke notified TSH's management that legal action would commence on December 1, 1987, unless outstanding realty and business taxes of 5.3 million were paid, or acceptable payment terms were agreed upon[1182]. Of that 5.3 million, the City of Etobicoke requested an immediate payment of approximately $2.35 million that represented business taxes and 1985 realty taxes.

Events taking place during 1988

[1106] By 1988, Castor had imposed controls over the TSH's bank accounts.

[1107] A 1987 Restated Operating Results for Topven, provided by Castor to C&L on February 24, 1988 for the 1987 audit, disclosed income before debt and depreciation of 2.9 million, and the following information regarding Castor's understanding of TSH's market value as of that date:

> "The appraisal used for financing purposes confirmed the value of $66 million for the hotel complex, which together with the extra development lands of approximately 15 acres (@ $800,000/acre = $12 million approximately) indicates a minimum value of $78 million for the property".[1183]

[1108] At the time of restructuring, Topven's financial statements disclosed an accumulated deficit of approximately 30 million[1184]. The restructuring transferred the Toronto Skyline property and operations into a new company with no deficit.

[1179] PW-1080-2 and PW-409
[1180] PW-1081A.
[1181] PW-1053-3, seq. p. 477.
[1182] PW-415
[1183] D-138
[1184] PW-431

[1109] The corporate restructuring of the project in 1988 was part of a final refinancing of the TSH.[1185] This refinancing had the effect of increasing Castor's loan exposure from 75 million (in 1987) to 111 million (in 1988).

[1110] Documents related to the first and second mortgages did not provide that all property taxes were current but only that "*In the event any amounts are owing, they shall be paid on a basis acceptable to the Lender.*"[1186] Also, the loans did not require the borrower to provide Castor with audited financial statements but only with financial statements prepared according to GAAP by a chartered accountant[1187]. Both minimal requirements were less onerous than prior loan covenants.

[1111] At the time of refinancing, property taxes of 3 million (including penalties)[1188] were in arrears for 1986 and 1987 and 1.3 million of 1988 property taxes remained outstanding. The Hotel cash flow was substantially less than that projected as at the date the loans were initially funded. The refinancing included arrangements with the City of Etobicoke to pay all 1986 and 1987 tax arrears by December 31, 1988.

[1112] The security on the 40 million loan included a mortgage on the land, buildings, furniture, fixtures and equipment of the Toronto Skyline, an assignment of revenues, leases and rents of the property, an assignment of the hotel management agreement, a guarantee of Topven (1988), and a pledge of issued and outstanding shares of Topven[1189].

[1113] The security on the $20 million loan included a second mortgage on the Toronto Skyline property and the same assignments, guarantees and pledges as the $40 million loan[1190].

[1114] The residual debt of $3.9 million was put into a grid note (loan 1148 to Topven), which grew over the years pursuant to capitalized interests on the grid note loan, the first and second mortgage loans to Topven (1988), as well as Castor's financing of the operating expenses of the TSH.[1191]

[1115] A balance sheet of 5943639 Ontario Ltd. as at August 31, 1988 showed that there was no value to the shares of 594369 Ontario Ltd[1192].

[1116] Interests on the $40 million first mortgage, the $20 million second mortgage and the $5 million grid note were all capitalized to the grid note[1193].

[1185] PW-420.
[1186] PW-212-1, pages 3(2) and 4(1).
[1187] PW-212-46, page 10, 7.1(e), (j) and (i).; PW-211-2, page 4(j) and (n).
[1188] PW-211-26
[1189] PW-212-46, page 9.
[1190] PW-211-2, page 1.
[1191] R. Smith, June 11, 2008 at pp. 172 -173; PW-167D. PW-276
[1192] PW-1460-4

[1117] YH had not and did not put any money into the TSH - it was only Castor which funded the operating shortfalls of the hotel, including payroll and property taxes.[1194] Even when the possibility of losing the hotel was tangible, Wersebe did not and would not provide any financial assistance[1195].

[1118] Negotiations were entered into by YHHL to try to sell at once the hotels that they owned or managed, but nothing materialized.

- On August 18, 1988, an initial offer was made to YHHL to purchase the hotels (MLV, TSH, CSH, OSH and Triumph) for 190 million.[1196]
- YHHL prepared a property summary of hotels that were being considered for sale.[1197]
- Subsequent counter-offers made by YHHL for higher amounts[1198] were ignored and the 190 million initial price was again proposed by the potential purchaser, subject to due diligence.[1199]
- By November 1988, it was evident that a higher price was not obtainable and the offer of 190 million was insufficient from the perspectives of YH and Castor.[1200]
- Other initiatives by YHHL to try to attract investors were recognized as unrealistic and were not pursued.[1201]
- A variety of scenarios were drafted by YHHL with different values ascribed to the management contracts. However, Prychidny explained that the management contracts were "worthless"[1202] and that these values were merely a "plug".[1203]

[1193] PW-1460-5
[1194] R. Smith, September 3, 2008, pp. 49 – 51, 55 – 56; PW-418; PW-1080-7; PW-1080-9; See also PW-414.
[1195] Prychidny, October 14, 2008, pp. 47–49.
[1196] PW-499. See also PW-499E.
[1197] D-140
[1198] PW-499A; Prychidny, November 4, 2008, pp. 214-220.
[1199] PW-499D; Prychidny, November 4, 2008, pp. 214-220.
[1200] PW-499B; Prychidny, November 4, 2008, pp. 214-220.
[1201] PW-499F; R. Smith, September 23, 2008, pp. 14-15.
[1202] Prychidny, November, 10, 2008, pp. 79 – 82.
[1203] Prychidny, November 4, 2008, pp. 133 – 134.

[1119] The income pre-debt fell far short of the projected budgets and was insufficient to service the annual interest obligations[1204]: the TSH recorded less than $2 million of pre-debt income but had an annual interest obligation of more than $15 million.

[1120] The mortgage and loan ledger cards indicated, in addition to the capitalized interest on the loans, that Castor was paying the fees and the operating expenses of the borrower.[1205]

[1121] On October 28, 1988 Castor instructed YHHL that, due to the refinancing, an audit of Topven would no longer be required for either 1987 or 1988, and the firm of O'Hagen & Scarrow would be used to prepare Notice to Reader's statements (not audited or reviewed) for Topven (1988)[1206].

[1122] In 1988, TSH generated only 1.8 million of cash flow before interests and depreciation,[1207] and the total accumulated deficit of its owners (Topven, Topven (88) and Lambert) as of December 31, 1988, was 54.7 million[1208].

[1123] Lambert paid interests in early 1989 and TSH could not have been the source of these funds: therefore, the funds must have come from another source. Although the evidence does not establish this other source for such payment of interests, it shows that cash circles of Castor's funds were the device used to pay interests on Lambert's loans thereafter[1209].

TSH appraisals

[1124] Appraisals or market value estimates of the TSH were prepared in 1988[1210]. The assumptions were provided by Prychidny, including the planned operational strategy and the assumption that 12 million worth of renovations would be completed within one year.[1211]

[1125] An appraisal prepared by Pannell, Kerr, Forster in relation to the Toronto Skyline, dated January 15, 1988[1212], provided an estimate of value between 56.2 and 62 million, without considering the value of the development land, estimated by Walter Prychidny at 8 to 10 million[1213].

[1204] PW-1084A and PW-424, bates p. 9; shows income pre-debt of $1.8M and a loss for the year of $9M (this is a preliminary report but the figures are confirmed in PW-429, the 1989 statement with comparative figures for 1988)
[1205] PW-167D.
[1206] PW-428, paragraph 2.
[1207] Froese, PW-2941, vol. 2, p.45, paragraph 2.92
[1208] Froese, PW-2941, vol. 2, p.46, paragraph 2.95
[1209] Froese, January 27, 2009,pp. 66 and following; Levi, January 14, 2010, pp.81 and following
[1210] PW-421; PW-422; PW-423
[1211] Prychidny, October 17, 2008, pp. 149-150.
[1212] PW-421
[1213] PW-422

[1126] A Gillis appraisal[1214], dated April 15, 1988 and signed by Mullins, appraised the TSH at a value of 93 million and included land and improvements, all the furniture, fixtures, equipment, licenses, contracts, leasehold interests, and goodwill. It attributed a value of 10 million to surplus land.

[1127] The Gillis appraisal assumed, among other matters, a net operating income of 7.4 million to 9.7 million for each of the five years subsequent to April 1988, an assumption well in excess of the income before interests and depreciation of 1.2 million that was realized in 1987 not to mention the net losses of approximately 9 million that were incurred during both years 1987 and 1988.

[1128] The Gillis appraisal included specific reference and comments on the Constellation Hotel:

> "Currently, the Constellation Hotel, located on Dixon Road airport corridor, just west of the subject property, is on the market for $116,500,000.00 including surplus land having an estimated market value of $7,500,000.00.
>
> The offering data was prepared by the management firm of Laventhol & Horvath, and includes a pro-forma maintainable income estimate for the hotel complex of $10,943,000.00 before financing depreciation and income taxes...
>
> The Constellation Hotel is considered to be comparable to the subject in location, site area (15.75 acres), total number of rooms (854), restaurant, convention and recreational amenities. It has a multi-level car park with a capacity of 1,300 cars plus surface parking on the surplus land.
>
> The Constellation Hotel is also similar to the subject in its historical development...
>
> The Constellation lacks the subject's superior amenities provided by the commercial mall tenants, but is considered to be superior in location, age and overall appearance.
>
> While the foregoing is only an offering, it is believed to reasonably reflect an overall capitalization rate for a large full service convention type hotel, within the airport market."

Other information

[1129] Castor treated TSH as unique and distinct from the YH loans and acted in an owner-like manner. For example:

[1214] PW-425

- The interests on the TSH loans were never accrued in account 046, which account was only used for YH direct loans or project loans;[1215]

- Stolzenberg was responsible for the appointment of the director and officer of the owner entities, and Castor provided them with an indemnification agreement.

[1130] Defendants' expert Morrison testified that «*it was generally known that it* (TSH) *was not a good project*», that «*it was a real dog.*»[1216]

[1131] C&L recorded a management representation to the effect that the Constellation Hotel located near to the TSH had been sold for approximately $115 million.

Experts' evidence

[1132] Plaintiff's experts concluded that the audited consolidated financial statements with respect to the carrying value of Castor's loans connected to the TSH project were materially misstated.

- Vance opined that the minimum LLP should be $20.4 million[1217];

- Rosen opined that the minimum LLP should be 21.9 million[1218];

- Froese opined that the minimum LLP should be 24.4 million[1219].

[1133] Plaintiff's experts also concluded that the loans should have been placed on a non-accrual basis[1220] and capitalized interests and fees should have thus been reversed.

[1134] Goodman severed his analysis of Lambert from the other TSH related loans, although he clearly understood that the TSH was owned by Lambert.

[1135] Goodman asserted GAAP did not permit him to assess the loss on the Lambert loans. He considered eight elements «*in determining whether it was probable that Castor would incur a loss on its loans to Lambert*»[1221], in order to support his conclusion of no reliable evidence of any such loss as at December 31, 1988 with respect to Lambert.

[1136] Before taking account of the Lambert loans, all experts came to similar surplus figures:

[1215] R. Smith, September 18, 2008, pp. 19–20.
[1216] Morrison, October 5, 2006, p, 141.
[1217] Vance, April 8, 2008, pp. 100-103; PW-2908
[1218] PW-3033; Rosen, April 7, 2009;
[1219] Froese, January 27, 2009, pp. 95 and following and PW-2941-4, Schedule 1
[1220] PW-2941, Vol. 2, p. 4; PW-2908, Vol. 1, p. 4-I-18 to 4-I-19; PW-3033, Vol. 2, Appendix A, p. 6.
[1221] D-1312, pp. 496–499

Expert	Surplus
Vance	23 million
Froese	19 million
Rosen	25.4 million
Goodman	24.9 million

[1137] Goodman's surplus figure could not cover the Lambert loans. Had Goodman taken account of the Lambert loans, as Plaintiff's experts did, Goodman would have come to a minimum deficiency figure of 22.3 million.

Conclusions

[1138] Evidence with respect to the beneficial ownership of the TSH is equivocal, but given the facts as they unfold during the relevant years (1988-1990), the Lambert loans cannot be assessed as part of the YH group of loans.

[1139] Ford's testimony that she would have seen financial statements of Lambert that showed that Lambert held marketable securities is neither credible nor reliable. The only source of funds available to Lambert to repay its loans was the value of the TSH.

[1140] At best, the market value of the TSH was 93 million: TSH did not perform financially at profitability levels that were even close to the projections included in the appraisal of Gillis Associates Real Estate Appraisers Limited dated April 15, 1988 – therefore, the assumptions underlying the Gillis valuation might be unreasonable.

[1141] Taking account of this best scenario as to market value, and the various figures proposed by all experts, Castor should have recorded a LLP of at least 18 million for its loans related to TSH.

CSH

Additional evidence specific to CSH

Beneficial Ownership

[1142] Skyeboat and 321351 held, between them, the shares of Skyview Hotels Ltd., which owned CSH.

[1143] No share certificates or minute books were located to determine the beneficial ownership of the CSH.

[1144] Evidence with respect to the beneficial ownership of the CSH after 1985 is equivocal, although Granton Patrick, a lawyer, asserted that he was «*the legal and beneficial owner of the company which owns the hotel*», i.e., 321351. As well, Gravenor & Keenan, a law firm, held an option over Patrick's position, with the option extending for 20 years.[1222]

[1145] Whiting stated that CSH was not part of the ownership chain of the YH group of companies[1223]. He referred to the hotels listed in Prychidny's schedule[1224] (which included the CSH) as the "*hotel properties that were within the York-Hannover Hotels sphere of influence*"[1225].

[1146] Ron Smith testified that:

- he received his instructions from Wersebe for the acquisition by 321351 of the leasehold interests from the Four Seasons Hotel, and for the completion of this acquisition[1226];
- 321351 was a company taken off the shelf just to hold the leasehold interests – it had no other assets[1227];
- the shares of 321351 were held in trust by Granton Patrick, a lawyer representing YH and Castor, upon the instructions of Wersebe and Stolzenberg[1228];
- Granton Patrick had no economic interest – he was just a nominee[1229];
- at Stolzenberg's insistence, the shares of Skyeboat were transferred over to Lakeland and Gravenor Keenan, Castor's law firm, was given an option to buy back the Granton Patrick interest, in 321351[1230];
- Four Seasons wanted a guarantee; it was not prepared to accept a YH guarantee; it wanted Castor's guarantee[1231];
- In 1986, Millican became a director and nominee of Skyeboat and Lakeland, further to instructions received from Stolzenberg,[1232] and thereafter, also of Skyview[1233];

[1222] PW-226
[1223] Whiting, November 18, 1999, pp.90-91
[1224] PW-499C-1
[1225] Whiting, February 14, 2000,p. 15
[1226] Ron Smith, September 5, 2008, pp.84-85
[1227] Ron Smith, September 5, 2008, p.87
[1228] Ron Smith, September 5, 2008, pp.85-86, 91-92
[1229] Ron Smith, September 5, 2008, p.88
[1230] Ron Smith, September 5, 2008, pp. 86,87, 91-92, 97 and PW-1086A
[1231] Ron Smith, September 5, 2008, pp.86-87
[1232] Ron Smith, September 5, 2008, p.100 ; see also PW-1086-4

- All approvals came from Stolzenberg[1234].

[1147] Prychidny testified that he did not know who the owner of the CSH was but that each time he needed instructions, from a management point of view, he turned to Castor[1235].

[1148] In letters dated September 14 and September 16, 1988 relating to negotiations to sell the hotels owned or managed by YHHL, including the CSH, Prychidny wrote:

> We have had the opportunity to canvas the **various owners** involved in the transaction in order to provide a counter-proposal acceptable to our principals[1236].
>
> On behalf of **our clients**, York-Hannover Hotels Ltd. agrees to pay (...) since **some of the owners** are involved in the London market, and the properties are not listed for sale, it may be very embarrassing to have you discuss a sale with a party **our owners** may be doing business with (...) **The owners** do not want the properties "shopped"[1237] (our emphasis)

[1149] The financial statements of Skyeboat Investments Ltd.[1238] signed by Doane Raymond Pannell include the following inscription: "*Note payable to affiliated company Castor*".

[1150] The Balance Sheet of 321351, part of a Notice to Reader prepared by Doane Raymond Pannell, includes the following inscription:" *Due to affiliated companies, Skyeboat, Skyview, Castor*"[1239].

Prior to 1988

[1151] Although the CSH was the best hotel managed by YHHL,[1240] it was already in financial difficulties by 1985. Its income from operations was insufficient to meet its obligations under the loan agreements,[1241] and it was struggling with various management weaknesses such as the inability to finalize its business plan.[1242] Concerns about the solvency of the owner of the freehold interest were expressed by Skyeboat's auditors who refused to issue the 1985 financial statements without having received confirmation that sufficient funds would be provided to meet obligations.

[1233] Ron Smith, September 5, 2008, p.110; see also PW-1463-10
[1234] Ron Smith, September 5, 2008, pp. 97-98-99,110-111
[1235] Prychidny, October 15, 2008, pp.174-175
[1236] D-1035
[1237] PW-2928
[1238] PW-466C
[1239] PW-465B
[1240] Prychidny, November 10, 2008, p. 137.
[1241] PW-1086-6.
[1242] PW-1080-2; R. Smith, September 5, 2008, pp. 102-105; D-1032.

[1152] The CSH was much less competitive in the marketplace and by 1986, Castor acknowledged:

> «We have bank-rolled these hotel projects [TSH and CSH] and kept them alive for the past 3 years [...] with the result that the projects are still seriously floundering and require substantial additional sums of money with no end in sight.»[1243]

[1153] Between 1985 and 1987, CSH experienced chronic cash shortages and turned to Castor to fund operating costs,[1244] including rent, payroll and taxes.[1245] No financial assistance for the CSH came from YHHL or Wersebe, although they were well aware of the hotel's financial situation and its need for cash, «*but none was ever forthcoming [...] from the York-Hannover group.* » The only financial support that the hotel could count on came from Castor, which Prychidny turned to when seeking instructions from the owner: «[...] *there was no one else to turn to, there was no other Mr. Skyview or Mr. Skyeboat or Mr. 321, it was just Castor or York Hannover* [...]»[1246].

[1154] The renovations contemplated by the Pannell Kerr Forster ("**PKF**") appraisal in early 1987 were never funded and the projections for income were never achieved.[1247]

[1155] The CSH defaulted on its covenants year after year but Castor never enforced its security.

[1156] As at year end 1987, the loans already amounted to 49.3 million,[1248] add in a contingent liability of 3.6 million and accrued interest receivable. Consequently, even before 1988 refinancing, Castor's exposure exceeded by almost 8 million the lower range of the estimate of value provided by the PKF report.

Events taking place during 1988

[1157] The CSH project had been in Castor's books since the early 80s and was refinanced in 1988.[1249]

[1158] Skyeboat and 321351 Alberta sold to Skyview their respective real estate, and operating assets and liabilities, and leaseholds, effective at the close of business on December 31, 1987[1250].

[1243] PW-1080-2.
[1244] PW-1086-1, p. 4-5; R. Smith, September 5, 2008, p. 75; Prychidny, October 14, 2008, pp. 39-40.
[1245] Prychidny, October 14, 2008, p. 74; October 15, 2008, pp. 192-195. See also PW-474, PW-1086-6.
[1246] Prychidny, October 15, 2008, pp. 194-195.
[1247] R. Smith, September 5, 2008, pp. 143-146.
[1248] PW-1053-27, seq. pp. 215-218, 230-231 (E212–E215, E227–E228) : audit confirmations returned to C&L
[1249] R. Smith September 5, 2008, pp. 147-148; PW-1053-23, seq. p. 168.
[1250] PW-468.

[1159] As a result of this 1988 restructuring, Castor created a 1st mortgage loan for 25 million in the Montreal portfolio and a 2nd mortgage loan for 16 million in the overseas portfolio (CHIF), and opened two deposit accounts: one for operating expenses and one for future renovations.

[1160] Security provided for the first and second mortgages included: a charge on the Calgary Skyline property, general assignment of revenues, leases and rents, assignment of the common shares of Skyview, assignment of the hotel management agreement, and guarantees provided by Skyeboat and 321351[1251].

[1161] The $25 million first mortgage to Castor was further secured by a $6 million cash deposit agreement, a cash deposit with Castor. Of the $6 million deposited funds, $2.5 million were to be used for capital renovations and $3.5 million were to be held as an interest reserve. As at December 31, 1988, the remaining deposited funds consisted of $2.5 million for the capital renovations reserve and $1.7 million for the interest reserve[1252].

[1162] CHL's guarantee of the VTB to Four Seasons Hotel Ltd. for 3.6 million remained.

[1163] By December 31, 1988, Castor's loans to 321351 Alberta and Skyeboat had increased from 6 million and 9.7 million, respectively, to 7.9 million and 10.8 million. The loan increases resulted primarily from capitalized interest[1253].

[1164] The 3.6 million promissory note of 321351 Alberta's owing to Four Seasons remained outstanding as at December 31, 1988.

[1165] At December 31, 1988, Skyview Hotels' financial statements disclosed that the long-term lease obligation regarding equipment owing to Calgary Convention Centre, had an outstanding balance of approximately $739,000, unchanged from 1987, and that other long-term lease obligations amounted to approximately $40,000[1254].

[1166] 1988 was the peak year for the hotel market and CSH's most profitable year, but it was still not able to meet its debt service requirements and the hotel continued to lose significant amounts of money after debt service.[1255]

[1167] In light of the ongoing difficulties with all of the YHHL hotels, the decision had been made in 1987 to try to sell the hotels as a group.[1256] In 1988, YHHL entered into

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[1251] PW-1087-1 and PW-1087-3.
[1252] PW-167S and PW-167T.
[1253] PW-167Q and PW-167R.
[1254] PW-467A, Financial Statement Note 5.
[1255] Prychidny, October 15, 2008, p. 175.
[1256] Prychidny, October 14, 2008, pp. 154-160.

negotiations to sell the hotels that it owned or managed all at once, but offers received fell well below what was deemed acceptable by either YHHL or Castor.[1257]

[1168] According to Prychidny, a sale of the hotels at a realistic price would have crystallized huge losses for Castor, even in 1988, the peak year for the hotel market.[1258]

[1169] The loan documents required monthly payments of interests, annual placement fees and annual financial statements of Skyview, and such covenants were not being respected - interests and fees on the CSH loans were being systematically capitalized[1259].

[1170] The planned renovations were not done even though the 1987 PKF appraisal assumed that the renovations would be completed by February 1988: capital expenditures paid in December 1988 included $5,000 of "*architectural fees related to hotel planned renovations*"[1260].

Loans as of December 31, 1988

[1171] At December 31, 1988, deducting the balance in hand of $4.2 million of the two Skyview deposits (capital renovations and interest reserve), Castor's exposure in connection to loans made to the CSH was $59.4 million, which resulted from:

Owed to CHL

- Loan 1097 to Skyview - 25 million – secured by 1st mortgage;
- Loan 1147 to Skyeboat- 10.8 million – secured by a pledge of shares;
- Loan 1143 to 321351- 7.9 million – secured by a pledge of shares;

Owed to CHIF

- Loan 790002/2005 to Skyview - 16 million – secured by second mortgage

Others

- Guarantee (VTB) to Four Seasons - 3.6 million.

[1257] D-1312, p. 418; PW-499, PW-499D, PW-2928; Prychidny, October 14, 2008, pp. 161-165, 169-170.
[1258] Prychidny, October 14, 2008, pp. 155–161.
[1259] PW-167R, PW-167Q, PW-167T
[1260] PW-467B, Bates page 000005.

Interests recognized as revenue

[1172] The required reversal of interests and fees, in respect of the CSH for 1988, was in the amount of $4.8 million[1261].

Loans and commitment letters

[1173] The loan agreements for the 1st and 2nd mortgage loans provided that interests were to be paid monthly and the borrower was to provide annual financial statements, prepared in accordance with GAAP by a CA.[1262]

[1174] With respect to the loans to 321351 and Skyeboat, the promissory notes indicated that interests were to be paid monthly and, in the event of default, the principal and interests would immediately fall due.[1263]

CSH: market study

[1175] In early 1987, a new estimate of value was prepared by PKF providing a range of values between 45 million and 55.6 million.[1264] The estimate was based on a number of assumptions, including renovations that were to be completed within a year so that higher room rates and higher occupancy rates could be achieved in time for the Calgary Olympics of February 1988.[1265]

[1176] This PKF market study was based on projected revenues that were never actually achieved by the CSH.

Other information

[1177] Account 046 was used by Castor as the clearing account for the YH Group loans.

[1178] Account 046 was never used in connection with any of the loans connected to the CSH, a fact that Goodman acknowledged but could not explain[1266].

Experts' evidence

[1179] There is no dispute that there was a security shortfall on Castor's loans in relation to the CSH.

[1261] PW-2908, Vol. 1, pp. S-8 to S-10.
[1262] PW-1087-1, PW-1087-3, PW-1087-3A.
[1263] PW-1087-7, PW-1087-8, PW-1087-10.
[1264] PW-469, bates 000004.
[1265] PW-2941, Vol. 2, pp. 144–145.
[1266] Goodman, October 26, 2009, pp.250 and following, namely p.254 "*Again, I can't explain absolutely everything in this*" and pp.255-256

[1180] All of Plaintiff's experts agree that the audited consolidated financial statements of Castor were materially misstated because the carrying value of the loans connected to the CSH was overstated.

[1181] Based on the assumption that one can rely on the appraisal of the CSH, the Plaintiff's experts identified the following minimum amount of loan loss provision required:

Expert	Minimum amount of LLP (or range of)
Vance	9.4 million
Froese	11.3 million[1267]
Rosen	3.8 to 14.4 million

[1182] Plaintiff's experts also agree that: «*the loans to 321351 Alberta, Skyeboat and Skyview Hotels should have been placed on a non-accrual basis as at December 31, 1988 or earlier*» and «*the financial implications to Castor of placing loans to borrowers connected to the Calgary Skyline on a non-accrual basis, and the magnitude of the increase in Castor's allowance for loan losses, created uncertainty as to Castor's ability to continue as a going concern*».[1268]

[1183] Goodman identified a loan loss exposure of 11.9 million[1269] based on a market value figure of 50.3 million[1270]. The 2.5 million dollar difference between Goodman and Vance represents the amount of the costs to complete renovations that Goodman did subtract from his proposed market value[1271].

[1184] Despite the loan security deficiency on these loans, Goodman opined that there was no probable and estimable loss given that there was a loan security surplus position on the other components of the YH loan portfolio that was available to offset it. Such conclusion is based on Goodman's presumption that the CSH was owned by Wersebe[1272] and that there was a right to offset against the surpluses in other YH projects.

[1185] Goodman was the only expert for either party that concluded unequivocally that the CSH was beneficially owned by Wersebe (and therefore part of the YH Group)

[1267] Froese, January 27, 2009, pp. 95 and following and PW-2941-4, Schedule 1
[1268] PW-2941, Vol. 2, p. 126; PW-3033, Vol. 2, Appendix G, p. 5.
[1269] D-1312, pp. 429–430.
[1270] D-1312, p.427
[1271] D-1312, p.436
[1272] Goodman, October 26, 2009, pp.33-34, 40 and following, 59-61, 65,113-114, 137

during the relevant years.[1273] For example, Selman suggested that Stolzenberg may have owned the leasehold rights.[1274]

[1186] Goodman relied on two references to support his statement that 321351 was owned by Wersebe: the testimony of Baudet, and exhibit PW-1086-3.[1275]

[1187] Goodman also concluded, "*from an accounting perspective*" as he said, that Lambert was owned by Wersebe – that Wersebe was the beneficial owner[1276] and the ultimate shareholder of Lambert[1277].

[1188] With respect to the beneficial ownership of Skyeboat, Goodman asserted that the shares were held by Lakeland and Lambert, and relied on the testimony of Baudet to conclude that the beneficial owner was Wersebe.

[1189] Goodman acknowledged that over the years, namely at year-end, cross collateralization was done through agreements as Castor and its borrower agreed to such course of action[1278].

Conclusions

[1190] Baudet never testified that 321351 was owned by Wersebe, and exhibit PW-1086-3 expressly states that a lawyer was the legal and beneficial owner of 321351.

[1191] Assessing evidence available[1279], Goodman came to the conclusion that CSH and Lambert were "owned" by Wersebe and therefore, loans to CSH were part of the YH group of loans.

[1192] The Court does not share Goodman's point of view in light of the following:

- The content of Smith's, Prychidny's and Whiting's testimonies (hereinabove mentioned) and the content of exhibits PW-234, PW-235, PW-236A, PW-236B, PW-465B, PW-466C, PW-1086A, PW-1086-4 and PW-1463-10;

- The fact that account 046 was never used in connection with any of the loans connected to the CSH, supports the conclusion that neither Castor nor York-Hannover believed that Wersebe was the owner of the CSH.

- Other evidence that, during the 1988 to 1990 period, ownership decisions were made by Castor[1280]; and

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[1273] D-1312, p. 416.
[1274] D-1295, pp. 33–34, para.4.1.33.
[1275] D-1312, p. 416, ftn 760 and 762.
[1276] Goodman, October 26, 2009, pp.176-187
[1277] Goodman, October 26, 2009, pp.187-190
[1278] Goodman, October 26, 2009, pp.67-72
[1279] Goodman, October 26, 2009, pp.128, 172-173, 239-241, 243

- Wightman's handwritten inscriptions in the AWPs made during the year-end wrap-up meeting with Stolzenberg "*Skyline loans are actually split between four owners*" and "*The only common feature is that they were under management by Skyline*".[1281]

[1193] CSH deficiencies could not be offset by alleged surpluses in the YH group of loans and a material LLP was needed.

OSH

Additional evidence specific to OSH

Prior to 1988

[1194] In the early 80s, Campeau had provided the YH group with an allowance of 5 million for renovations, but only 2 million of such sum was actually used for the OSH. Therefore, as early as 1985, the OSH was a "tired" hotel while YHHL still had to pay a rent, which had been increased in order to allow Campeau to amortize the 5 million leasehold improvement payment for renovations.[1282]

[1195] Castor's involvement with the OSH and its loans to Skyline (80) commenced in 1984. Castor's loan was thereafter been extended annually.

[1196] From the outset, the hotel could never generate sufficient revenue for YHHL to meet its lease payments to Campeau, let alone to service its interest and fee obligations to Castor.

[1197] From 1987 and up to the 1991 period, Campeau repeatedly sent letters of default to YHHL, Skyline (80) and Castor. [1283] As an example : on July 26, 1988, Campeau wrote the following letter :

> Skyline Hotels (1980) Ltd. ("Skyline") is in default of its covenant to pay rent under the Lease with Campeau Corporation (...)
>
> Please be advised that the Lease as modified is hereby forfeited subjects to all rights of Campeau Corporation (...)
>
> Campeau Corporation requires vacant possession of the leased premises. In recognition of the fact that a hotel operation is on-going, Campeau Corporation is prepared to allow you a period of two weeks from today's date in order to close down or move the hotel operation from the leased premises. However, this two

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[1280] See the sections of the present judgment relating to LLP for TSH in 1988, 1989 and 1990 and LLP for CSH in 1989 and 1990

[1281] PW-1053-12, page 77

[1282] Prychidny, October 14, 2008, pp.42-43; Prychidny, October 15, 2008, pp.144-147

[1283] Prychidny, October 15, 2008, pp. 145-153; PW-450 series

week grace is conditional upon receipt by Campeau Corporation of the attached Consent to the issuance of a Writ of Possession executed by Skyline (...)[1284]

Events taking place during 1988

[1198] 1988 Financial statements of Skyline (80) indicate:

- $1,875 of income before interest and rent;
- $1,804 of rent;
- $4,726 of interest expense;
- $4,655 of loss before depreciation; and
- $15,097 of shareholder deficiency[1285].

[1199] OSH did not perform well financially. Its levels of profitability were not even close to the projections that were included in the Fitzsimmons appraisal dated July 22, 1988, which is referred to further on in the present judgment.

[1200] In order that a settlement could be reached with Campeau, the landlord, CHL advanced $949,048.64 which was charged to Loan 1121/1123 in the name of YHHHL – and was described as "*$4mm Grid Note, Skyline 80*" in the loan ledger.

Loans as of December 31, 1988

[1201] As at December 31, 1988, the following amounts were owed to Castor in relation to the OSH:

- Loan 1049[1286] to Skyline 80 - $10.4 million
- Part of loans 1121/1123 to YHHHL[1287] - $992,000.

[1202] Loan 1049 was secured by a fixed and floating charge debenture on all assets of the borrower, including furniture, fixtures and equipment of the Ottawa Skyline Hotel, assignment of leasehold of hotel, and pledge of various shares of YHHHL, YHHIL, YHHL and Skyline 80.

[1203] Skyline 80's only significant asset was its leasehold interest in the OSH.

[1284] PW-450-W
[1285] PW-454
[1286] PW-453-1
[1287] PW-452

Interests recognized as revenue

[1204] Interests on Loan 1049 were capitalized on a monthly basis through account 046 and, at the year end, a circular transaction (cash circle) was made to offset the accrued interests.

Loans and commitment letters

[1205] The loan documentation for loan 1049 to Skyline (80) called for[1288] the borrower to provide annual financial statements, revenue and expense statements, rent rolls and statement of capital expenditures when requested by the lender, and also to pay when due all accounts payable and taxes owing on the lease. None of these covenants was being fulfilled by the borrower, who also failed to pay interests and fees when due.

OSH appraisals

[1206] The appraisal figures used by C&L for the purpose of their 1988 audit were based on a Mullins appraisal of the leasehold interest dated January 15, 1985 [1289] which gave the leasehold interest a value of $9.5 million, and on an appraisal of General Appraisal of Canada Limited ("**General Appraisal**") dated January 22, 1985[1290], which gave the furniture and equipment a value of $5.6 million, for a total value of $15.1 million.

- The value given by General Appraisal is a replacement value (new equipment).
- The value given by Mullins appears to also include the value of the furniture, the fixtures and the equipment[1291].

[1207] An appraisal prepared by Fitzsimmons[1292] commissioned by a third party (in connection with a failed Maritime Life refinancing), dated March 1, 1987, established a future potential value of $29 million based on a $10.4 million renovation program being carried out on the hotel, which operates for a time after such renovations are done in order to fully implement the planned management and the marketing programs. $16 million of that $29 million appraisal value is ascribed to the freehold interest of Campeau. Therefore, in order to achieve the $13 million value left to Skyline 80, a renovation program in excess of $10 million had to be performed.

[1208] Another appraisal was obtained, the Juteau valuation[1293] dated July 22, 1987, also premised on the same renovation program costing in excess of $10 million. As

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[1288] For example, see PW-1093-1
[1289] PW-460
[1290] PW-461
[1291] PW-460, bates #000015, 000045, 000047, 000050, and 000055
[1292] PW-462
[1293] D-44

opposed to the Maritime Life situation, however, this appraisal was commissioned by YH and not by an outside lender. This appraisal determined that the freehold value of the property was approximately $33.8 million, and that the leasehold value to Castor, after renovation, was $16.7 million.

Other information

[1209] When Maritime Life received the Fitzsimmons appraisal, it reduced its financing proposal from $10 million to $6 million. An additional $3 million would be provided only if the hotel achieved the projected performance. In view of such reduction, and because the investment clearly did not make sense, the Maritime Life financing lapsed.[1294]

[1210] Prychidny testified that, as the manager and the person mandated to operate the hotel, it didn't make business sense to spend $10 million to potentially earn $3 million of value.[1295]

[1211] Prychidny testified that he expressed to Stolzenberg, from 1988 onwards, that the OSH was «*worth nothing*»[1296].

Experts' evidence

[1212] Only Vance and Goodman provided an opinion with respect to the OSH. They both computed a security deficiency. The more significant difference between Vance and Goodman relates to the use of the appraisals in relation to this property.

[1213] Vance opined that the available appraisals could not be used as audit evidence given the unrealistic assumptions that had been used, and that no value, or very little value ($0.6M), should be given or could be given to the leasehold interest, which could be forfeited by Campeau.

[1214] Vance also came to the conclusion that no value could be given to Skyline 80 shares in light of their 1988 financial statements[1297].

[1215] Vance opined that a minimum loan loss provision of 10.9 million should have been recorded and that all interests and fee revenue on the OSH loans ($2.16 million[1298]) should have been reversed.

[1216] Goodman acknowledged that there was a deficiency in Castor's loan position of $6.3 million[1299] based on the $6.7 million value that he attributed to the leasehold interest [1300].

[1294] Prychidny, October 15, 2008, pp. 167-168.
[1295] Prychidny, October 15, 2008, pp. 163, 166.
[1296] Prychidny, November 3, 2008, p. 40.
[1297] PW-454
[1298] PW-2908, Vol. 1, S-8 to S-10.

[1217] On the usefulness of the appraisals, Goodman wrote: "*the Juteau appraisal, in my view, was the most appropriate to use in the calculation of the December 31, 1988 freehold market value of the property, whereas the Fitzsimmons appraisal was the most credible in providing an estimate of the required renovation costs to achieve the freehold market value*".[1301]

[1218] Goodman nevertheless concluded that it was reasonable for Castor not to record a LLP since there were other amounts of surplus to offset the deficiency.

Conclusions

[1219] The loans associated with the OSH were in default, non-performing and the project was in severe financial difficulty.

[1220] In cases where the borrowers are in breach of their loan covenants, where they cannot and do not pay interests or fees for several years, and where the leasehold interest is on the brink of forfeiture every single month, GAAP cannot be interpreted as principles allowing the fact that there is reasonable assurance of the collectability of the revenue associated with such loans.

[1221] Goodman's theory that surpluses in the YH group of loans existed and could be used to offset deficiencies is rejected, as discussed earlier and further on in the present judgment.

[1222] Vance's opinion that a material loan loss provision was required, and that all interests and fees associated with these loans should have been reversed, and the loans placed on a non-accrual basis, prevails.

[1299] D-1312, p.458
[1300] D-1312, p. 453
[1301] D-1312, p.448

TWTC

Positions in a nutshell

Plaintiff

[1223] Plaintiff submits that because Castor's loans added no value to these projects, which were already seriously over-leveraged, Castor would have had no effective way of protecting its position other than to take over the prior ranking debt. Castor did not intend nor did it have the ability to do that.

[1224] Plaintiff says that, in each case, Castor was sitting in subordinate positions to project lenders and co-developers, with no direct security on the real estate, and was unable to control its own destiny.

[1225] Even though the circumstances revealed by the evidence lead Plaintiff's expert Vance not to recommend a LLP in his 2008 report, Plaintiff submits it is clear that there was no available surplus to Castor.

[1226] Moreover, Plaintiff asserts that all of the TWTC loans should have been placed on a non-accrual basis for 1988 and that all revenue and fees capitalized to the loans ($4.4 million) should have been reversed over in accordance with GAAP.

Defendants

[1227] Defendants argue no LLP was required in 1988 in relation to TWTC. Rather, a surplus in the amount of $26.6 million was available to Castor to apply to other YH positions.

Additional evidence

Loans as of December 31, 1988 and security

[1228] As of December 31, 1988, Castor's exposure for loans relating to the TWTC amounted to 47.7 million:

- Loan 1046 to TWDC: $18.2 million
- Loan 1067 to YHDL.: $ 15.5 million
- Loan 1120 or 1149 to TWTCI : $10 million
- Loan 1090 to YHDL: $3.3 million
- Investment in TWTCP : $ 0.6 million

[1229] As of December 31, 1988, the security that Castor held for its loans was essentially a pledge of equity interests (as opposed to a mortgage on a property) [1302]which, altogether, represented a 36.24% interest in the TWTC equity[1303].

Loan 1046

[1230] Loan 1046 to TWDC was initially made in December 1984, for $4.5 million, at the interest rate of prime plus 6%[1304]. There was no credit assessment made before the loan was granted[1305].

[1231] The loan was for one year and the principal and accrued interests were both due and payable on December 14, 1985. As one covenant, TWDC was to provide annual financial statements to CHL within 120 days of its fiscal year end[1306].

[1232] In September 1985, the loan was increased with a one year term to September 30, 1986. The interest terms were changed in that an "Interest Reserve" was created.[1307] As long as there was credit available, the monthly interest charges were to be paid by using the Interest Reserve and increasing the loan. Again, TWDC undertook to provide annual financial statements to CHL within 120 days of its fiscal year end[1308].

[1233] The loan increased to $12.5 million[1309]. Part of the increase of the loan was to pay a syndication fee to CHIF which was trying to syndicate part of the project to European investors.[1310]

[1234] At the end of December 1986, the loan was again increased to $15 million[1311].

[1235] Castor's collateral security for Loan 1046 was a pledge of the shares of TWTCI owned by TWDC and ranking in second position behind a pledge to Bimcor[1312].

[1236] No payments were ever received on Loan 1046, interest was continually capitalized and the loan was extended for one more year on each annual maturity date[1313].

[1302] Goodman, September 23, 2009, pp.179-180
[1303] Goodman, September 23, 2009, p. 180
[1304] Ron Smith, September 16, 2008, pp.96 and following; PW-1067-1
[1305] Ron Smith, September 16, 2008, p.98
[1306] PW-1067-1
[1307] PW-1067-3 (section "purpose" item 4)
[1308] PW-1067-3, page 5
[1309] PW-1067-3
[1310] Ron Smith, September 16, 2008, pp. 99-100; PW-1067-3 (section "purpose", item 2 at page 1 of the Loan summary)
[1311] PW-1067-5
[1312] PW-1067-1 (section "Security" at pages 1 and 2 of the Loan summary)
[1313] Ron Smith, September 16, 2008, pp. 100 and following; see also PW-167 (loan 1046); PW-1067-7 and PW-1067-10

Loan 1067

[1237] Loan 1067 to YHDL was initially advanced in December 1985, as part of the 1985 year-end transactions (account 046), with a one year term requiring interest, at the rate of prime plus 6%, to be paid on a monthly basis[1314]. Within 120 days of its fiscal year end, YHDL undertook to provide annual financial statements to CHL[1315]. No credit assessment was ever done by Castor[1316].

[1238] Loan 1067 was at the $8 million level in 1986 and increased to $15.5 million by December 31, 1987[1317].

[1239] Loan 1067 was renewed and extended on or before each annual maturity date throughout the period the loan was outstanding and no payments of principal or interest were ever received by CHL[1318].

[1240] The collateral was a pledge of the shares of TWTCI owned by YHDL[1319].

Loan 1090

[1241] Loan 1090 was initially advanced in December 1987 in the amount of $3,300,000[1320], at the interest rate of prime plus 6%, and was part of the 1987 year-end cash circle transaction whereby the proceeds were then returned to CHL as repayments of other YHDL indebtedness[1321]. No credit assessment of the debtor of the loan was ever done by Castor[1322].

[1242] As Ron Smith said "*there were only so many projects available at that point in time and we were starting to run out of the projects to attach ourselves to*"[1323].

[1243] Loan 1090 was secured by two options[1324]: one option to acquire 50% of the 12.5% of the TWTC project from 752608 Ontario Limited, and one option to acquire 76% of the outstanding units in the Skyline Triumph Limited Partnership. In order to exercise the first option - to acquire 50% of the 12.5% of the TWTC project from 752608 Ontario Limited- a further payment of $5,971,250 plus interest from December 1, 1987 would be required[1325]. Similarly, the option to acquire the units in the Skyline Triumph Limited Partnership required a further payment.

[1314] PW-1066-B; PW-1068-1; Ron Smith, September 16, 2008, pp. 108 and following
[1315] PW-1068-1 (page 3)
[1316] Ron Smith, September 16, 2008, p. 110
[1317] PW-1068-3, PW-1068-5 and PW-1068-7
[1318] PW-1068 (series)
[1319] PW-1068-1 (page 2)
[1320] PW-1061-1; PW-1066B
[1321] PW-1056A-1
[1322] Ron Smith, September 16, 2008, p.116
[1323] Ron Smith, September 16, 2008, p. 112
[1324] Ron Smith, September 16, 2008, pp.114 and following
[1325] PW-1061-3 and PW-1061-4

[1244] In 1988, to further reallocate year-end indebtedness, Castor made Loan 1120 to TWTCI.

Loan 1120

[1245] Loan 1120 to TWTCI was created in December 1988[1326], as part of the 1988 year-end cash circle transaction[1327], with a term to December 15, 1992. Interest was to be payable monthly commencing with January 1, 1989. TWTCI undertook to provide annual financial statements within 120 days of its fiscal year end to CHL.

[1246] Castor agreed at that point in time to provide up to 15 million dollars financing to TWTCI, 9 million of which would be a reallocation of the YH year-end (account 046), and 6 million of which would be a portion to assist YH for any ownership cost[1328].

[1247] One of the first costs covered was the repayment of the Bimcor/Northern Telecom loan in an amount slightly over a million dollars: the disbursement took place by the end of 1988[1329]. YH did not have the money and they asked Castor to fund the reimbursement[1330].

[1248] Throughout the period the loan was outstanding, no payments of interest were ever received by CHL.

[1249] As part of the loan to TWTCI, Castor was to obtain a legal opinion to the effect that the security had been duly executed and constituted a first charge on the borrowers' pledged assets[1331]. Castor attempted unsuccessfully to register its security interest in TWTCI against the TWTC property: the co-ownership agreements between YHDL and Camrost required that Camrost approve any such registration, but no such approval was ever obtained[1332].

Prior to 1988

[1250] YHDL's partner in TWTC, Camrost, was primarily a residential developer, although they did have some commercial projects[1333].

[1251] It had been agreed between partners in the project that any proceeds from the sale of the condominium towers would be used as equity for the development of the office sites[1334].

[1326] Ron Smith, May 14, 2008, pp.159-160; PW-1069-1
[1327] Vance, April 16, 2008, p.71-72
[1328] Ron Smith, September 16, 2008, p.106, 122 and following, p.128 ; PW-1069-1 (section "purpose")
[1329] Ron Smith, September 16. 2008, p.126
[1330] Ron Smith, September 16, 2008, p.129
[1331] PW-1069-1 (item 4, page 3)
[1332] Ron Smith, September 16, 2008, p. 130-131; Goodman, November 23, 2009, p.202
[1333] Ron Smith, September 16, 2008, p. 94; Goodman, September 23, 2009, p. 156

[1252] As per the partnership agreement, Camrost had the right to buy out YH at 85% of the project total value in the case of a default by YH [1335].

[1253] York-Hannover had planned to syndicate off its position to investors through TWDC[1336].Then, rather than syndicate in TWDC, they decided they would syndicate their positions from TWTCI, and they did succeed in syndicating part of their position (to 696604 Ontario Ltd.- Peter Luerssen, Elfh – Stolzenberg) [1337].

[1254] As early as June 1987, York-Hannover was already in default to its co-owner Camrost.[1338]

1988 events

[1255] TWTC was YHDL's largest planned development project[1339]. TWTC was an important and ambitious project in downtown Toronto, well situated[1340].

[1256] The building permits were submitted in December 1987 and the TWTC condominium project went into "development mode" on January 18, 1988. The condominium lands were acquired outright from The Toronto Harbour Commissioners on May 24, 1988 and construction began shortly thereafter. [1341]

[1257] By June 1988, 90% of the 699 units had been pre-sold[1342].

[1258] The planned costs of construction were over $600,000,000[1343]. The approved budget for the construction of the two condominium towers was $193 million[1344]. The projected costs for the construction of the office towers were $422 million[1345].

[1259] Construction of the two condominium towers commenced in September 1988[1346].

[1260] At September 30, 1988, the financial statements of the office and commercial project indicated a bank indebtedness of $6,144,843 while the condominium project

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[1334] Ron Smith, September 16, 2008, p.142-143; Ron Smith, September 24, 2008, p.52; Goodman, November 23, 2009, pp.213 -214
[1335] Goodman, November 23, 2009, p.203-204; PW-1161-9
[1336] Ron Smith, September 16, 2008, p. 91
[1337] Ron Smith, September 16, 2008, pp. 91-92
[1338] PW-1161-7.
[1339] Goodman, September 23, 2009, p.155
[1340] Ron Smith, September 24, 2008, p.49
[1341] PW-1069-18
[1342] PW-1069-1
[1343] PW-1161-20 cover page and p. 1 ; PW-1069-18 bates p. 62
[1344] PW-1161-20; Goodman, September 23, 2009, p. 158
[1345] PW-1069-18; Goodman, September 23, 2009, p.159
[1346] PW-1069-20, bates p. 3 and Goodman, September 23,2009 p. 162-163

financial statements indicated a bank loan of $1,300,000 outstanding at October 31, 1988 for total prior ranking debt of $7,444,843[1347].

[1261] By December 1988, 94% of the units had been pre-sold and the projected sell-out value was $2.0 million higher than the approved budget.[1348]

[1262] As at December 31, 1988 the construction of the office and commercial project had not even started.

[1263] The first renewal of loan 1046, in 1985[1349], had provided for an interest reserve of $1,878,000. By 1988, that interest reserve had been totally utilized and the borrower was contractually obliged «*to put on deposit with the lender sufficient funds to cover all remaining anticipated monthly interest and extension fee payments through to the maturity date of the loan.*»[1350]

[1264] Ron Smith provided C&L with a chart concerning the current legal ownership structure of the TWTC as of November 1988[1351].

[1265] Castor's position on TWTC was a backend position, said Ron Smith :[1352]

> «Well, we weren't at that position, we were funding the co-ownership equity position at the back end. There were lenders directly on the projects that were providing acquisition financing for the sites, they were providing development financing for the various condo projects, and they had direct mortgages on those properties, so they had provided the funding for that to the joint venture. So we weren't even at that level, we were way behind that level and we were just relying on the co-ownership interest to collateralize our position.»

[1266] The risk of not realizing anything from the collateral was far greater with an equity position as security for the loans, added Ron Smith:[1353]

> «Oh, mathematically, you can take percentages and go against general valuations, but until you actually realize on your positions and actually sell the project, sell the condominiums, pay off all the parties going down, you really don't know what you're going to get. It's ... probably the best position you're going to get is on paper which is a projection, but when you come down to the final position, there's a lot of things that are going to crop up that you're not aware of at the front end. So it's very difficult to say you're going to get that amount of money.»

[1347] PW-1069-21
[1348] PW-1069-20
[1349] PW-1067-3.
[1350] PW-1067-10, page.2; PW-1067-12, page 3; PW-1067-15, page 2.
[1351] Ron Smith, September 16, 2008, p. 180
[1352] R. Smith, September 16, 2008, p. 154.
[1353] R. Smith, September 16, 2008, pp. 151-153.

Appraisals

[1267] As of February 12, 1987, Stewart, Young & Mason appraised a 50% part in the TWTC project between $62.6 and $104 million[1354]. No C&L audit staff member ever questioned Ron Smith regarding the assumptions in this Stewart, Young & Mason appraisal, the only appraisal Castor had for the audit[1355].

[1268] In their AWPs, C&L referred to a Stewart Young & Mason appraisal which would establish a value between $182 million and $285 million.[1356] The evidence in the record is that such appraisal does not exist.

[1269] The evidence shows that in June 1988, Royal LePage prepared a valuation of TWTCI's 50% undivided interest in the estimated equity distributions from the TWTC condominium project. This was before construction started, but well after the sales program had already demonstrated a significant level of pre-sales. Royal LePage estimated that the equity of a 50% interest had a value of $38.4 million (i.e. $76.8 million for a 100% interest)[1357]. This amount included a value for the retail centre within the condominium towers amounting to approximately $5.9 million[1358].

Loan covenants

[1270] In the commitment letters, YHDL covenanted to provide interim and annual financial statements.[1359] Notwithstanding such covenants, YHDL never provided financial statements during the relevant years nor did it meet its interest obligations. All interest was merely capitalized to account 046/Loan 1153.[1360]

Experts' opinions

[1271] Plaintiff's three experts each dealt with Castor's loans to TWTC differently.

- Vance had originally opined that a loan loss provision was required for the TWTC project, in his 1997 report, but in his 2008 report, he did not recommend any loan loss provision because of the uncertainty regarding the value of the TWTC land sites and whether this would flow to Castor.[1361]
- Rosen recommended a $25 million LLP.
- Froese did not provide any opinion regarding the TWTC project.

[1354] PW-1069-17
[1355] Ron Smith, September 16, 2008, p.163-166, 172-173, p.178-179
[1356] PW-1053-23, seq. p. 201.
[1357] PW-1069-18A; PW-1161-21; PW-1161-11; PW-1161-6; PW-1161-12
[1358] PW-1069-18A
[1359] PW-1068-1.
[1360] PW-1056F.
[1361] PW-2908, Vol. 2, D-14, D-15.

Vance

[1272] In his 1997 report, Vance concluded that a $43 million LLP was required[1362]. In testimony at the first trial he produced new calculations using a different methodology and retained a $28 million LLP (the low end of his calculations of LLP)[1363]. In the current trial, Vance did not recommend a LLP.

[1273] Vance computed a number of possible loss scenarios[1364] but declined to recommend any loan loss provision due to uncertainty.

[1274] The evidence leading to Vance's change of opinion was an appraisal[1365] which "*would appear on the face of it to provide value for the loan*"[1366].

[1275] Vance explained that the Coldwell Banker appraisal (the appraisal that made him change his opinion) raised some questions because it only appraised two of the three sites for the office towers, a situation which he found odd. Nevertheless, applying the same value to the third site (assuming that value could be realized), there was enough doubt in his mind for him not to recommend a LLP.[1367]

[1276] Vance admitted that the changes to his opinion were material[1368].

[1277] Vance characterized Castor's security as "poor", the reason being that although it could become owner of the shares and partnership units, Castor could not force the sale of the project[1369].

[1278] Vance opined:

> "Offers in the real estate industry are often very speculative and contain a number of conditions that can render the amount somewhat meaningless".
>
> "A listing is even more uncertain than an offer as an indicator of value".[1370]

[1279] As opposed to Goodman, who opined on that topic as follows:

> Whether the offers and listings referred to by Vance were speculative and uncertain or not, they were indicative of judgments taken by individuals who were closest to the TWTC real estate project at the time and, in the absence of completed transactions, were useful sources of information on the facts,

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[1362] Vance, April 18, 2008, p.163
[1363] Vance, April 18, 2008, p.165
[1364] PW-2908
[1365] PW-1161-24; Vance, April 16, 2008, p. 200
[1366] Vance, March 4, 2008, pp. 40-41
[1367] Vance, April 15, 2008, pp.45 and followings; Vance, April 18, 2008, pp.167-168
[1368] Vance April 18, 2008 p. 163-168 and 177, PW-1467-1
[1369] PW-2908, volume II, page D-2
[1370] PW-2908, Volume II, p. D-9

circumstances and evidence that had to be used for the preparation of timely and reliable loan valuation estimates in accordance with GAAP.[1371]

Rosen

[1280] The only one of Plaintiff's experts to opine on the required loan loss provision for TWTC was Rosen. His minimum loan loss provision for 1988 was $25 million.[1372]

Goodman

[1281] Goodman opined that not only no loan loss provision was required for the TWTC loans but, rather, there was a substantial surplus of $26.6 million that Castor was entitled to utilize to offset against other loan deficiencies elsewhere in the YH portfolio[1373].

[1282] Goodman used a combined total value of $226.5 million, all derived from a Royal LePage analysis[1374]:

- For the condominium component of the project, and as the condominiums were almost all pre-sold, Goodman used the estimated cash profit, i.e. $47 million net of costs to complete[1375].

- For the office towers component of the project, a development project[1376], Goodman valued the retail component at $5.9 million[1377] and the office component at $173.6 million[1378].

[1283] Contrary to Vance, Goodman felt there were plenty of value indicators with respect to the land sites[1379].

[1284] Goodman applied the percentage of interests over which Castor had direct and indirect interests (36.24%) to the value of the collateral[1380].

[1285] Goodman calculated that Castor's exposure was $47.9 million including the loan balances of loan 1046 ($18.2), loan 1067 ($15.5), loan 1090 ($3.3), loan 1149 ($10.0), the investment in TWTCLP units ($0.6 million) and the accrued interests ($0.3 million).

[1371] D-1312, pp.220-221
[1372] PW-3033, Vol. 2, Appendix E, p. 3; PW-3033-1.
[1373] D-1329; Goodman, September 23, 2009, pp.175 and following
[1374] Goodman, September 23, 2009, p.187-188
[1375] D-1312, TWTC-3 and PW-1069-18, bates 16; Goodman, September 24, 2009, p. 27-28
[1376] Goodman, September 23, 2009, pp.155-156;
[1377] PW-1069-18A
[1378] D-1330 and PW-1161-24; Goodman, September 24. 2009, pp.30 and following
[1379] Goodman, September 23, 2009, p.184
[1380] Goodman, September 24, 2009, p.37

[1286] Goodman explained[1381] he had no problem with the fact that Castor was unable to force a sale of the project because that was not Castor's strategy or intent. What was very important was that Castor could become an owner of the shares and partnership units, because that is where the value was.

[1287] Goodman's security enforcement plan for Castor was as follows:

- In the event of YHDL's default for non-payment of principal or interest, Castor would realize the value of its TWTCI security by enforcing its security on those TWTC loans that would provide Castor with the shares of TWTCI and Proko Options Inc.
- Castor would have been able to work with Camrost, a 50% owner of the TWTC, to complete the condominium project and to develop one office tower on site 1, even though the joint venture agreements with Camrost required that YHDL be the joint venture partner.
- Camrost and Castor would have chosen not to build on the other office tower land (sites 2a and 2b) until a buyer could be found or lead tenants signed up.

[1288] The difference between Rosen's minimum LLP of $25 million and Goodman's surplus of $26.6 million is attributable to disagreements on the value of TWTCI's equity that was held as security or directly owned by Castor.

Interests recognized as revenue

[1289] In 1988, Castor recognized 4,447,053 in interests and fees on loans 1046 and 1067:

- Interests on Loan 1046: $1,778,934
- Fees on loan 1046: $ 558,420
- Interests on loan 1067: $2,109,699

Conclusions

[1290] Castor's security was totally dependent on the potential sale price of the TWTC project and the timing of any sale, after completion.

[1291] If preponderance of evidence leads to not recognising a LLP, it does not mean, as Goodman would have the Court conclude, that there was an available surplus to offset other YH liabilities.

[1381] Goodman, September 23, 2009, pp.178-181

[1292] Goodman's opinion as to the alleged value of the TWTC and the supposed surplus that would be available to Castor does not stand up to scrutiny.

- Goodman ascribes to the TWTC a value of $226.5 million in 1988, $261.8 million in 1989 and $277.2 million in 1990. In fact, Goodman concludes that the fair market value of the TWTC office land sites purchased for $12.6 million was $187.3 million in 1990.[1382] This value is totally inconsistent with the marketing results of Coldwell Banker when it exposed the property to the market, discussed later in the present judgment.

- Goodman further relies on a Stewart, Young & Mason appraisal, as a value indicator, which neither Smith nor Whiting saw and which was never provided to C&L. While having chosen to refer to an unseen Stewart, Young & Mason appraisal, Goodman admitted that he did not consider nor include in his Report:

    - reference to PW-1069-17 which indicated a lower value;[1383]

    - the fact that the 7.51% interest in the TWTC project held by 696044 was acquired from Peter Luerssen for an implied total project value of $94 million; or,

    - the testimony of Whiting that the market value for the entire TWTC project in 1990 was $150 million.[1384]

[1293] On the preponderance of evidence, the Court concludes there was no surplus available.

Meadowlark

Positions in a nutshell

Plaintiff

[1294] Plaintiff says Castor's loans related to Meadowlark were in jeopardy virtually from the beginning of this financing (in the early 80s) because of the inability to compete with the West Edmonton Mall ("**WEM**") located about a mile away. As financing to carry out planned renovations could not be raised, the project's losses continued to increase.

[1295] Plaintiff adds that by the end of 1988, Castor had determined that Meadowlark could not successfully emerge from the shadow of the WEM. The decision was made for both Castor and YH to try to sell the property and to recover the investment.[1385]

[1382] D-1312, p. 209.
[1383] Goodman, November 23, 2009, pp. 196-197.
[1384] Whiting, February 14, 2000, pp. 103-111.
[1385] R. Smith, September 16, 2008, pp. 34–36.

[1296] Plaintiff argues that the various letters of intent and offers for Meadowlark, received in the years 1988 to 1990, fell far short of the amount that would have been necessary for Castor to recover its loan.[1386] For example, an evaluation of what Castor would have received if Meadowlark had been sold for $17.5 million, once the first mortgage was repaid and arrears and commissions were paid, amounts to almost nothing.[1387]

[1297] Plaintiff submits that not surprisingly Goodman relies on the second 1988 Shaske appraisal to arrive at his "*best estimate of market value*" of $27 million without considering that the assumptions therein or other factual evidence demonstrate that this value was totally optimistic and utterly unsupportable. Plaintiff argues the evidence is clear that the proposed renovations that were assumed in this appraisal ($5 million) were not going to be done and that the occupancy assumptions were totally unrealistic and were not being met. It is evident that if the first mortgage loan was in jeopardy at that time, there was no reasonable assurance of collectability for the Castor loans which ranked below.

[1298] Plaintiff concludes that the value indicators that Goodman relied on are unrealistic, speculative and do not represent GAAP values or even attempt to reflect commercial reality.

Defendants

[1299] Defendants plead that none of Plaintiff's experts testified in chief with respect to Castor's loans in connection with the Meadowlark project and that, as a result, Goodman's conclusion that there was a surplus of $4.6 million is the only valid opinion on this project before the Court.

[1300] Defendants add that Goodman used market values and computed a security surplus of $4.6 million, in accordance with his 5-step methodology, supported by a letter of opinion and two earlier appraisals.

Evidence

[1301] The YH Group held 100% of Meadowlark[1388] : 50% of that interest was held in YHDL; the other 50% was held in Raulino, part of Wersebe's European Group[1389].

[1386] PW-1112-14.
[1387] PW-1112-17.
[1388] D-1238, PW-1112-18, PW-1112F and PW-3033, vol 2. Tab F, p.4
[1389] PW-1112F

Loans as of December 31, 1988

[1302] As of December 31, 1988, Castor's exposure to loans relating to the Meadowlark shopping center amounted to $7.7 million:

- Loan 1030, a 2nd mortgage loan to Leeds Development (1981) Ltd.– $7 million.
- Loan 1117, a loan advanced in 1988 to Leeds Development (1981) Ltd. to cover operating expenses - $0.6 million.
- Accrued interests – $ 0.1 million.

[1303] Castor's loans were subordinated to the $16.1 million first mortgage loan held by the Bank of Montreal[1390]. Castor's loans to Leeds Development (1981) Ltd. were also secured by a guarantee provided by YHDL.

Interests recognized as revenue

[1304] During 1988, $0.9 million was recognized as revenue by Castor on loans relating to the Meadowlark shopping center[1391].

Prior to 1988

[1305] At that time, the WEM was the largest shopping center in the world. Before the WEM was built, Meadowlark was a successful shopping center. However, after the WEM opened, approximately a mile away, Meadowlark suffered, and so did about every other retail centre in Edmonton[1392].

[1306] From 1983 onwards, the property was struggling. Sears, the anchor tenant moved out[1393] and had to be replaced.

[1307] The TD Bank was paid off and Castor increased its loan exposure on the property up to approximately $22 million and took over all of the financing on the property[1394].

[1390] PW-1112A
[1391] PW-1112-G
[1392] Ron Smith, September 16, 2008, p.30
[1393] Ron Smith, September 16, 2008, p.31; Ron Smith, September 24, 2008, pp.78 and following
[1394] Ron Smith, September 16, 2008, p.31

[1308] By 1986, the Bank of Montreal chipped in and put a $15 million first mortgage on the property and Castor subordinated its position to end up with a $7 million exposure[1395].

[1309] There was no credit analysis performed by Castor in respect of the credit worthiness of the borrowers Leeds Development (1981) Ltd. and Raulino Canada Ltd. All Castor relied on was their interest in the property[1396].

1988 Events

[1310] Prior to the 1988 year-end, due to unpaid municipal taxes, Meadowlark was notified that it was in default of one of the major terms of the BMO mortgage. At that time, YH did not have the resources to pay the outstanding taxes on the property without financing from Castor, and it was looking for a new $5 million loan from BMO to carry out the merchandising and renovation program that the property required.[1397]

[1311] Moreover, the BMO was concerned about the impact on the value of the asset due to the significant decrease in occupancy, and further noted that the promised upgrade program had not been carried out.[1398]

[1312] On October 3, 1988, BMO advised its borrower and Castor that taxes were in arrears and that the situation had to be corrected[1399].

[1313] By the end of 1988, the owners had made the decision to put the Meadowlark shopping center on a sale mode to try to recover their investment in the property[1400].

[1314] In January 1989, Castor was informed by YH that BMO had transferred the first mortgage loan to its work out group. According to the assessment of YH, Meadowlark was «*in extreme danger of complete disaster*».[1401]

[1315] Efforts were made to try to recover $22 million from a sale of the property, but that never materialized[1402].

Appraisals

[1395] Ron Smith, September 16, 2008, pp.32-33, 53
[1396] Ron Smith, September 16, 2008, p.50
[1397] PW-1112-8A.; Ron Smith, September 16, 2008, p. 34
[1398] PW-1112-9.
[1399] Ron Smith, September 16, 2008, pp.58-59
[1400] Ron Smith, September 16, 2008, pp.34-35, 54-55
[1401] PW-1112-10; Ron Smith, September 16, 2008, pp.63-66
[1402] Ron Smith, September 16, 2008, pp.36 and following

[1316] On April 11, 1984, an appraisal indicated a value of $28.9 million[1403].

[1317] There was an appraisal prepared by Edward J. Shaske & Associates Ltd. dated July 2, 1986 for $20.5 million.[1404]

[1318] In 1988, two appraisal reports on the property were provided by Edward J. Shaske & Associates Ltd.

- The first appraisal dated March 14, 1988 provided an estimate of value of $21.0 million and indicated: "*At the present time, the shopping centre is affected by unoccupied bays, monthly tenancies, and uncertainty of continued operations by the owners*".[1405] Instructions to the appraiser had been provided by BMO.

- The later appraisal dated July 18, 1988 provided an estimate of value of $27 million but indicated: «*As the feasibility of continued operations is not our area of expertise, we have relied solely on the recommendations of the studies and have assumed that a complete "face-lift" or "retrofit" of the mall and site will occur in the immediate future ... A progressive marketing and merchandising strategy is not only a must – but a necessity.* ». For this second appraisal, instructions had been provided by YHDL and assumed the following : «*the "retrofit" is completed and full occupancy occurs over the course of a two-year time frame.* »[1406]

Experts' evidence

[1319] Froese was aware that YHDL had an interest in Meadowlark and that Castor had a loan in connection with it, but he did not do any work on the collateral available for that loan[1407].

[1320] Rosen included a section on Meadowlark in his report and recommended a minimum loan loss provision of $7.0 million: Rosen assumed that Meadowlark was not worth more than the balances outstanding on the Bank of Montreal first mortgage and other priority ranking creditors[1408]. Rosen said there was a difference between the total loan exposure to the property and what a decent appraisal would reveal as the value[1409].

[1403] PW-1112H
[1404] PW-1112I
[1405] PW-1112J-1.
[1406] PW-1112J, bates pp. 15-16.
[1407] Froese, December 4, 2008, pp.155-156; January 8, 2009, pp.203-207
[1408] PW-3033, vol.2, Tab F
[1409] Rosen, March 26, 2009, p.200-201

[1321] Goodman admitted that Meadowlark was "*a shopping centre that was not performing particularly well*"[1410] but, nevertheless, he [1411] concluded that there was a surplus of value available to Castor of $4.6 million[1412]. He characterized Rosen's approach as a distressed value approach.[1413]

[1322] Goodman concluded to such a surplus on the basis of an appraisal of $27 million which was taking into account major retrofit of the centre and full occupancy over the course of a two year time frame and he did not deduct the costs of those renovations[1414].

[1323] Goodman's security enforcement plan was the following: Castor would probably have realized the value of its Meadowlark security by enforcing its security in respect of loan 1030 and by becoming the sole owner of Meadowlark. Thereafter, and provided Castor would have determined that it would not be worthwhile to renovate the centre given the competitive threat of the WEM, Castor would have sold the shopping centre to the highest bidder in the normal course of business, without the distressed restructuring circumstances facing YHDL. Throughout this process, Castor would service the mortgage of BMO.

Conclusions

[1324] Defendants' proposition that the Court should conclude that there was a surplus of $4.6 million by the mere fact that Goodman was the only expert to have opined in direct examination on the topic is ill-founded.

[1325] As it is the case for any witness, including expert witnesses, the Court must assess the credibility and the reliability of testimonies[1415].

[1326] Goodman's opinion that there would have been a surplus lies on shaky ground and does not hold water: it is neither credible nor reliable. In the circumstances described above, computing from a property value of $27 million is totally unreasonable.

[1327] At best, the property value could have been enough to reimburse BMO and Castor but no one could have reasonably expected a surplus. In fact, Rosen might even have been right when he opined that a LLP was required in 1988.

[1410] Goodman, November 30, 2009, p.202
[1411] Goodman, September 24, 2009, pp.81-111
[1412] D-1312, pp.251-265; Goodman, September 24, 2009, p.82
[1413] Goodman, September 24, 2009, pp.88-97
[1414] Goodman, November 30, 2009, p.204
[1415] Royer, Jean-Claude, *La preuve civile*, 4 éd. Cowansville, (Qc), Yvon Blais, 2008, at §120, 484; *Shawinigan Engineering Co. c. Naud*, [1929] R.C.S. 341 at 343; *Lapointe c. Hôpital Le Gardeur*, [1992] 1 R.C.S. 351 at 358; AZ-92111029; J.E. 92-302. *Droit de la famille – 103252*, [2010] QCCA 2173; AZ-50695343; *P.L. c. Benchetrit* [2010] QCCA 1505, para.25 to 31; AZ-50666756; J.E. 2010-1600; *L.F. c. A.D.*, AZ-50342156 at paras. 76, 81, 83, J.E. 2006-9, [2006] R.D.F. 175 (rés.).

1989 financial statements

Some figures and notes content of the 1989 statements

[1328] According to its balance sheet, Castor had:

- $1,424,051 of investments in mortgages, secured debentures and advances, as more fully disclosed in notes 2, 3, 4 and 10;
- $100 000 of liabilities through debentures, as more fully disclosed in note 6.

[1329] According to the consolidated net earnings statement, Castor's revenues for 1989 were $197,711,000 as more fully disclosed in note 9, and Castor's net earnings for 1989 were $28,410,000.

[1330] According to note 10 on related party transactions:

- secured debentures and advances due from shareholders in the amount of $9,076,000 were included in investments in mortgages, secured debentures and advances; and
- transactions during the year, and amounts due to or from shareholders and directors, not otherwise disclosed separately in the financial statements, were as follows:
    - accrued interests and other payables : $1,047,000
    - interest revenue : $1,338,000
    - other expenses: $357,000

[1331] Notes 2, 3, 4, 6 and 9 read as follows:

> 2. Investments in mortgages, secured debentures and advances
> The investments in mortgages, secured debentures and advances are in various currencies and bear interest at varying rates from 7 1/2% to Canadian bank prime rate plus 6% per annum and mature as follows:
>
1990	1,055,702
1991	121,799
1992	84,253
1993	157,460
1994	4,416
1995	421
and subsequent years	
	1,424,051

3. Notes payable

(a) These notes are payable in various currencies and bear interest at varying rates from 6 ½% to 15 15/16% and mature as follows:

	TOTAL	1990	1991	1992	1994
Secured	238,477	220,977	17,500	-	-
Unsecured	406,996	328,838	7,000	60,158	11,000
	645,473	549,815	24,500	60,158	11,000

(b) Mortgages having an approximate book value of $236,587 have been pledged as security for the secured notes payable.

4. Bank Loans and advances

(a) Bank loans and advances consist of term loans and advances bearing interest at floating rates and varying fixed rates from 5 13/16% to 15 3/16% per annum.

(b) The term loans mature as follows:

TOTAL	1990	1991	1994
515,186	375,993	104,124	35,069

(c) Mortgages having an approximate book value of $189,980 have been pledged as security for the bank loans totalling $188,482.

6. Debentures

	1989	1988
(a) Debentures maturing on June 30, 1997 bearing interest at The Royal Bank of Canada prime rate plus 2 ¼% but not less than a minimum of 11% per annum. After June 30, 1992, the company has the right to prepay the principal amount. Interest on the debentures is payable semi-annually.	50,000	50,000
(b) Debentures maturing on June 30, 2002 bearing interest at The Royal Bank of Canada prime rate plus 2 3/8% but not less than a minimum of 11% per annum. After June 30, 1994, the company has the right to prepay the principal amount. Interest on the debentures is payable semi-annually.	50,000	50,000
	100,000	100,000

9. Revenue

Details of revenue are as follows:

	1989	1988
Interest and discounts	183,793	117,366
Commissions	13,579	14,689
Share of revenue from investments and joint ventures	339	355
	197,711	132,410

Materially misstated (1989)

[1332] The 1989 statements were materially misstated.

Absence of a SCFP showing the sources and uses of cash and cash equivalents

[1333] A SCFP was required: section 1540 and its italicized recommendations were clear.

[1334] The analysis developed and the conclusions enunciated in the 1988 financial statements section of the present judgment apply *mutatis mutandis*.

Undisclosed related party transactions

[1335] No doubt related party transactions were undisclosed in the 1989 financial statements. The analysis developed and the conclusions enunciated in the 1988 financial statements section of the present judgment apply *mutatis mutandis*.

[1336] Over and above the situations discussed in the 1988 section, two other transactions which took place in 1989 raise conclusive or potential undisclosed related party transactions: a loan made through Global management in trust for the benefit of 166505 Canada Inc., and the purchase of an airplane by Jet lease 900 and the charter agreement of such airplane with Castor.

166505 Canada Inc.

[1337] On May 26, 1989, CHIF, represented by Stolzenberg, instructed Global Management Ltd. ("**Global**"), represented by Bänziger, to make a loan on its behalf to 166505 Canada Inc. ("**166505**") in the amount of $8,691,375. [1416]

[1416] PW-2285

[1338] By a loan agreement dated May 26, 1989, Global, represented by Bänziger loaned to 166505, represented by Stolzenberg, $8,691,375. In their agreement, Global and 166505 stipulated that the interest was payable monthly and they stated that the purpose for the loan was as follows: "*for the purpose of the acquisition of a participation in Perkins Paper*"[1417].

[1339] Previously, Wightman had introduced Stolzenberg to Perkins Paper[1418], one of Wightman's audit clients - a situation discussed later under the subheading "*independence*". Stolzenberg invested in Perkins Paper, through 166505, and with Castor's money[1419].

[1340] Castor's records clearly disclosed that the proceeds of the $8,691,375 loan were disbursed to "Phillips and Vineberg in trust" for the benefit of 166505[1420].

[1341] At year-end the loan balance was $9,527,407, and all interest accrued on the loan during the year, in the amount of $836,032, was capitalized to the loan and recognized as revenue[1421].

[1342] In her working papers, Ford indicated that no loan file existed.[1422]

[1343] The loan was not disclosed as a related party transaction and it should have been[1423], a fact that Defendants' expert Selman acknowledged.[1424]

Jet lease 900

[1344] Jet lease 900 ("**Jet lease**") owned an aircraft which was purchased with a financing from Banque Paribas. Castor chartered the airplane. Wightman knew about these transactions: he was involved in structuring them.[1425]

[1345] In 1989, Castor made a $6 million deposit in connection with this charter agreement and set the amount as a prepaid expense in its books and records.

[1346] Vance opined that the Jet lease transactions were related party transactions because Stolzenberg was the beneficial owner of Jet Lease[1426], a fact that he derived

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[1417] PW-2285, bates 005317
[1418] Wightman, September 5, 1995 p.71
[1419] Wightman, September 5, 1995, pp.71-81
[1420] PW-696
[1421] PW-1053-89-4A, seq. p. 250
[1422] PW-1053-89, sequential p. 263.
[1423] Vance, March 12, 2008, pp.31 and following
[1424] Selman, May 14, 2009, pp.19-20; Selman, June 9, 2009, pp.245-247
[1425] Vance, June 4, 2008, pp.87-90
[1426] Vance, March 12, 2008; Vance, June 4, 2008, p.83

from a declaration of Gourdeau, the trustee, and from the content of the examination of Stolzenberg under section 163 of the Bankruptcy act[1427].

[1347] Assuming that Stolzenberg beneficially owned the shares of Jet Lease or significantly influenced Jet lease, and assuming that there would have been a residual value after the reimbursement of the loan to Banque Paribas, the transaction should have been disclosed as a related party transaction: Selman agreed[1428].

[1348] No conclusion can be drawn, however, since the declaration of Gourdeau is not evidence before this Court and since the examination of Stolzenberg under section 163 of the Bankruptcy Act is not part of the court record.

Artificial improvements of liquidity and undisclosed restricted cash

[1349] Castor's liquidity was artificially improved in the 1989 consolidated audited financial statements as a result of the following elements:

- the maturities used in notes 2, 3 and 4;
- the 100 million debenture transaction;
- the undisclosed restricted cash in the amount of £18.8M ($42 million).

Liquidity improvements (notes 2, 3 and 4)

Positions (in a nutshell)

Plaintiff

[1350] Plaintiff argues that :

- The Notes 2, 3 and 4 to the 1989 consolidated audited financial statements were materially misleading and disclosed a false picture of liquidity matching and solvency.
- The maturity notes conveyed to the reader that there was good maturity matching but in reality, it was the opposite. There was no reasonable expectation that the loans included as "current" would be, or could be, repaid during the current year.
- The maturity dates of various assets (loans receivable) and liabilities (loans payable) were altered during the audit; changes, unsupported by audit evidence, were accepted by C&L to the maturity dates. By advancing the due date of

[1427] Vance, June 4, 2008, pp.83 and following
[1428] Selman, May 14, 2009 p.21

various receivables before their actual due dates and by extending the due date of various liabilities beyond their actual due dates, Castor improved its apparent liquidity position.

Defendants

[1351] Defendants plead that:

- Plaintiffs' experts misread the notes to the financial statements.
    - Vance and Rosen have asserted that these notes were misleading because they were possibly incorrect with respect to the amounts shown as maturing in future years, and because they misled the reader into believing that Castor was going to receive as much as 70-80% of its revenue in cash within the next year, whereas in reality, Castor's assets were not that liquid.
    - Rosen described the mismatch as being between long-term lending and short-term borrowing.
- Plaintiffs' experts are attempting to read something into the financial statement notes that is not there, nor required to be there. Rosen and Vance confused the concepts of "maturity" and "liquidity".
- Plaintiffs failed to demonstrate that the disclosures as to contractual maturity dates made in the 1989 financial statements were not materially correct.

Maturity changes made in 1989

[1352] Changes were made to maturity dates. These changes were made by C&L during the audit work in the field or, at Castor's suggestion, after the audit work in the field was completed. Those changes concerned loans and notes payable totalling $145 million.[1429]

- CHL's bank loans originally inscribed as maturing in 1990 were reclassified to mature in 1991:
    - Société Générale (Canada) - $6.8 million[1430]
    - Banque Nationale de Paris ("**BNP**") - $2.4 million[1431]
    - BNP- $2.4 million[1432]

[1429] PW-2908, vol. 1 chapter 4, pages 4F-23 and following; Vance, March 12, 2008, pp.133 and following
[1430] PW-1053-18-3, BB100
[1431] PW-1053-18-3, BB101

- Crédit Commercial de France ("**CCF**") – $966,000[1433]
- CCF- $1.9 million[1434]
- CCF - $6.2 million[1435]
- CCF - $2.9 million[1436]
- Caisse Centrale Desjardins - $10 million[1437]
- Caisse Centrale Desjardins - $7.5 million[1438]
- Caisse Centrale Desjardins -$7 million[1439]

- CHIF's bank loans originally inscribed as maturing in 1990 were reclassified to mature in 1991:
  - DG Bank L.A. - US $10 million[1440]
  - DSL Bank, Boon – DEM 20 million[1441]
- Notes payable by CHIF, originally inscribed as maturing in 1990, were reclassified to mature in 1992 or in subsequent years:
  - Bristol Equity Holdings – $60.1 million[1442] – new maturity 1992
  - Tara - $4 million – new maturity 1994
  - Tara - $5 million – new maturity 1994
  - Tara - $ 2 million – new maturity 1994

Specific additional evidence

CHL bank loans

[1432] PW-1053-18-3, BB101
[1433] PW-1053-18-3, BB101
[1434] PW-1053-18-3, BB101
[1435] PW-1053-18-3, BB101
[1436] PW-1053-18-3, BB101
[1437] PW-1053-18-3, BB143
[1438] PW-1053-18-3, BB143
[1439] PW-1053-18-3, BB163A
[1440] PW-1053-90-5A, sequential page 96
[1441] PW-1053-90-5A, sequential pages 64 and 71
[1442] PW-1053-90-5A, sequential. p. 102

[1353] Castor maintained a ledger which captured information on each deposit or each loan drawdown: the identity of the lender, the term, the maturity date, the rate of interest and the amount of interest due on maturity[1443].

[1354] "B.A." and "P.N." inscriptions on Castor maturity listings stand for Bankers Acceptance and Promissory Note[1444].

[1355] Castor had to repay Bankers Acceptance and Promissory Notes at their respective maturity dates[1445] even though they had been issued within an evergreen credit facility. Credit facility maturities and Bankers Acceptance or Promissory Notes maturities were two different things[1446]. Credit facility could run for several years but their terms sometimes indicated that individual borrowings were limited to a specified term, such as 60, 90, 180 or 360 days.

[1356] Placement cards for all of these loans indicated a maturity date of 1990 and, for all of them, bank confirmations received by C&L showed a 1990 maturity date[1447].

[1357] When there was a Bankers Acceptance or a Promissory Note, the inscription relating to maturity on the placement cards was the Bankers Acceptance or the Promissory Note maturity. When there was neither a Bankers Acceptance nor a Promissory Note, the inscription relating to maturity on the placement card was the date of the next interest payment[1448].

[1358] Loans by Société Générale, BNP and CCF were Bankers Acceptance.

[1359] Loans by Caisse Centrale Desjardins were made through a Promissory Note.

[1360] During his field work at CHL's office, Joron noticed that a maturity date as shown on a placement card[1449] was not always the maturity date appearing in the applicable commitment letter, and he noted his observation in the AWPs[1450].

[1361] In various situations, faced with different maturity dates, but without any further steps taken, Joron relied on the maturity date of the credit facility appearing in the commitment letters and not on the information appearing on the placement cards and the confirmation letters.

[1443] Simon, April 23, 2009, p.144
[1444] Simon, April 28,2009, pp.220-221 ; PW-1053-18-3
[1445] Simon, April 28,2009, p.233
[1446] Simon, April 28, 2009, p.245
[1447] PW-1053-18, sequential pages 148-149 (BNP), 150 -154 (CCF), 168 (Société Générale), 187-188 (Caisse Centrale Desjardins)
[1448] Simon, April 28,2009, p.234
[1449] PW-167
[1450] PW-1053-18-3, BB-99A

[1362] The January 20, 1989 commitment letter of Société Générale[1451], and the October 25, 1989 commitment letter[1452] that superseded it, gave Castor possibilities to borrow under Bankers Acceptance through an operating line of credit or through the evergreen facility. The operating line was granted for a short period (May 31, 1989 and May 31, 1990) renewable at the bank's discretion and the evergreen facility was granted for a basic term of 2 years.

[1363] By a commitment letter dated October 6, 1989[1453], BNP granted a revolving credit of $5 million to Castor for a term of 2 years, renewable every year at BNP's sole discretion. This credit was available by way of Bankers Acceptance or by way of direct advances. In case of an event of default, Castor and BNP had stipulated that Castor's right to make further borrowings would immediately terminate.

[1364] By a commitment letter dated September 27, 1989, CCF provided two credit facilities to Castor: a 2 year revolving evergreen facility (facility A) and a demand operating facility (facility B)[1454].The facilities were available through draws in a minimum amount of $500,000 by way of direct advances or Bankers Acceptance limited to 90 days and subject to availability. Facility A was to be 100% secured and was subject to CCF's and its solicitors' approval of the guarantees to be provided, on a case by case basis.

[1365] On November 24, 1989, for the purpose of its own audit, CCF sent an audit confirmation request to Castor. This confirmation request listed the four Bankers' Acceptance as maturing in 1990 and Stolzenberg confirmed them as correct[1455].

[1366] By a commitment letter dated May 2, 1989, Caisse Centrale Desjardins extended to Castor a credit facility known as "Credit A" for a total amount of $13 million. $7.5 million of that facility were dedicated to MLV and $5.5 million remained undrawn at that date[1456]. It was agreed that Credit A would take the form of revolving loans for an initial period of 2 years – that Castor would retain the option to borrow, repay and re-borrow- and that such loans would be evidenced by either floating rate notes or term notes for periods of 7 to 365 days depending on the availability of funds and provided that the terms were within the credit period. The "*drawdown/repayment procedures*" paragraph included the following restriction to repayment: "*No prepayment will be accepted before maturity of a term note*". The clause "*events of default*" included the following: "*immediately and without notice if the Borrower fails to pay the principal amount of the loans when due and payable or to pay interest on the loans when due and payable*".

[1451] D-565
[1452] D-566-1
[1453] D-561
[1454] D-571
[1455] PW-2412
[1456] D-570

[1367] Castor also had evergreen credit facilities with Caisse Centrale Desjardins[1457] and transactions within such facilities were registered on a placement card, which was part of Castor's books and records[1458].

CHIF bank loans

[1368] These loans appeared on the CHIF maturity list[1459] which indicated a 1990 maturity date.

[1369] DG bank answered the request confirmation as follows: "*We have checked our records and do not show this item. Please recheck your records.*"[1460] No follow up was done.

[1370] DSL bank confirmed that the amount was due in 1990[1461]. CHIF's records, in addition to the confirmation from DSL, also consistently show that the amounts were loaned on a short-term basis and matured in 1990[1462].

[1371] The loans made under the revolving credit agreement signed with DSL were loans for a period of 360 days[1463]. Provided it was not in default, CHIF, upon the expiration of a loan, was allowed from time to time to choose to continue an outstanding loan by giving an irrevocable notice of continuation[1464]. Notwithstanding the maturity date of the credit facility, payment of principal for each outstanding loan was due and payable upon its expiration, unless CHIF had chosen to extend the loan and had given proper notice[1465].

[1372] Gross told C&L that all loans were of current nature, as noted by C&L in their AWPs[1466]. Gross testified accordingly[1467].

Notes payable

[1373] In a letter dated February 8, 1990, Bänziger asked for changes to maturity dates to notes payable.[1468] Aware of that request, Ford asked Bänziger, in writing, to provide

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[1457] D-567-1
[1458] Simon, April 28, 2009, p.245 ; PW-2485-1
[1459] PW-1053-90-5A
[1460] PW-1133A as bates #1784
[1461] PW-1133A as bates #1789
[1462] Gross, February 1-5, 1999, pp.779-785
[1463] D-333-1, article 2.1 A
[1464] D-333-1, article 2.1 C
[1465] D-333-1, article 2.4 A
[1466] PW-1053-90-6, CC-2
[1467] Gross, February 1-5, 1999, pp.779 to 788
[1468] PW-1053-72-15

her with further information[1469]. Ford's request went unanswered, but the changes were made nevertheless by C&L.

[1374] Confirmations had been sent to all lenders, including Bristol and Tara, indicating the original maturity dates. Bristol returned a signed confirmation, but Tara did not.

[1375] The Bristol note is shown as maturing in 1990 on the maturity listing[1470]. In its answer to the confirmation request, signed by Bänziger on its behalf, Bristol confirmed a 1990 maturity date[1471]. However, in his letter of February 8, 1990 requesting changes, Bänziger stated that the Bristol deposit was connected to a receivable from Marketchief maturing only in 1992 and that, consequently, it could not be called for earlier.

[1376] Tara was a name under which members of the White family interacted with Castor for investments.

[1377] On the maturity listing, the Tara notes were shown[1472] with a maturity date set out as 99.99.99, i.e. without a maturity date and due on demand. The maturity date appearing on the copy of the confirmation request was December 31, 1989, the fiscal year-end[1473].

[1378] All documentation in the Tara deposit folders, since the inception of the deposits, refers to "call deposits", deposits due on demand.

[1379] In his letter of February 8, 1990 requesting changes, Bänziger wrote that the Tara deposits were included under demand notes for technical reasons[1474].

[1380] Gross observed that the Tara notes that he was shown were not drawn in the usual Castor format.[1475]

[1381] In the AWPs, C&L wrote that all notes payable were of a current nature as per Gross, i.e. maturing in 1990[1476].

Experts' opinions – Maturity notes 2, 3 and 4

[1382] Vance indicated that the fiscal year-end as a maturity date would indicate a debt payable on demand, and that such was the case for the Tara notes.

[1469] PW-1053-72-16
[1470] PW-1053-90-5A
[1471] PW-1133A as bates # 1692
[1472] PW-1053-90-5A at seq. p. 124
[1473] PW-1053-73-1
[1474] PW-1053-72-15
[1475] Gross rogatory commission at pp.588-590
[1476] PW-1053-90-4, AA-50

[1383] Vance opined that all the above maturity date changes were wrongly made[1477] : no changes could be made without sufficient appropriate evidence, which evidence C&L did not have; dates, as confirmed by banks or other lenders through the confirmation process used by C&L, should not have been altered.

[1384] In the case of the Bristol deposit, Vance acknowledged there was obviously a mismatch in maturities. Without a proper legal opinion on hand, C&L could not assume that Castor had a right to offset. At maturity, Castor would have or could have required other security from the borrower.

[1385] Except for a $2,500,000 portion owed under the CCF demand facility[1478] and the $10 million loan from Caisse Centrale Desjardins[1479], Selman opined that there was a reasonable basis for changing the maturity dates made to loans owed by Castor and identified by Vance. In the case of the two exceptions, Selman opined that the maturity table, as revised with C&L's consent, was wrongly stated.

[1386] In evergreen facilities, Selman opined that the shorter term was only used to create an opportunity for banks to change the interest rate[1480] and that the facilities expiration dates could be used as maturity dates for the purposes of notes 2, 3 and 4. His analysis rests on the following articulated facts[1481]:

- Banks committed to facilities that would remain in place as long as Castor met covenants agreed to in the commitment letters.
- As long as Castor met its covenants, Banks could not otherwise justify a demand for repayment.
- Banks were bound to renew if Castor chose to renew.
- Obviously, Castor would renew if it was in its interest to do so.

[1387] Therefore, as long as the changes of maturity dates remained within the expiration of the facility, Selman opined it could be done – it was in accordance with GAAP.

[1388] In the Bristol case, Selman opined that the available agreements were not sufficiently unclear[1482] for C&L to require a legal opinion before accepting the right to offset.

[1477] PW-2908, vol. 1 chapter 4, pages 4F-23 and following; Vance, March 12, 2008, pp.133 and following
[1478] D-1295, p.306
[1479] Selman, May 21, 2009, pp.104-110
[1480] Selman, May 21, 2009, pp.83-85
[1481] Selman, May 21, 2009, pp.81-82
[1482] PW-2214-A and PW-2115

[1389] In the case of the Tara notes, unless the notes shown to Gross were not signed notes in the hands of the White[1483], Selman was not prepared to accept that their 1994 maturity dates were wrong.

Conclusions

[1390] There is no quarrel between experts that the due dates on the Bankers Acceptance and the Promissory Notes were shorter in term than the expiration dates of the credit facilities.

[1391] The due dates on the Bankers Acceptance and the Promissory Notes, confirmed as correct by financial institutions through the audit confirmation process, should not have been changed without further appropriate audit evidence. Castor had rights to renew Bankers Acceptance or Promissory Notes under its evergreen credit facilities but those rights were conditional to compliance with all covenants at renewal specific dates.

[1392] Given Castor's global situation, including the purposes and the content of notes 2, 3 and 4, Vance's opinions prevail. The analysis developed and the conclusions enunciated on this topic in the 1988 financial statements section of this judgment apply *mutatis mutandis*.

Liquidity improvements (100 million debentures)

[1393] In 1989, Revenue Canada audited Castor's $4 million payment to Gambazzi in the context of the issuance of the $100 million debentures. Relying on information from Wightman and Castor employees, Marcinski of C&L presented Castor's position, asserting the validity of the transaction[1484].

[1394] The analysis developed and the conclusions enunciated on this topic in the 1988 financial statements section of this judgment apply *mutatis mutandis*.

Undisclosed restricted cash

[1395] Castor had an unclassified balance sheet in its 1989 financial statements which included the heading "*Cash in bank and short-term deposits*".

[1396] GAAP required that «*cash subject to restrictions that prevent its use for current purposes*» be excluded from current assets.[1485]

[1483] D-327 and D-329
[1484] Marcinski, January. 10, 1996, pp.163-188
[1485] PW-1419-2, section 3000 "cash"

[1397] Without any note disclosure, a reader of the financial statements would assume that the amount shown under the heading "*Cash in bank and short-term deposits*" was available and usable for general purposes[1486]. It was not the case.

Positions (in a nutshell)

Plaintiff

[1398] Plaintiff argues £18.8M of restricted cash should have been disclosed.

[1399] Moreover, plaintiff adds that had it been discovered that Castor had signed an unenforceable pledge under Irish law, management's good faith would have been questioned.

Defendants

[1400] Defendants acknowledge that a pledge of a deposit ought to be disclosed if it is material under GAAP.

[1401] However, given the ruling of the Irish Court that the pledge was unenforceable, Defendants submit it should not have been disclosed as restricted cash.

[1402] Subsidiarily, Defendants argue that the restriction would not have been material to the financial statements audited by C&L, even if it had been enforceable, since it represented only about 3% of Castor's consolidated assets.

Evidence

[1403] In December 1989, Castor set up a loan with Credit Suisse Canada for £18.8 million (pounds sterling) to finance the incorporation of its subsidiary CHI[1487].The loan facility referred to its security as "*a payment obligation issued by Credit Suisse Zurich in favour of Credit Suisse Canada*"[1488].

[1404] Castor used the proceeds of the loan to pay for the CHI shares issued to it [1489] and such payment was deposited at Credit Suisse Zurich. A pledge of funds deposited at Credit Suisse Zurich was signed by Stolzenberg to secure the loan of Credit Suisse Canada.

[1486] PW-1419-2, section 3000; Vance, March 13, 2008, p.29.
[1487] PW-511
[1488] PW-511
[1489] PW-534

[1405] Credit Suisse Canada confirmed to C&L the term loan with a due date in 1994 and its security "*payment obligation from Credit Suisse Zurich*"[1490].

[1406] No confirmation was requested from Credit Suisse Zurich[1491] but the European AWPs of C&L included information on a guarantee (number 54-200) in the amount of £18.8 million in favour of Credit Suisse Canada Toronto and information on the charged fee for such guarantee, in the amount of £14.1 pounds sterling[1492].

[1407] The next year, for the 1990 audit, a bank confirmation[1493] was requested and received by C&L Ireland: the confirmation dated February 4, 1991 showed, on its last page, that the £18.8 million fiduciary deposit was fully pledged[1494].

[1408] According to Cunningham, an Irish partner of C&L who audited CHI, the pledge was illegal under the Irish Companies Act[1495].

[1409] On December 12, 1997[1496], the Irish High Court held that a pledge to secure a £18.8 million loan of CHL from Credit Suisse Canada[1497] existed since inception, but that such pledge was unenforceable under Irish law.

Experts' evidence

[1410] Vance opined that restricted cash in the amount of £18.8M ($42 million) was not disclosed[1498].

[1411] Asked what an auditor would have done had he been made aware of the unenforceability of the pledge because of its illegality under the Irish Companies Act, Vance answered that the auditor would have found that his client was engaging into illegal acts, and would have moved to the appropriate section of GAAP and GAAS to deal with such a situation.

> Again, that's going into the legal round. What an auditor would do in the normal course, a competent auditor would determine that the bank thinks it's pledged and then you would say "We're going to have to disclose it as pledged" and the client "Winkwink, notch-notch, we did it but we know under Irish law, it's unenforceable", now the auditors got a bigger problem because his client is

[1490] PW-1053-18-10, sequential page 33
[1491] Vance, June 6, 2008, p.15
[1492] PW-1053-72-19, sequential page 205; Vance June 6, 2008, pp.15 and following
[1493] PW-546
[1494] D-582
[1495] Cunningham, November 26, 1998, p.80
[1496] D-582
[1497] D-582, namely pp. 13, 19 - 20
[1498] PW-2908, Vol. 1, p. 4-F-56

> engaging in technically illegal acts, and we have sections in the handbook when you find your client entering into illegal act...[1499]

[1412] At the end of the day, Vance opined that under GAAP, the amount had to be disclosed as restricted cash, in the absence of a decision by a court of law that it was unenforceable[1500].

[1413] Selman opined that the cash related to Credit Suisse indebtedness for the 1989 audit may not actually have been restricted cash because of the unenforceability of the pledge under the Irish law[1501].

Conclusions

[1414] No evidence shows that Castor would have been aware of the unenforceability of the £18.8million pledge granted to Credit Suisse Zurich. The pledge was declared unenforceable in 1997, but until then it had been signed by Castor and it had been acted upon by Castor and its lenders.

[1415] Therefore £18.8millin should have been disclosed as restricted cash.

Undisclosed Capitalised interests and inappropriate revenue recognition

[1416] The analysis developed and the conclusions enunciated on this topic in the 1988 financial statements section of this judgment apply *mutatis mutandis*.

Understatement of LLP and overstatement of carrying value of Castor's loan portfolio and equity

[1417] In 1989, Castor represented a carrying value of loans (investments in mortgages, secured debentures and advances) of $1,424,051 in its audited financial statements: it represented that the figure of $1,424,051 was the lower of estimated realizable value and cost.

[1418] At December 31, 1989, could the carrying value of loans, at the lower of estimated realizable value and cost, be $1,424,051 or an amount close enough to $1,424,051 to avoid a material misstatement?

[1419] Taking account of the facts as they unfolded, viewed and analysed in the context of the relationship that existed between Castor and YH, the obvious conclusion is that the carrying value of loans could not be $1,424,051 or an amount close enough to $1,424,051 to avoid a material misstatement.

[1499] Vance, June 6, 2008, p.47
[1500] Vance, June 6, 2008, p.49-50
[1501] D-1295, p. 328

[1420] The task of assessing the exact quantum of any LLP that might have been required for 1989 is neither achievable nor necessary. This litigation is not about what the precise content Castor's financial statements for 1989 should have been – it is about whether or not C&L's 1989 audited financial statements of Castor presented fairly the financial position of Castor in accordance with GAAP, as they purported to do.

Positions in a nutshell

[1421] Plaintiff and Defendants positions, summed-up in the 1988 audited financial statements section of the present judgment, apply *mutatis mutandis*.

[1422] Plaintiff argues that a minimum LLP of $185.1 million[1502] should have been taken.

[1423] Defendants argue that there was no need for a LLP.

Experts' figures

[1424] All plaintiff's experts opine that LLP should have been taken in 1989, the lowest minimum LLP assessment being in the amount of $185.1 million as per calculations of Froese.

[1425] Vance proposes a total minimum LLP of 243.8 million, breaking down as follows:

Project/Category	Vance's proposed minimum LLP
MLV	60 million
YH Corporate loans	111.1 million
MEC	20.9 million
TSH	29.3 million
CHS	18 million
OSH	14.5 million

[1426] Rosen proposes LLP ranges between 321.9 million and 457.9 million, breaking down as follows[1503]:

[1502] PW-2941-4 - Minimum figure calculated by Froese

Project/Category	Approach A - Low	Approach A- High	Approach B- Low	Approach B- High
MLV	50 million	64.9 million	80 million	85 million
YH Corporate loans	113 million	157 million	113 million	157 million
MEC	45.8 million	53.1 million	45.8 million	53.1 million
TSH	24.9 million	28.9 million	44.9 million	48.9 million
CSH	12.2 million	22.8 million	22.2 million	32.8 million
TWTC	69 million	73 million	69 million	73 million
Meadowlark	7 million	8.1 million	7 million	8.1 million

[1427] Froese proposes LLP ranged between 185.1 and 230.9 million, breaking down as follows[1504]:

Project/Category	Low	High
MLV	52.2 million	52.2 million
YH Corporate loans	87.8 million	93.9 million
MEC	1.4 million	27.4 million
CHS	12.7 million	26.4 million
THS	31 million	31 million

[1428] Goodman opines that no LLPs were needed.

[1429] Goodman applied his 5 step methodology (previously described).

[1430] Again, the more serious dispute between Plaintiff's' experts and Goodman is with respect to the value used for step 1 and the proper application of step 5 under GAAP, given Castor's reality and the realities of Castor's borrowers.

[1503] PW-3033, volume 2
[1504] PW-2941-4; PW-2941, volume 1, p. 25

Analysis and Conclusions

[1431] The loans looked at by experts are largely the same but Plaintiff's experts and Goodman used different groupings depending on the conclusions they reached as to the ownership of some properties or entities.

[1432] The discussion of the LLP issue is done, in light of the burden of proof that rests on Plaintiff, by using Plaintiff experts' groupings and the following sub-headings: MLV, YH Corporate loans, MEC, TSH, CSH, OSH, TWTC and Meadowlark.

MLV

Experts' positions

[1433] Plaintiff's experts opined that LLPs were required for MLV, the proposed minimum LLPs being:

- 60 million, according to Vance.
- 52.2 million, according to Froese.
- 54.4 million, according to Rosen.

[1434] Goodman opined that no LLPs were needed for MLV.

Additional evidence specific to MLV

1989 Events

[1435] The renovations that were contemplated since 1983 had not yet been completed[1505].

[1436] The MLV hotels lost the Sheraton brand[1506].

[1437] National Bank and FICAN were upset over December 1988 and January 1989 interest payments being past due[1507]. Counsel for Mellon had requested a mortgage statement from the National Bank and FICAN but YHHL thought it was not prudent to show Mellon that MLV's accounts were almost 90 days in arrears. YHHL asked Castor to provide an advance to MLVII of $572,279 so it could pay arrears before the interests of February became due and obtain clean statements[1508].

[1505] Prychidny, October 14, 2008, pp.37-38
[1506] Prychidny, October 14, 2008, pp.36-38
[1507] PW-1070F (tab #10); PW-1070F-6 (Tab # 11)
[1508] PW-481F

[1438] On February 28, 1989, Castor transferred $282,545.40 to pay the December interest payments of National Bank and FICAN[1509].

[1439] In March 1989, National Bank and FICAN continued to exercise pressure for payment[1510] and Castor issued a check to MLVII to allow it to pay one more month of interests on the National Bank and FICAN loans and prevent these loans from being 90 days in arrears.[1511] A similar scenario took place every month, thereafter[1512].

[1440] On April 11, 1989, Prychidny wrote to Wersebe and Stolzenberg "*MLV desperately requires cash funding or faces various disconnect notices with respect to its utilities*" and " *As we all know, the property loses approximate $100,000 per month before debt service during the off-season*".[1513]

[1441] In a letter dated May 9, 1989, Ron Smith mentioned to YHHL that Castor's preferred position was to sell the properties as soon as possible, if a decent price could be achieved. Ron Smith wrote "*considering that MLV is totally over-leveraged, we want to minimize the amount of funding that we put in forward, especially any unsecured portion*".[1514] In his letter, Ron Smith also stated that "*the tough part is we know the MLV income projections are weak and most probably not attainable*".

[1442] Through a letter of its solicitors, FICAN advised Castor that it intended to proceed with an application to the Supreme Court of Ontario for an order appointing a receiver and manager of MLVII[1515].

[1443] The Mellon Bank refinancing did not take place.[1516] On August 21, 1989 Mellon provided formal notice to YHHL that the expired commitment to provide financing for the MLV complex was withdrawn[1517].

[1444] Cash was removed from the hotel without authorization[1518].

[1445] On September 8, 1989, FICAN filled its motion before the Supreme Court of Ontario to have C&L appointed as receiver to MLVII[1519]. Stolzenberg was upset that C&L could be appointed receiver of MLV[1520].

[1509] PW-1070F-7
[1510] PW-1070F-9
[1511] PW-1070F-10
[1512] See for example: PW-1070F-11, PW-1070F-12, PW-1070F-13, PW-1070F-14, PW-1070F-15, PW-1070F-16, PW-1070F-17, PW-1070F-23, PW-1070F-24. See also PW-1070-H and PW-1070H-1
[1513] PW-488
[1514] PW-492F-1
[1515] PW-1070F-18
[1516] PW-492A
[1517] PW-492C
[1518] PW-489
[1519] PW-1070F-18A
[1520] Ron Smith, September, 22, 2008, p.242-243

[1446] On September 12, 1989, FICAN consented to withdraw its motion and to postpone any further similar action until November 15, 1989 to allow a refinancing to go through, subject to various terms and conditions including a guarantee of payment from Castor[1521].

[1447] On October 17, 1989, YHHL wrote to Stolzenberg that if Castor was not providing it the funds required to pay the National Bank by October 20, 1989, YHHL was expecting the National Bank to demand payment of its entire loan during the week of October 23rd. [1522]

[1448] On November 13, 1989, FICAN's solicitors advised Castor that they had been instructed to proceed with their motion to appoint a receiver to MLVII[1523].

[1449] An agreement intervened between Castor and FICAN and Castor issued various checks to pay interests, legal fees and collection fees to FICAN[1524].

[1450] MLVII's financial condition worsened during 1989:

- Commitment letter from Mellon had expired and was withdrawn;
- YH had not been successful at attempts to sell the properties;
- National Bank and FICAN claimed their loans were in default and demanded immediate payments;
- MLVII continued to produce poor financial results[1525];
- Castor loan to fund operating shortfalls, which by its terms was to be repaid by September 15, 1988, was not repaid in 1989. Instead, the balance of the loan had increased to $4.76 million.

[1451] Income projections used to value the hotels, in 1988, and the Mall, in 1989, were not met[1526].

[1452] Castor received unaudited financial statements of MLVII as of December 31, 1989[1527] reporting net losses of more than 3 million.

[1453] As of December 31, 1989, the annual interest obligation of MLV was 24.1 million on outstanding loans totalling 166 million[1528].

[1521] PW-1070F-20; PW-1070F-22
[1522] PW-482C
[1523] PW-1070F-25
[1524] PW-1070F-27, PW-1070F-28, PW-1070F-29,PW-1070F-30, PW-1070F-33
[1525] PW-1053-19, sequential pages 161-162; PW-478G; PW-478H
[1526] PW-494, bates 000089, PW-496, bates 000064 and PW-478I
[1527] PW-478G

Loans as of December 31, 1989

[1454] At December 31, 1989, $109.2 million of loans were owed to Castor in relation to the MLV properties (some to CHL and some to CHIF).

Loans owed to CHL

- Loan 1105 to MLVII –4.8 million[1529]
- Loan 1048 to YHLP – 14 million[1530]
- Loan 1125 to KVWI – 7.2 million[1531]
- Loan 1126 to MLVII – 4.8 million[1532]
- Loan 1136 to MLVII (re FICAN) – 0.1 million[1533]
- Loan 1011 to Harling International – 3 million[1534]
- Loan 1012 to Runaldri S.A. – 2 million[1535]
- Loan 1013 to Charbocean Trading – 4 million[1536]
- Loan 1014 to Harling Finance – 7.5 million[1537]
- Loan 1015 to Gebeau Overseas – 5 million[1538]
- Loan 1016 to Gebeau Holding – 2.420 million[1539]
- Loan 1017 to Harling International – 3 million[1540]

[1528] PW-1076B
[1529] PW-1053-19, sequential pages 154-155
[1530] PW-1053-19, sequential pages 152-153
[1531] PW-1053-19, sequential pages 233-235
[1532] PW-1053-19, sequential pages 156-157
[1533] PW-1053-19, sequential page 99
[1534] PW-1053-19-11, sequential pages 134-135
[1535] PW-1053-19-11, sequential pages 136-137
[1536] PW-1053-19-11, sequential pages 138-139
[1537] PW-1053-19-11, sequential pages 144-145
[1538] PW-1053-19-11, sequential pages 142-143
[1539] PW-1053-19-11, sequential pages 140-141
[1540] PW-1053-19-11, sequential pages 146-147

- Loan 1018 to Trade Retriever – 2.280 million[1541]
- Loan 1019 to Trade Retriever – 2.220 million[1542]

Loans owed to CHIF

- Loan 770001/0009 to Runaldri –4.2 million[1543]
- Loan 26100/0004 to Charbocean Trading –8.4 million[1544]
- Loan 385005/3010 to Gebau Overseas - 9.9 million[1545]
- Loan 385009/3005 to Gebau Overseas –3.3 million[1546]
- Loan 385009/0003 to Gebau Overseas –3.8 million[1547]
- Loan 38500/0008 to Gebau Overseas – 0.9 million[1548]
- Loan 38500/0004 to Gebau Overseas – 3.704 million[1549]
- Loan 441004/3010 to Harling International – 4.5 million[1550]
- Loan 441004/0008 to Harling International –8.4million[1551]
- Loan 890000/0010 to Trade Retriever –5.5 million[1552]

[1455] CHL's loans to YHLP, KVWI and MLV investors remained unchanged from 1988 balances[1553].

[1456] CHL's loans to MLVII increased from $3.3 million to $10 million, including accrued interests.

[1457] CHIF's loans to MLV investors increased from $40.3 million to $46.2 million due to interest capitalization.

[1541] PW-1053-19-11, sequential pages 148-149
[1542] PW-1053-19-11, sequential pages 150-151
[1543] PW-1053-89, sequential pages 240, 250, 261
[1544] PW-1053-89, sequential pages 240, 249, 261
[1545] PW-1053-89, sequential pages 240, 249, 261
[1546] PW-1053-89, sequential pages 240, 249, 261
[1547] PW-1053-89, sequential pages 240, 249, 261
[1548] PW-1053-89, sequential pages 240, 249, 261
[1549] PW-1053-89, sequential pages 240, 249, 261
[1550] PW-1053-89, sequential page 240, 249, 261
[1551] PW-1053-89, sequential page 240, 249, 261
[1552] PW-1053-89, sequential page 240, 250, 261
[1553] PW-1053-19, sequential pages 20-21

Interests recognized as revenue

[1458] In 1989, Castor recognized interests totalling $9,537,718.57 as revenue on MLV related loans[1554].

Appraisals 1989

[1459] McKittrick of Jones McKittrick Somer Ltd. prepared an appraisal to assist YHHL management in evaluating the MLV mall (including the mall, the amusement park land and the observation tower)[1555]. It provided a market value opinion of 26 million, calculated through the income approach and based on the following assumptions:

- Income projections based on the assumption that a walkway to join different levels would be completed in the spring of 1989.
- Rental income projected to increase annually (at various rates) and expenses projected to increase by 5% to match inflation.
- Vacancy rates projected at 7.5%, compared to current vacancy rates of 19%.
- Base rents projected to increase by 100% the first year and, thereafter, by 5% annually due to the new walkway.
- A discount rate of 12%.

[1460] In their AWPs, C&L wrote they had seen a $40 million appraisal for the mall and the amusement park land prepared by R.W. Hughes[1556]. Ron Smith testified that no such appraisal ever existed, a testimony the Court finds credible and reliable[1557].

[1461] In August 1989, for the purpose of seeking investors who were not hotel investors, but who required income tax write-offs, Prychidny prepared a written estimate of value of the MLV mall and developable land, apart from the hotel properties, in which he inscribed a value of $40 million: $30 million for the mall, and $10 million for the developable land[1558].

[1462] At trial, Prychidny explained the circumstances surrounding this proposal and affirmed that, notwithstanding its content, there was no value to developable land[1559]:

- The proposal was prepared to explore the possibility of developing a master limited partnership;

[1554] PW-1075A
[1555] PW-496
[1556] PW-1053-19-9
[1557] Ron Smith, May 16, 2008, p.173
[1558] D-145
[1559] Prychidny, November 10, 2008, pp.114 and following

- The proposed transaction assumed that the three MLV hotels (the Foxhead, the Brock and the Village Inn) would be sold to a master limited partnership for $70 million with these investors investing in it under the terms and conditions described;

- The proposal did not bear resemblance to the market place and Prychidny was embarrassed to present it;

- Nevertheless, YHHL approached wealthy individual real estate promoters who required tax write-offs, but to no avail. These promoters were not interested in pursuing discussions;

- This proposal included a 40 million value based on the McKittrick appraisal (26 million rounded to 30 million) plus 10 million proposed by Wersebe for developable land;

- But there was no developable land and no value.

> And there's actually, when you look at the property itself, there's really no excess land, unless you tore down the Village Inn Motel.
>
> I recall clearing him on that, saying that the mall and the hotels required parking, so if you assume there's surplus land, you'd lose a parking. He responded that well, then we would build a multi-level parking structure to accommodate the parking and build the developable real estate above that. So, there was no accounting for the cost to build this multi-level parking if in fact that can be done[1560].

[1463] There were no contemporaneous appraisals for the amusement park assets. The only appraisal available was the Mullins appraisal of 1983 which estimated the replacement cost of the rides at $6.8 million[1561].

Experts' evidence

[1464] Vance opined that a minimum LLP of $60 million was required, based on the following elements:

- A maximum total value of $93.7 million ($67.7 million for the hotels and wax museum plus $26 million for the mall and amusement park);

- Prior ranking debts and other adjustments of $48.7 million;

- Castor's total exposure of $108.5 million;

[1560] Prychidny, November 10, 2008, pp.116-117
[1561] PW-493

- A deficiency of $59,823 million (rounded at $60 million) and no other sources to cover it. [1562]

[1465] Vance opined that using a total value of $144 million was totally inappropriate in the circumstances and that the value figure should not exceed $93.7 million.

[1466] Vance's opinion on the topic of "*other possible sources for payment*", summed up in the 1988 financial statements section of this judgment, applies *mutatis mutandis* to the 1989 situation.

[1467] Froese opined that a minimum LLP of $52.2 million was required, based on the following elements:

- Total value of $101.7 million ($67.7 million for the hotels and the wax museum plus $26 million for the mall and amusement park land, plus 6.5 million for the amusement park rides, plus $1.4 million for current assets);
- Prior ranking debts and other adjustments of $45.2 million;
- Castor's total exposure of $108.5 million;
- A deficiency of $52.2 million and no other sources to cover it[1563].

[1468] Rosen opined that a minimum LLP of $50 million was required, based on the following elements:

- Total value of $117 million ($91 million for the hotels and the wax museum plus $26 million for the mall and amusement park);
- Castor's total exposure of $114.5 million;
- A minimum deficiency between value available to Castor and Castor's total exposure of $50 million[1564].

[1469] Goodman opined that no LLPs were required, even though he calculated a deficiency of $12.6 million, based on the following elements[1565]:

- A total value of $140.9 million resulting from the $40 million value figure for the mall, the amusement park land and the surplus developable land, plus the $104 million figure for the hotels and wax museum, less $9.6 million for costs of enhancements, plus $6.5 million figure value for the amusement park rides;

[1562] PW-2908, vol. 2, section A; PW-2908, vol. 3, Tab # 1; Vance, April 9, 2008
[1563] PW-2941, vol.3, p.57; Froese, November 25, 2008
[1564] Rosen, February 3, 2009; Rosen, April 8, 2009; PW-3033, vol II, section D
[1565] D-1295, p. 349

- Prior ranking debts (Great-West, FICAN and National bank) and other adjustments of $44.3 million;
- Castor's total exposure of $109.2 million;
- A deficiency between value available to Castor (96.6 million) and Castor's total exposure ($109.2 million) of $12.6 million;
- The availability of other sources to cover the deficiency (Gambazzi's deposits and Wersebe's and Stolzenberg's guarantees.)

[1470] Goodman testified about his understanding of the expression " *a property is over leveraged"* as follows:

> The conventional views of what overleveraged would mean from a standpoint of a property can range from the following: One, there is indebtedness associated with or attached to a property that exceeds the cost of the property.
>
> There can be indebtedness, either attached to or associated with the property, that can exceed its market value.
>
> Or thirdly, there can be indebtedness, attached to or associated with the property, that can exceed its liquidation value.
>
> The term "overleveraged" is used in those three contexts and one would have to look at the particular facts of any situation to determine in what context the term "overleveraged" was being used in order to determine whether it's with respect to the cost of the property, the market value of the property or the liquidation value of the property, or some other value of the property[1566].

[1471] Goodman acknowledged that when Ron Smith was using the expression "*running out of projects*", Ron Smith meant that the debt on projects was already over 100% of the project market value[1567].

Conclusions

Value and minimum deficiency before other recovery sources

[1472] For the reasons expressed in the 1988 financial statements section of this judgment, and in light of the additional specific evidence regarding the MLV project during 1989, the 104 million value figure cannot be used to value the hotels.

[1473] The 40 million value figure used by Goodman for the mall, the amusement park and the excess land, based on the $26 million appraisal and a memo written by

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[1566] Goodman, November 30, 2009, pp.94-95
[1567] Goodman, November 30, 2009, p.100-101

Prychidny cannot be used either. Prychidny's testimony, that the Court finds credible and reliable, indicates that no "excess land" value existed.

[1474] The best possible scenario, as in 1988, would result into a total value figure of $100 million.

[1475] Based on a total value figure of $100 million, taking account of the minimum prior ranking debts and other adjustments figure (Goodman's figure of $44.3 million) and of the minimum Castor total exposure (Vance's and Froese's figure of $108.5 million), the minimum deficiency on MLV is $ 52.9 million.

Other possible sources of recovery

[1476] The analysis developed and the conclusions enunciated in the 1988 financial statements section of this judgment apply *mutatis mutandis.*

YH Corporate loans

[1477] The loans which are part of the YH Corporate loans for 1989, and which were looked at by Plaintiff's experts, are those described under the subheading "*YH Corporate loans*" of the 1988 financial statements section of the present judgment[1568] and the new loan created at year-end, loan 1137.

Experts' positions

[1478] Plaintiff's experts opined that a LLP was required for the YH corporate loans, such proposed minimum LLP being:

- 111.1 million, according to Vance.[1569]
- 80.6 million, according to Froese -with a middle point, then, of 97.4 million[1570] or, assuming various factual hypotheses suggested during cross-examination, a range of 87.8 to 93.9 million with a mid-point, then, of 90.8 million.[1571]
- 113 million, according to Rosen.[1572]

[1479] Goodman opined that no LLPs were needed for the YH corporate loans.

[1568] Account 046/loan 1053 , Loans 1123, 1081, 1092, 1090 and 1091, the CFAG loans and some various loans made by CHIF to Harling and KVWI
[1569] PW-2908, vol.II, p.B-15
[1570] PW-2941, volume 4, p. 2; PW-2941 new page 65, Froese, November 28, 2008, p.162
[1571] PW-2941-4, schedule 3 and schedule 4
[1572] Plaintiff's written submissions of July 8, 2010, p.22

Additional evidence specific to YH Corporate loans

1989 events

[1480] In 1989, Stolzenberg signed, on behalf of Castor, an acknowledgement confirming that Wersebe's European holdings would not be included in provisions of Wersebe's personal guarantees provided to Castor.[1573] Such acknowledgement was the result of previous discussions and understandings.[1574]

[1481] In July 1989, loan 1081 to YHDHL was increased from $30 million to $35 million. The term of the loan was extended from July 31, 1989 to November 1, 1990 and the personal guarantee of Wersebe was increased to $21,125,000[1575].

[1482] YH executives (Wersebe, Whiting and Lyndon) determined that the North American YH Group deficiency exceeded $349 million as at September 1989[1576], and that Castor's exposure to such deficiency was $245 million.[1577]

[1483] Whiting, chief financial officer of YHDL, prepared a "Fair Value Balance Sheet" for YHDL as at September 30, 1989[1578] that Stolzenberg described as "*hot air*".[1579]

[1484] Said fair value balance sheet as at September 30, 1989[1580] :

- Disclosed an adjusted equity deficiency of $33.9 million;
- Attributed no value to receivables from parent/affiliated companies totalling $133,869,000[1581]
- Assumed that YHDL's $3.8 million investment in shares of YHLP had no value;
- Assumed that YHDL's receivable from Gebau Overseas had no value;

[1573] PW-1058-4
[1574] PW-1058-2
[1575] PW-1054-14
[1576] Whiting, November 29, 1999, pp. 186-188.
[1577] PW-1157; Vance, April 15, 2010, pp. 65-66.
[1578] PW-1149
[1579] Whiting April 26, 2000, p. 116.
[1580] PW-1149.
[1581] Those are the receivables that were the object of the draft adverse opinion of YHDL's auditors (PW-1148)

- Assumed that a receivable from Harling International was impaired;
- Reflected the following fair market values of properties:
  - MEC : $300 million
  - Hazelton Lanes: $182 million
  - TWTC and TWTC option: $472 million
  - Palace II : $ 9 million
  - Triumph Hotel : $50 million
  - Meadowlark: $22 million.

[1485] YH management threatened to resign *en masse* unless Castor agreed to fund YH's operating requirements.[1582]

[1486] On December 4, 1989 and as part of the year-end reallocation of the balance appearing in account 046, Castor provided a $10 million loan to YHH Investments ("**YHHI**"), loan 1137, secured by a pledge of all management contracts on the three Skyline Hotels and MLV[1583].

[1487] On December 11, 1989, as part of the year-end reallocation of the balance appearing in account 046 and given capitalization of interest on the loan itself[1584], loan 1123 to KVWIL increased from $14.4 million to $27 million, the maturity date of the loan was extended from December 1989 to December 1990[1585] and Wersebe's personal guarantee was increased to $22.5 million[1586].

[1488] Effective December 29, 1989, loan 1090 to YHDL increased and went from $3.2 million to $6.5 million, and its term was extended from December 1989 to December 1990[1587].

[1489] Loan 1092, in the amount of $10 million, was extended from December 1989 to December 1990.

[1490] In December 1989, documents were shown by YH to Castor evidencing YH's insolvency.[1588] YH management determined that Castor was seriously exposed to deficiencies.[1589]

[1582] Quigley, March 15, 2010, pp. 213-214; March 16, 2010, pp. 63-64.
[1583] PW-1062-1
[1584] PW-1056C, page 2
[1585] PW-1058-6
[1586] PW-1058-6
[1587] PW-1061-6

[1491] In a year-end memo dated December 28, 1989, Ron Smith provided direction to YHDL that the loans proceeds of $13.2 million were to pay interest and principal related to specified YHDL loans to Castor and requested that YHDL facilitate the flow of funds.[1590]

[1492] In late December 1989, Castor resorted again to a cash circle operation. On December 26, 1989, Castor disbursed $13.2 million to McLean & Kerr. Those advances funded two loan transactions made with YHDL (the increase in the amount of $10 million of loan 1067 and the increase in the amount of $3.2 million of loan 1090). Most of the funds were returned to Castor and recorded as payments of interest, fees and principal on various loans. [1591] Two checks totalling $13.2 million payable to McLean &Kerr in trust were issued by CHL and recorded in CHL's cash disbursement journal[1592]. On the same day, CHL collected $12,868,000.00.[1593]

[1493] The balance in G/L account 046 was $120,229 as at December 31, 1989[1594].

- At December 31, 1988, account 046 had been reduced to $1,834 992.04.[1595]
- During 1989, account 046 grew at least to $35 945,229.00[1596] by December 29, 1989 when it was reduced by a transfer of $35 825,000.00.[1597]
- Part of the above increase was due :
    - to capitalization of interest (over $13.5 million);
    - to fees in excess of $3 million;
    - to accrued interests in excess of $3 million on the CFAG loans ; and
    - to advances to and on behalf of YHDL (over $17.5 million).[1598]

[1588] PW-1149; PW-499C-1; PW-1153; Whiting, November 17, 1999, pp. 93-103.
[1589] PW-1157; Vance, April 15, 2010. pp.65-66; Whiting, November 29, 1999, pp. 186-188
[1590] PW-1061-7
[1591] PW-2941, volume 4, p.30, paragraph 2.74
[1592] PW-96, bates 000003 and 000004
[1593] PW-96, bates 000195; PW-2908,vol. II, pp B-11 and B-12
[1594] PW-80, bates 000049
[1595] PW-79, bates 52 and PW-80, bates 000045
[1596] PW-80, bates 000045 to 000049
[1597] PW-80, bates 000049. See loans 1081, 1137, 1042 and 1123 to which the reallocation was made
[1598] PW-80, bates 000045 to 000049 (see namely for list of journal entries and of cash disbursements); as examples of journal entries see PW-95, bates 000018, 000080 and 000081, 000127 and 000128, 000132 and 000133, 000163, 000178 to 000184, 000267 to 000270, 000291 and 000292, 000334

[1494] C&L looked at account 046, made notes in their audit working papers, namely of the capitalization of interest.[1599]

[1495] CFAG loans ($20 million) were unchanged during 1989.

[1496] Castor did not record a specific allowance for LLPs for any YH corporate loans in 1989.

Loans as of December 31, 1989

[1497] As of December 31, 1989, the balances of "YH Corporate loans" owed to Castor and specifically reviewed by Plaintiff's experts were:

- Loan 1123 to KVWIL- 27 million[1600]
- Loan 1081 to YHDHL – 35 million[1601]
- Loan 1092 to YHDL- 10 million[1602]
- Loan 1091 to YHDL – 29 million[1603]
- Loan 1090 to YHDL- 6.5 million[1604]
- Loan 1137 to YHHI - 10 million[1605]
- CFAG loans to YH – 20 million[1606].

Interests recognised as revenue

[1498] In 1989, Castor recognized interests on YH corporate loans totalling $21.2 million as revenue[1607].

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and 000335, 000343 and 000344, 000410 to 000414, 000567 and 000568; as examples of cash disbursements see: PW-96, bates 000015 and 000016, 000050 and 000066, 000074 and 000079, 000081 and 000082, 00085 and 00086, 00091 and 00092, 000107 and 000108, 000141.

[1599] PW-1053-19, sequential pages 24 and 26

[1600] PW-1053-19, sequential pages 236-238

[1601] PW-1053-19, sequential pages 208-210

[1602] PW-1053-19, sequential pages 206-207

[1603] PW-1053-19, sequential pages 181-183

[1604] PW-1053-19, sequential pages 204-205

[1605] PW-1053-19, sequential pages 251-252

[1606] PW-1053-73, sequential pages 296-300; PW-1053-72, sequential pages 94, 112, 146, 273, 286;

[1607] PW-1485 R; PW-2908. Vol.1, S-9

Experts' evidence

Vance

[1499] Vance used the same methodology as he used for the 1988 financial statements.[1608] He opined that Castor's exposure to YH Corporate loans amounted to $121 million[1609] and that the minimum LLP was of $111 million.[1610]

[1500] Vance explained why Castor's exposure had increased: the snowball effect of the capitalization of interest.[1611]

[1501] Vance took into account various financial statements.[1612] Those financial statements or their content were available to C&L or should have been made available to C&L had they asked for them since the YH group had the obligation to regularly provide financial statements and financial information to Castor (according to loan covenants signed).[1613]

[1502] Vance looked at the Wersebe's personal guarantees and concluded they had no value.[1614]

[1503] Vance namely looked at the financial situations of YHDHL and KVWIL and he concluded that they had not improved.[1615]

[1504] Vance indicated that the content of the "*fair value balance sheet*" prepared by Whiting was relevant namely in light of the draft adverse audit opinion[1616] received by YHDL.[1617]

Froese

[1505] Froese reached the conclusion that there was no collateral value to the common or special shares of YHDL.[1618]

[1506] Froese took account of the "fair value balance sheet" prepared by Whiting as of September 30, 1989 (PW-1149) and he explained why.[1619] Froese indicated that it was

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[1608] Vance, April 14, 2008, pp.166 and followings
[1609] Vance, April 14, 2008, pp.165-166
[1610] Vance, April 14, 2008, p.156
[1611] Vance, April 14, 2008, p.157
[1612] PW-1137-4, PW-1138-1, PW-1136-5, PW-1140, PW-1165-1.
[1613] Vance, April 14, 2008, pp.177-178
[1614] Vance, April 14, 2008, p.142
[1615] Vance, April 14, 2008, pp.167 and followings
[1616] PW-1148A
[1617] Vance, April 14, 2008, pp.175-176
[1618] Froese, November 28, 2008, pp.8 and followings

showing a significant shortfall along with a lot of inter-company parent affiliates provisions.[1620] He confirmed that PW-1149 included values in excess of the reality.[1621]Acknowledging that it had been prepared for negotiation purposes and that it had not been audited, Froese said the amount of negative equity shown was nevertheless consistent with:

- the information gathered by Thorne Ernst & Whinney who had issued a draft adverse opinion[1622] that there were significant write-downs or provisions required;
- the inability of YHDL to make its payments as they came due;
- the fact that YHDL was not able to provide audited financial statements to Castor as it had to; and
- the testimony of Ron Smith in relation to his evaluation of loans to YHDL. [1623]

[1507] Froese confirmed he had considered the possibility that YH could have withheld information such as the draft adverse audit opinion[1624] but he added that C&L should have raised questions, which they did not. Given the loan covenants signed by the YH group, Froese explained that asking questions would have lead C&L somewhere independent of the answers; it would have raised issues as to why no audited financial statements were provided to Castor or as to why communication of them was refused.[1625]

> Let's go to the example you used, then, the adverse audit opinion. I would agree with you that York-Hannover would not necessarily want to disclose a draft adverse audit opinion to either Castor or to Coopers & Lybrand. And what I outlined in my testimony was that in requesting an audited financial statements for nineteen eighty- eight (1988), the auditors either will get something or they won't. And if they're told there isn't one available, Castor says there's not one available from York-Hannover, they've not finished their audit yet or whatever they're told, you have the option of asking to speak to the auditors. If you're not given permission for that, that tells you information as an auditor as well, why can't I speak to the auditors of the borrowers? So, either way, I think it raises

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[1619] Froese, November 28, 2008, pp.59 and followings; Froese, January, 8 2009, pp.192 -238; Froese, January 9, 2009, pp.23- 57
[1620] Froese, November 28, 2008, p.64
[1621] Froese, January 9, 2009, pp.46-48
[1622] PW-1148A
[1623] Froese, November 28, 2008, p.64-66; Froese, January 9, 2009, pp. 104-105; Ron Smith, Mai 14, 2008, pp.56 -63 ;
[1624] PW-1148A
[1625] Froese, December 4, 2008, pp.187; Froese, January 9, 2009, pp.117-122-

> issues that you want to deal with as an auditor, as to whether this loan is a problem loan and how much work you want to do around that one.[1626]

[1508] Froese explained how he had treated the two options that had been granted as collateral.[1627]

[1509] Froese explained why he had given no value in 1989 to receivables granted as collateral for loan 1092.[1628]

[1510] Froese confirmed he had given no value to the management contracts given as security for loan 1137 and explained why: Froese namely took into account the general circumstances of the hotels' operations and a subsequent event (a change in security) that took place in March of 1990 specifying that C&L should have been still working on the 1989 audit given all the issues they should have looked at before issuing their report.[1629]

[1511] Froese said he had given no value to Wersebe's personal guarantee in 1989. He reiterated that C&L had never looked at Wersebe's financial situation.[1630]

[1512] Froese confirmed that his position concerning the CFAG loans for the 1989 financial statements was the same as for 1988.[1631]

[1513] Froese explained why there were some differences in the low end of his suggested range of LLPs and why there were some differences between the suggested ranges of Plaintiff's experts.[1632] Nevertheless, Froese confirmed he was confortable to opine that a large LLP was required for the YH Corporate loans.[1633]

[1514] Given the differences between experts, Froese summarized the relevant questions or issues for the Court as follows:

> The first question is: Are the ranges approximately reasonable? And you'll have to evaluate the ranges. But the second part of it is: What should Coopers & Lybrand have reasonably come up with as a range had they complied with GAAS?[1634]

[1626] Froese, December 4, 2008, pp.187-188
[1627] Froese, November 28, 2008, pp.69-71
[1628] Froese, November 28, 2008, pp.71-72
[1629] Froese, November 28, 2008, pp.72-76
[1630] Froese, November 28, 2008, p.137
[1631] Froese, November 28, 2008, pp.121 and followings
[1632] Froese, December 5, 2008, pp.12-18;
[1633] Froese, January 9, 2009, pp.117-122
[1634] Froese, December 5, 2008, p.17

[1515] Rosen confirmed he had prepared a range of LLPs, not a best possible estimate.[1635]

[1516] Rosen reaffirmed he had given C&L the benefit of the doubt when calculating his suggested ranges of LLPs.[1636]

Goodman

[1517] Goodman's positions relating to the YH Corporate loans for the 1989 audit is the same as for the 1988 audit and has already been discussed earlier in the present judgment.

Conclusions

[1518] The events that took place during 1989 strengthen the conclusion that personal guarantees granted by Wersebe were worthless to Castor in that they were limited to Wersebe's interests in his North American entities[1637] which were fully leveraged and insolvent.[1638]

[1519] All the comments made relating to the YH Corporate loans for the 1988 audit, under the subheading "*YH Corporate loans*", apply *mutatis mutandis* to the 1989 audit.

[1520] Even though it might not have been communicated to C&L when they did their audit field work for the 1989 audit, as Froese acknowledged during his testimony, the Court finds using exhibit PW-1149 in GAAP analysis, as Plaintiff's experts did, is appropriate since PW-1149 was remitted then to Castor and since it represented the contemporaneous position or understanding of Castor's debtors (YH group) representatives.

[1521] Plaintiff experts' opinions must prevail: a huge LLP was required in relation to the YH Corporate loans in 1989.

MEC

Experts' positions

Plaintiff's experts

[1522] All plaintiff experts opined a LLP was required for the MEC in 1989 and they all added that the loans should have been placed on a non-accrual basis during 1989.

[1635] Rosen, April 8, 2009, pp.18-19
[1636] Rosen, April 8, 2009, pp.33-34
[1637] Ron. Smith, May 14, 2008, pp. 212-213, 246-247; PW-1058-2; PW-1058-4.
[1638] Ron Smith, May 14, 2008, p.83; PW-1153; Prychidny, October 14, 2008, pp.83-85; D-1312, ES-25, 154

[1523] Vance opined the minimum required LLP was in the amount of 20.9 million,[1639] Froese opined his mid-point was 14.4 million (his range being 1.4 to 27.4 million)[1640] and Rosen calculated a range between 59 and 73 million using the methodology of percentage of completion.[1641]

[1524] Vance used a MEC market value at completion of $303 million including the pad[1642] ($261 million[1643] plus $ 42 million for the pad).

[1525] Froese used a range of market value for the MEC project, excluding the pad, of $266 to $285 million.[1644]

[1526] Froese indicated that the LLP could have been a nominal amount had Castor placed the loans related to MEC on a non-accrual basis in 1989, ceased to accrue interest on the loans and disclosed the extent of loans on a non-accrual basis in its financial statements.[1645]This was not done.

[1527] Vance and Froese took into account future interest payable to Castor, as part of the costs to complete.

Goodman

[1528] Goodman opined that there was a surplus of $15 million in 1989 using the following figures:[1646]

- Total value: $331.1 million;
    - MEC market value at completion : $317 million ($275 million[1647] plus $42 million);
    - Palace II and tunnel : $11 million;
    - Contribution from third parties and tenant accounts receivable : $3.1 million
- Total value of collateral security : $265.9 million;
- Prior ranking creditor exposure: $ 103.4 million;

[1639] Vance, April, 10, 2008, pp.94 and following
[1640] PW-2941, volume 3, p.169 and PW-2941-4, schedule 1; Froese, November 26, 2008, pp. 76-84
[1641] PW-3033; Rosen, April 7, 2009, pp.67-75, 168-169, and 185 and following
[1642] Vance, April, 10, 2008, p.95
[1643] PW-1108
[1644] PW-2941, vol. 3, p.205
[1645] PW-2941, volume 3, pp.169-170, 205 and PW-2941-4, schedule 1 note 7; Froese, November 26, 2008, pp. 76-84
[1646] D-1325;
[1647] His best estimate from PW-1108A

- Castor's exposure to MEC project: $ 147.5 million.

[1529] Goodman did not include future interest payable to Castor in his costs to complete.

[1530] Goodman explained that his loan security surplus had declined from 1988 (from 58.4 million to 15 million) as a result of the following factors:

- Delays and cost increases;
- Absence of contemporaneous appraisal.[1648]

Additional evidence specific to MEC

Generalities

[1531] After the project started, and all through 1989, there were various slowdowns due to the changes of the scope of the project, from Scheme A to Scheme B and C for the pad. Costs escalated[1649] namely as a result of changes in the scope of the project[1650].

[1532] Bank of Montreal agreed that they would continue funding the project, but they made it very clear that they were the last ones in and the first ones out, and that they expected that the owners or Castor would cover any deficiency before Bank of Montreal would put up any additional funds[1651].

[1533] Dragonas more or less became the person representing the owners' interests under 97872[1652] which started taking over control of the project from YHDL. Most of the overruns and the costs relating to the development of the office pad were put through the loan facility granted to 97872[1653], loan 1145.

[1534] According to MEC's audited financial statements for the year ended September 30, 1989, project costs incurred as of that date were $197 million and estimated costs to complete the property under development were approximately $80 million, resulting in an estimated total cost of the project of $277 million[1654].

[1648] D-1312, p. 145
[1649] Ron Smith, September 15. 2008, p. 157
[1650] Ron Smith, September 15, 2008, pp.196-197
[1651] Ron Smith, September 15, 2008, p. 157
[1652] Ron Smith, September 15, 2008, p. 160
[1653] Ron Smith, September 15, 2008, p. 160,162-163, 178-179; PW-1104, tab 11
[1654] D-99A, page 7.

[1535] In the Fair Value Balance Sheet prepared by YHDL, dated December 14, 1989, Whiting assumed that the fair market value of 100% of the MEC would be $300 million[1655].

[1536] The December 1989 Monthly Project Report, dated February 6, 1990, provided the following analysis of project economics: [1656]

> "Based upon Royal LePage appraisal of August 5, 1988 (with office tower), *the economics of the project are:*
>
> | | |
> |---|---|
> | *Mean appraisal value* | *275,000,000* |
> | *(Based on a N.O.I. of $18,508,000)* | |
> | *Less: Total project loans* | *209,416,826* |
> | *Equity before advances* | *65,583,174* |
> | *Less: Co-owners' advances* | *33,609,477* |
> | *NET EQUITY* | *31,973,697"* |

[1537] At December 31, 1989, Castor had equity loans outstanding of $24 million to YHDL, $10 million to 612044, and $30.2 million to 97872, or almost exactly the amount of "equity before advances" calculated in the Report.

[1538] There was no additional appraisal done in 1989.

Specific facts of 1989

[1539] Castor provided a new loan facility to Palace II of up to $3 million.[1657] The proceeds of this loan were used to pay interests and fees on CHIF loan of $7.55 million, as well as legal fees.[1658]

[1540] Unaudited financial statements for 97872 for the year ended July 31, 1989, a notice to reader dated January 14, 1990, disclosed a deficit of $6.8 million.[1659]

[1541] Draft audited financial statements for 97872 for the year ended September 30, 1989 were transmitted by Peat Marwick Thorne to Goulakos with a letter listing outstanding significant matters, including the following:

> Receipt of final audited financial statements of the Montreal Eaton Center Project from our Montreal office. I understand these statements will be finalized upon resolution of the project financing negotiations. [1660]

[1655] PW-1149.
[1656] D-99E.
[1657] PW-283A-3
[1658] PW-283A-2
[1659] D-96

[1542] Unaudited financial statements for 612044 for the year ended October 31, 1989, a notice to reader dated November 14, 1989, disclosed :

- a deficit of $2.8 million;
- an advance of $2,345,317 from 606752 Ontario Limited;
- a $7.5 million investment in 97872;
- a $100 investment in Palace II. [1661]

[1543] In November 1989, Castor extended its $7.5 million loan to 612044 from November 1989 to November 1990 and increased it to $10 million.[1662] 612044 agreed to limit encumbrances against its assets and the issuance of additional shares. 612044 reiterated that security included 100% of the common shares of 97872 and $7.5 million of the preferred shares of 97872.[1663]

[1544] In December 1989, Castor provided a revolving line of credit to 97872 in the amount of up to $45 million (loan 1145). The purpose of the loan was disclosed as to "*finance Borrower's investment in real estate.*"[1664]

[1545] The audited financial statements of MEC for the year ended September 30, 1989, with the auditor's report dated December 15, 1989, indicated that the project costs incurred were $197 million and that the estimated costs to complete were approximately $80 million for a total of $277 million.[1665] These statements also disclosed a subsequent event: the sale of the pad for an amount of $42 million.[1666]

[1546] In its "Fair value balance sheet", prepared by Whiting and remitted to Castor, YH:

- Assumed that the fair market value of 100% of the MEC was $300 million;
- Disclosed that the Palace II Developments had a value of approximately equal to its liabilities;
- Reflected MEC at a net investment value of $7 million.[1667]

Loans as of December 31, 1989

[1660] PW-565-7C-1
[1661] PW-566-2
[1662] PW-1103-2
[1663] PW-1063-8
[1664] PW-1103-5
[1665] D-99A, page 7
[1666] D-99A, page 8; see also PW-1108B, appendix E
[1667] PW-1149

[1547] Castor's total exposure to MEC as of December 31, 1989 amounted to 147.5 million:

- Loan 1100 : 55.5 million[1668]
- Loan 1109: 4.1 million[1669]
- Loan 1101: 10.1 million[1670]
- Loan 1103: 4 million[1671]
- Loan 1145 : 30.6 million[1672]
- Loan 1042: 24.2 million [1673] as part of the year-end reallocation of account 046, an additional amount of $10 million was put to loan 1042[1674]
- Loan 1095: 10.1 million[1675]
- Loan 1146: 1.3 million[1676]
- Loan 701,001/2001 : 7.6 million[1677]

Interests recognised as revenue

[1548] In 1989, Castor recognized interests on the MEC related loans totalling $16,562,323.00 as revenue[1678].

Conclusions

[1549] The Court finds that Vance's value of $261 million, in accordance with the content of the Royal LePage appraisal PW-1108, should have been used. Had Goodman used such a figure, and assuming he would have been right on all other figures, there would have been no surplus.

[1668] PW-1053-19, sequential pages 222-223
[1669] PW-1053-19, sequential pages 224-225
[1670] PW-1053-19, sequential pages 226-227
[1671] PW-1053-19, sequential pages 226-227
[1672] Ron Smith, September 15, 2008, p. 163; PW-1100B; PW-1105; PW-1053-19, sequential pages 228-229
[1673] PW-1063; PW-1056-C; PW-1105
[1674] Ron Smith, September 15, 2008, p.175; PW-85 ; PW-1053-19 sequential pages 24 and 26 and 211-212
[1675] No LEQ was completed in 1989 but one was done in 1990 and confirmed there was no change to the loan balance – see PW-1053-15, sequential pages 294-295
[1676] PW-1053-19, sequential page 97
[1677] PW-1053-89, sequential page 235
[1678] PW-1105

[1550] This being said, given all evidence available[1679] but without agreeing to any specific components found in Goodman's computations for MEC, the Court does not conclude that a LLP was required for the MEC project in 1989 - it was arguable that no LLP was required.

TSH

Experts' positions

[1551] All plaintiff experts came to the conclusion that a LLP was required, their minimum LLP being:

- Vance : $29.3 million[1680]
- Froese: $31 million[1681]
- Rosen: $24.9 to $28.9 million[1682]

[1552] All plaintiff experts also concluded that loans should have been placed on a non-accrual basis.[1683]

[1553] Vance used the $93 million figure as value for the purpose of his calculations but he opined that by doing so he was clearly coming up with a minimal LLP:

> Q.- You've seemed to express some reservation with respect to the value that was given by the appraiser, considering amongst others this issue of the actual revenue versus the projections that were used. Did you use yourself the value of ninety-three (93) million in your calculation of the loan loss provisions?
>
> A.- Yes, I did. I am not able to... There is no other appraised value around. I was trying to get a... what I would call a minimum loan loss provision, so by using the ninety-three (93) million dollar value, that's, I guess, the best it can get insofar as value of the property goes and in addition to using the ninety-three (93) million dollars, I did not apply a loan-to-value ratio either, I didn't discount the value to eighty percent (80%) of the collateral, so that's why I say my provision is most certainly a minimum provision.[1684]

[1554] Goodman concluded that there was no need for a LLP but he severed his analysis of the Lambert loans totalling $39.4 million from the TSH indebtedness.[1685]

[1679] Namely PW-1149 (value of $300 million for MEC as per YH- Whiting)
[1680] Vance, April 8, 2008, pp. 165 and following
[1681] Froese, January 27, 2009, pp. 94 and following; PW-2941-4 ;
[1682] PW-3033; Rosen, February 4, 2009, pp.195 and following; Rosen, April 7, 2009, pp.169 and following; Rosen, April 22, 2009, pp.201 and following
[1683] PW-2941, Vol. 2, p. 4; PW-2908, Vol. 1, p. 4-I-18 to 4-I-19; PW-3033, Vol. 2, Appendix A, p. 6.
[1684] Vance, April 8, 2008, pp.145-146
[1685] D-1312, p. 395

Goodman evaluated the exposure of Castor to the TSH at $79.9 million only and he therefore opined that there was a surplus of $9.9 million.[1686]

[1555] Had Goodman taken account of the Lambert loans totalling $39.4 million,[1687] Goodman would have come to a minimum deficiency figure of $ 29.3 million, same figure as Vance's minimum LLP.

1989 events

[1556] The peak year for the hotel real estate market had been 1988 and it was not possible to obtain as good a price for any of the hotels in 1989.[1688]

[1557] An analysis of the value of TSH prepared by Prychidny at year-end 1989 assumed that $10 million worth of renovations to the hotel were required and estimated the realizable value of the TSH at $50 million.[1689]

[1558] The income pre-debt fell far short of the projected budgets and was insufficient to service the annual interest obligations.[1690]

[1559] Overdue 1988 realty taxes of $414,277 and 1989 realty taxes of $1,480,224 (excluding interest and penalties) remained unpaid by June of 1990[1691].

[1560] The 1989 unaudited financial statements for Topven (1988) disclosed a deficit of $16,894,000.51.[1692]

[1561] The figures in the month end report for the TSH for December 1989 disclose negative information about the TSH operations in 1989 : the decline in revenues over the year, the actual income pre-debt of $298,970 as compared to the budgeted amount of $3.5M and the net income pre-debt of negative $14.5 million.[1693]

[1562] Cash circles were used to pay interest on Lambert's loans.[1694]

[1563] The total accumulated deficit of the TSH owners (Topven, Topven (88) and Lambert) as of December 31, 1989, was $71.2 million.[1695]

[1686] D-1312, p. 398
[1687] PW-1053-89, sequential page 249
[1688] Prychidny, October 14, 2008, p. 218; November 4, 2008, pp. 243 – 245.
[1689] PW-499C; PW-499C-1: The TSH's monthly financial statements reported income pre-debt at year-end of $1.8M for 1988 (PW-424); $298,000 for 1989 (PW-429) and -$2M for 1990 (PW-430).
[1690] PW-1084A and PW-424, bates p. 9; shows income pre-debt of $1.8M and a loss for the year of $9M (this is a preliminary report but the figures are confirmed in PW-429, the 1989 statement with comparative figures for 1988); PW-1084B and PW-429, bates p. 14; PW-1084C and PW-430, bates p. 11.
[1691] PW-447A-1.
[1692] PW-433A.
[1693] PW-429
[1694] Froese, January 27, 2009, pp. 66 and following; Levi, January 14, 2010, pp. 81 and following

Loans as of December 31, 1989

[1564] At December 31, 1989, $117.2 million were owed to Castor (CHL and CHIF) in relation to loans made in connection to TSH.

Owed to CHL

- Loan 1107 - $40 million[1696]
- GL 066 (operating line) - $17.8 million[1697]

Owed to CHIF

- Loan 888002/2003 - $20 million[1698]
- Loan 576000/3002 - $32.6 million[1699]
- Loan 576001/3009 - $ 6.8 million[1700]

Interests recognised as revenue

[1565] $ 11,149,835.43 of capitalized interest on CHL loans 1107 and GL66 and on CHIF's loan 888002/2003 was recognized as revenue in 1989.[1701]

Appraisals 1989

[1566] There was no new appraisal in 1989.

[1567] C&L used the 1988 appraisal of $93 million.[1702]

Conclusions

[1568] The comments and analysis made under the subheading relating to the TSH in the 1988 consolidated audited financial statements section of the present judgment apply *mutatis mutandis* to 1989.

[1695] Froese, PW-2941, vol.2, paragraph 2.95; PW-444a and PW-444b
[1696] PW-1053-19, sequential pages 171-173
[1697] PW-1053-19, sequential pages 174-175
[1698] PW-1053-89, sequential page 250
[1699] PW-1053-89, sequential page 249
[1700] PW-1053-89, sequential page 249
[1701] PW-1081A
[1702] PW-423

[1569] The indebtedness increased and the value of the TSH did not. At best, the market value of the TSH was $93 million, but the evidence shows it was probably much less than $93 million.

[1570] Taking account of the best possible scenario as to market value (at $93 million), and the various figures proposed by all experts, Castor should have recorded at least a LLP of $ 24.2 million.[1703]

CSH

Experts' positions

[1571] There is no dispute between the experts that there were material loss exposures in each of the years in connection with the CSH project. The issue in dispute is whether GAAP required that loan loss provisions be taken.

[1572] The Plaintiff's experts identified the following minimum required LLP on the assumption that one could rely on the appraisal of the CSH:

- Vance : $18 million[1704]
- Froese : $13.4 to $27.2 million[1705] or, as per cross-examination hypothesis, $12.7 million to $ 26.4 million[1706]
- Rosen : $12.2 to $22.8 million[1707]

[1573] Plaintiff's experts agreed that the loans should have been placed on a non-accrual basis. Moreover, the magnitude of the increase in Castor's allowance for loan losses created uncertainty as to Castor's ability to continue as a going concern.[1708]

[1574] Using a property value of $50.3 million from which he deducted $2 million to cover renovations, Goodman calculated a loan deficiency of $20.2 million.[1709] However, and as he concluded for the 1988 audit and for the same reasons, he opined there was no need for a LLP in 1989.[1710]

[1703] Indebtedness of $117.2 million less best scenario of market value of $93 million
[1704] PW-2908, Vol. 1, S-9
[1705] PW-2941, Vol. 1, p. 25.
[1706] PW-2941-4
[1707] PW-3033, Vol. 2, Appendix G, p.3, Approach A (unadjusted figures).
[1708] PW-2908, Vol. 1, pp. S-8 to S-10; PW-2941, Vol. 2, p. 126; PW-3033, Vol. 2, Appendix G, p. 5.
[1709] D-1312, p. 428
[1710] D-1312, p. 430

Additional evidence specific to CSH

1989 events

[1575] The hotel continued to lose significant amounts of money after debt service.[1711] C&L did review the 1989 financial statements of Skyview showing a loss for the year of over $7 million and a cumulative deficit of $11.7 million.[1712]

[1576] The loan covenants were not respected by Castor's borrowers and interest and fees were systematically capitalized.

[1577] The planned renovations mentioned in the PKF market study[1713], and relied upon by C&L in their 1988 audit, were not yet done even though the assumption was that they would be completed by February 1988.

Loans as of December 31, 1989

[1578] The same loans from Castor and CHIF (NV) loans to Skyview Hotels, Skyeboat and 321351 Alberta were in place in 1989, as in 1988, except that the loan balances had increased, primarily as a result of capitalized interest.

[1579] By December 31, 1989, Castor's loans to 321351 Alberta and Skyeboat had increased and went from $7.9 million and $10.8 million, respectively, to $9.7 million and $12.1 million. The loan increases resulted primarily from capitalized interest[1714].

[1580] Interest on the $25 million first mortgage and $16 million second mortgage was accrued in the interest reserve account, with the result that the reserve was depleted. The balance went from a deposit of $1.7 million at the end of 1988, to $3.4 million owing to Castor by the 1989 year end. The balance in this account was reclassified to loan 1154 in February 1990[1715].

Interests recognised as revenue

[1581] The interest and fees recognized in respect of the CSH for 1989, which should have been reversed, were in the amount of $ 9.4 million.[1716]

[1711] Prychidny, October 15, 2008, p. 175
[1712] PW-467C
[1713] PW-469
[1714] PW-167Q and PW-167R.
[1715] PW-167T.
[1716] PW-2908, vol. 1, page S-9

Conclusions

[1582] The comments and analysis made under the subheading relating to the CSH in the 1988 consolidated audited financial statements section of the present judgment apply *mutatis mutandis* to 1989.

[1583] The indebtedness increased and the value of the CSH did not.

[1584] Taking account of the various figures proposed by all experts, Castor should have recorded a material LLP relating to the CSH loans in 1989.[1717]

OSH

Experts' positions

[1585] The only one of Plaintiff's expert to opined on the OSH was Vance. He concluded that a LLP of $ 14.5 million should have been recorded by Castor in 1989.[1718] He also opined that all interest and fee revenue on the OSH loans should have been reversed.

[1586] Vance came to that LLP taking into account the following information:

- Value of property after renovations completed : $ 29 million[1719]
- Value of Campeau's interest: $16 million[1720]
- Castor's exposure : $14.5 million[1721]

[1587] Vance explained why he had come to this result as follows:

> In nineteen eighty-nine (1989) and nineteen ninety (1990), the income that was generated by the property was not sufficient to cover the rent and therefore, this basis of taking the value and extracting the rent value out of it, you would come to a negative amount for the actual lease operations. You would be taking out more than was being generated and have no value, and that is representative by the financial statements of the Ottawa Skyline, that it did not have value, it was saddled with debt and so therefore, after the rent, then there was a huge interest charge that would be paid and they have large loss es.

[1717] The lowest LLP calculated is Rosen's minimum at $ 12.2 million.
[1718] Vance, April 9, 2008, pp.41 and following, p.57
[1719] Vance, April 9, 2008, pp. 46, 52
[1720] Vance, April 9, 2008, p. 46
[1721] Vance, April 9, 2008, pp. 55-56

> So, in nineteen eighty-nine (1989) and ninety ('90), certainly the values used in the Fitzsimmons' appraisal, is predicating it on income after the rent of one million four hundred ninety-six thousand (1,496,000) or two million one hundred twelve thousand dollars ($1,112,000), and they're just not appropriate at all, so therefore, I have no basis to give it value and as the operations were running at a loss, if you were looking at the value of a business, calculating a value of a business that runs at losses, there really is no value.
>
> So therefore, the loan loss provisions in nineteen eighty-nine (1989) are fourteen million four hundred ninety-four thousand dollars ($14,494,000) or fourteen million five (14,5) and in nineteen ninety (1990), nineteen million one hundred eighty-two thousand (19,182,000) or nineteen million two hundred thousand (19,200,000).[1722]

> The loan to that were again the shares of Skyline 80, which was the hotel, and when you came right back to it, the hotel, that certainly had no value, it was... deficits were growing, its operating losses were increasing and it just continued throughout the three (3) years to increase. In nineteen eighty-eight (1988) and eighty-nine ('89), there were its own financial statements and in nineteen ninety (1990), it was sold in March to 687292, and I've prepared an exhibit, I think, PW-1464-3, merely to combine the two (2) sets of financial statements to show the operating results, and the losses in nineteen ninety (1990) again that were... As before depreciation was six million two hundred and fourteen thousand dollars ($6,214,000) and the deficits increased throughout that period. So, there really was no value accruing to the hotel, in fact it was deteriorating quite rapidly.[1723]

[1588] Defendants' expert, Goodman, acknowledged that there was a deficiency in Castor's loan position of $ 3.9 million.[1724] He came to that deficiency using the following values and exposure figures:

- Value of property : $33.8 million
- Costs of required renovations : $ 6 million
- Value of Campeau's interest : $ 17 million
- Value available to Castor : $10.8 million
- Castor's exposure : 14.7 million

[1722] Vance, April 9, 2008, pp. 73-74
[1723] Vance, April 9, 2008, pp. 75-76
[1724] D-1312, ES-28; D-1312, p. 459

[1589] Goodman used the Juteau appraisal instead of the Fitzsimmons appraisal which was commissioned by a third party and which provided specific details of the renovation costs to achieve the proposed values, and even though C&L had relied on the Fitzsimmons appraisal for purposes of its 1989 audit.[1725]

Additional evidence specific to OSH

1989 events

[1590] From 1988 onwards, Prychidny expressed to Stolzenberg that the OSH was "worth nothing".[1726]

[1591] In 1989, there was not enough income to pay the rent to Campeau.[1727]

[1592] Campeau repeatedly sent letters of default to YHHL, Skyline (80) and Castor.[1728]

[1593] There was insufficient revenue to pay any of the interest to Castor, and all interest was capitalized.[1729]

[1594] As of December 1989, Wersebe and YH management respectively assessed the market value of the leasehold at $10 million[1730] and $15 million.[1731]

Loans as of December 31, 1989

[1595] As of December 31, 1989, the following amounts were owed to Castor in relation to the OSH:

- Loan 1049 to Skyline 80 - $10.6 million[1732]
- Loan 1152[1733] - $ 4 million[1734]

Interests recognised as revenue

[1596] $2,317,884.92 of capitalized interests were recognized as revenue in 1989.[1735]

[1725] PW-1053-19, sequential page 244
[1726] Prychidny, November 3, 2008, p. 40
[1727] Vance, April 9, 2008, pp. 64, 73
[1728] PW-450 series; Prychidny, October 15, 2008, pp. 145-153
[1729] PW-1097
[1730] PW-499C-1
[1731] PW-499
[1732] PW-1053-19, sequential pages 245-247
[1733] PW-452-1A; PW-1053-19, sequential page 99; PW-1053-15, sequential page 284
[1734] PW-2908, vol. 3, page 55; D-1312, p. 454
[1735] PW-1097

Conclusions

[1597] Vance's opinion prevails.

[1598] It is not reasonable to use the Fitzsimmons appraisal figures in the circumstances, as Goodman did.

[1599] Moreover, the analysis and conclusions expressed under the subheading OSH in the 1988 consolidated audited financial statements section of the present judgement apply *mutatis mutandis*.

TWTC

Additional evidence specific to TWTC

1989 events

[1600] Castor's exposure relating to loans secured through the TWTC project increased in 1989, from $47.7 million to $73.7 million.

[1601] 607670 Ontario Inc. ("**607670**") a wholly-owned subsidiary of CHL, acquired all of the shares of 696604 Ontario Ltd. ("**696604**") from Peter Luerssen, for $7,065,000.

[1602] 696604 owned 87 of the 213 units of the TWTCLP, which partnership had a 18.375% interest of the TWTC project. Therefore, through the transaction, CHL acquired a further 7.506% interest in the TWTC project.

[1603] As part of a loan to TWTCI, Castor was to obtain a legal opinion to the effect that the security had been duly executed and constituted a first charge on the borrowers' pledged assets.[1736]

[1604] In a legal opinion dated August 29, 1989, McLean & Kerr opined on the consents required for registration.[1737] It also described that in the event of a default, the co-owner could buy the co-ownership interest of York-Hannover at rebate. The co-ownership agreement between Camrost, YHDL and others clearly stipulated the aforesaid consequence of a default by a co-owner.[1738]

[1605] Castor was unsuccessful in having its security interest perfected.[1739]

[1606] In September 1989, Castor was informed that YH's 50% interest (assuming the exercise and payment of the option) would be $86.8 million for the land and 50% of the

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[1736] PW-1069-1.
[1737] PW-1069-5.
[1738] PW-1161-11.
[1739] PW-1069-6, PW-1069-7, PW-1069-12, PW-1069-14, PW-1069-15, PW-1069-16, PW-1161-16, PW-1161-17

condominium value of $ 69.9 million.[1740] YH estimated the net value of the three remaining office sites at $121 million based on a price of $100 per square foot.[1741]

[1607] Commenting the condominium net value of $ 69.9 million, Ron Smith indicated that they were merely "estimates" and that the «*profit numbers were pre-tax and, it should be noted that the profit is pledged towards the development of the office towers.*»[1742] Ron Smith concluded as follows:

> In conclusion, we should secure our position and attempt to get KVW to sell out and realize the present value of the project. While KVW maintains that each of the 3 development sites has potential for $30 to $40 million of additional profit, a lot of time, effort and strong equity support are required to get to this profit. It is a high risk scenario at this stage and I am not sure whether it is worth any more than what the present office pads are worth at present."[1743]

[1608] A value estimate as to the office tower lands was issued[1744] prior to Coldwell Banker being granted a mandate to sell such lands.

[1609] In December 1989, Coldwell Banker was mandated to attempt to sell the office tower lands for the sum of $145 million. Rapidly, it became apparent that such amount could and would not be achieved.[1745]

[1610] In a memo dated February 20, 1990, David Whiting reviewed the progress of the attempts to sell the land sites as discussed during a meeting that had taken place on February 8, 1990. Whiting wrote the following conclusion:[1746]

> The general view was that we had not given the agents sufficient time. Markborough wants equity financing which JLW can assist with after their current trip. We will get a further update on the international scene shortly. Markborough's price is unlikely to exceed $85 million. A development pro-forma, prepared jointly by the sales agents, is attached. The reduced value of $70sq/ft. to $90 sq/ft. is "explained" by Coldwell Banker as it being misinformed on the 40 Bay streat deal. They believe Trizec/Bramelea renegotiated down to the $100 sq/ft. range as well as different economic mood now from even late fall – soft landing has become doom and gloom.

[1740] PW-1069-8.
[1741] PW-1069-10
[1742] PW-1069-10.
[1743] PW-1069-10 ; see also Ron Smith, September 16, 2008, pp. 146-147
[1744] PW-1161-24; PW-1161-23; Whiting, December 9, 1999, p. 146-147.
[1745] PW-1161-30; PW-1161-31
[1746] PW-1161-31

Loans as of December 31, 1989

[1611] As of December 31. 1989, Castor's exposure for loans relating to the TWTC amounted to $ 73.7 million[1747] :

- Loan 1046 : $21 million[1748]
- Loan 1067 : $ 25.5 million[1749]
- Loan 1120/1149 : $12.3 million[1750]
- Loan 1090 : $ 6.5 million[1751]
- Investment in TWTCLP : $0.6 million
- Investment in 607670 Ontario Inc. : $7.1 million
- Accrued interests : $0.7 million

[1612] As of December 31, 1989, the security that Castor held for its loans was essentially a pledge of equity interests (as opposed to a mortgage on a property) which, altogether, represented a 43.75% interest in the TWTC's equity.[1752]

Experts' position

[1613] Vance did not recommend a LLP in the following circumstances:

> PW-1161-24, which is a value estimate of Phases I and II, was produced by David Whiting on December 9, 1999 from the boxes of the Trustee in Bankruptcy of York-Hannover Developments Ltd. This document was not available to C&L as it did not form part of the books and records of Castor. Had C&L made further inquiries in 1989 regarding the "offer" and determined the existence of this document, they would, in our opinion, have been justified in applying the provisions of section 5360 of the Handbook (PW-1419-2A) with respect to this estimate of value and only once these procedures would have been satisfactorily completed, the value estimate could then have been applied to the land sites with the result that a loan loss provision would not have been required. Consequently, owing to the uncertainty regarding the value of the land sites and whether this value could flow to castor, and as the financial statements were materially misstated and misleading because of other matters raised in this report, we have

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[1747] PW-2908, vol. II, pp. D-3 and D-4; D-1312, p. 210
[1748] PW-1053-19, sequential pages 93, 189-190
[1749] PW-1053-19, sequential pages 93, 191-192
[1750] PW-1053-19, sequential pages 93, 193-194
[1751] PW-1053-19, sequential page 98
[1752] Goodman, September 23, 2009, p. 180

no longer provided for a loss on the loans secured by the Toronto World Trade Center.[1753]

[1614] Rosen recommended a LLP based on different methodologies.[1754]

[1615] Goodman opined that the collateral security value supporting Castor's loans amounted to $104 million as at December 31, 1989 and that there was, therefore, a surplus of $30.3 million.[1755]

Conclusions

[1616] As proposed by Vance, the Court concludes that it could be that no LLP was required in relation to loans secured by the TWTC project in 1989.

[1617] However, the Court rejects Goodman's suggestion that there was a surplus available to Castor against which Castor could have cured deficiencies of other loans. In the circumstances above described, this suggestion does not hold water.

[1618] Moreover, the analysis and conclusions expressed under the subheading "TWTC" in the 1988 consolidated audited financial statements section of the present judgment apply *mutatis mutandis*.

Meadowlark

Additional evidence

1989 events

[1619] The situation did not improve in 1989.

[1620] The interests were capitalised 50%-50% in account 046 and under Raulino's grid note.[1756] The borrowers were not complying with their loan covenants.

[1621] In January 1989, Castor was informed by YH that BMO had transferred the first mortgage loan to its work out group. According to the assessment of YH, Meadowlark was «*in extreme danger of complete disaster*».[1757]

[1622] Castor continued to fund taxes owed by Meadowlark as well as operating expenses and mortgage payments to BMO.[1758]

[1753] PW-2908, vol. II, pp. D-14 and D-15
[1754] PW-3033, vol II, section E, pp. 21-31
[1755] D-1312, p. 214
[1756] PW-103, PW-1112G
[1757] PW-1112-10

[1623] Various letters of intent and offers received for Meadowlark fell short of the amount that would have been necessary for Castor to recover its loan : the amounts offered during 1989 varied from $10 million to $14.5 million.[1759]

[1624] As of December 31, 1989, an amount of $ 15.6 million was due to the BMO, the first mortgage creditor.

[1625] Castor recorded a LLP of $1.2 million in 1989.[1760]

Loans as of December 31, 1989

[1626] Castor's exposure to loans relating to the Meadowlark shopping center amounted to $ 8.3 million as of December 31, 1989.[1761]

- Loan 1030 : $ 7 million[1762]
- Loan 1117 : $0.6 million[1763]
- Amount receivable from 332756 Alberta : $ 0.6 million
- Accrued interest on Castor loans : $ 0.1 million[1764]

Interest recognized as revenue

[1627] The amount of $ 1,057,120.57 of interests was recognized in 1989 on the loans relating to Meadowlark.[1765]

Experts' positions

[1628] Rosen was the only expert mandated by the Plaintiff to opine on the Meadowlark project. He opined that a LLP was required for the total amount owed to Castor and that the revenue recognised should have been reversed.[1766]

[1629] Goodman opined there was a deficiency of only $0.7 million[1767] but to conclude accordingly, he assessed the value of the shopping center at $22 million and took account of the LLP of $1.2 million taken by Castor.

[1758] PW-1112-8B; PW-1112-12;
[1759] D-1002; D-1005; D-1194; D-1312, p. 254
[1760] PW-1053-19, sequential pages 88, 89,
[1761] D-1312, p. 259
[1762] PW-1053-19, sequential page 200 - 202
[1763] PW-1053-19, sequential pages 89, 95, 100
[1764] PW-1053-19, sequential page 200
[1765] PW-1112G
[1766] PW-3033, vol. II section F; PW-1112 G
[1767] D-1312, p. 259, 261

[1630] Goodman added that there was no need for a LLP because there were surpluses available elsewhere within the YH group to offset against the Meadowlark deficiency.[1768]

Conclusions

[1631] Rosen's opinion must prevail.

[1632] A LLP representing the total amount due to Castor should have been taken. Moreover, because there was clearly no reasonable assurance of the collectability of the interest on these loans, the amount of $1,057,120.57 of recognized interests should have been reversed in 1989.

[1633] The value of the Meadowlark shopping center was not and could not be $22 million. The appraisals of the Meadowlark shopping center were based on unrealistic occupancy levels which were not being met. The offers received during 1989 varied from $10 to $14.5 million, while the amount due to the first ranking creditor, BMO, was $15.6 million.

[1634] Leeds could not pay the amount of $ 0.6 million and Castor took a LLP. In those circumstances, Castor could not reasonably expect Leeds to be able to pay a greater amount of $ 7 million.

[1635] Moreover, Goodman's theory of surpluses available does not hold water taking into account Castor's own doings: Castor took a LLP of $1.2 million. On that topic of Goodman's theory of available surpluses, all previous comments made by the Court apply *mutatis mutandis*.

[1768] D-1312, p.261

1990 financial statements

Some specific facts of 1990

[1636] By year-end 1990, Castor needed to cover about $40M of accrued interest and other advances due by YH. C&L was clearly aware of the extent of interest capitalization.[1769]

[1637] The Canadian and the American economy entered into a recession: the Canadian economy went into recession in the second quarter of 1990 and the American economy followed in the third quarter of 1990.[1770]

Some figures and notes content of the 1990 statements

[1638] According to its balance sheet, Castor had:

- $1.689,973 of investments in mortgages, secured debentures and advances, as more fully disclosed in notes 2, 3, 4 and 10;
- $100 000 of liabilities through debentures, as more fully disclosed in note 6.

[1639] According to the consolidated net earnings statement, Castor's revenues for 1990 were $259,246 000, as more fully disclosed in note 9, and Castor's net earnings for 1990 were $31,200 000.

[1640] According to note 10 on related party transactions:

- secured debentures and advances due from shareholders in the amount of 16,101 000$ were included in investments, in mortgages, secured debentures and advances; and
- transactions during the year, and amounts due to or from shareholders and directors, not otherwise disclosed separately in the financial statements, were as follows:
    - accrued interests and other payables : $2,461 000
    - interest revenue : $1,332 000
    - other expenses: $380 000

[1769] PW-1053-87 sequential pages 32-33 – see also PW-1053-19, E-55A and E-59 (1989), PW-1053-3-1 and PW-1053-76-1 and Vance, March 10, 2008, pp.53 and following

[1770] D-1341, p. 16; Lapointe, October 13, 2009, pp.118-119, 137,

[1641] Notes 2, 3, 4, 6 and 9 read as follows:

2. Investments in mortgages, secured debentures and advances

The investments in mortgages, secured debentures and advances are in various currencies and bear interest at varying rates from 7 1/2% to Canadian bank prime rate plus 6% per annum and mature as follows:

	1990	1989
1990	-	1,055,702
1991	1,321,314	121,799
1992	181,800	84,253
1993	173,525	157,460
1994	12,550	4,416
1995 and subsequent years	784	421
	1,689,973	1,424,051

3. Notes payable

(a) These notes are payable in various currencies and bear interest at varying rates from 7 1/16% to 15 ¼% and mature as follows:

	1990	1989
1990	-	549,815
1991	689,616	24,500
1992	122,966	60,158
1994	11,000	11,000
	823,582	645,473

(b) Mortgages amounting to $240,806 have been pledged as security for secured notes payable totalling $244,115.

4. Bank Loans and advances

(a) Bank loans and advances consist of term loans and advances bearing interest at floating rates and varying fixed rates from 8 1/8% to 15 3/16% per annum.

(b) The term loans and advances mature as follows:

	1990	1989
1990	-	375,993
1991	519,713	104,124
1994	42,078	35,069
	561,791	515,186

(c) Mortgages amounting to $244,375 have been pledged as security for bank loans totalling $243,000.

6. Debentures

	1990	1989
	$	$
(a) Debentures maturing on June 30, 1997 bearing interest payable semi-annually at The Royal Bank of Canada prime rate plus 2 ¼% but not less than a minimum of 11% per annum. After June 30, 1992, the company has the right to prepay the principal amount..	50,000	50,000
(b) Debentures maturing on June 30, 2002 bearing interest payable semi-annually at The Royal Bank of Canada prime rate plus 2 3/8% but not less than a minimum of 11% per annum. After June 30, 1994, the company has the right to prepay the principal amount.	50,000	50,000
	100,000	100,000

9. Revenue

Details of revenue are as follows:

	1990	1989
	$	$
Interest	247,935	183,793
Commissions	11,086	13,579
Share of revenue from investments and joint ventures	225	339
	259,246	197,711

Materially misstated (1990)

[1642] The 1990 audited financial statements were materially misstated.

Absence of a SCFP showing the sources and uses of cash and cash equivalents

[1643] A SCFP was required: section 1540 and its italicized recommendations were clear.

[1644] The analysis developed and the conclusions enunciated in the 1988 and 1989 financial statements sections of this judgment apply *mutatis mutandis*.

Undisclosed related party transactions

[1645] No doubt related party transactions were undisclosed in the 1990 financial statements. The analysis developed and the conclusions enunciated in the 1988 and the 1989 financial statements sections of this judgment apply *mutatis mutandis*.

[1646] Above and beyond the situations discussed in the 1988 and the 1989 sections of this judgment, the transfer of CHL's loan 1049 to 687292 (which purchased YH's interest and debts in relation to the OSH) clearly constitutes an undisclosed related party transaction.

[1647] Prychidny testified that when the Skyline (80) interest was transferred to 687292, «*there was no resistence by either Mr. von Wersebe or David Whiting. It was actually a sense of relief I got from Mr. Whiting, because the transferring included a transfer of*

Castor debt ... so they were getting rid of, I guess you can say, a lease situation that couldn't pay the rent...».[1771]

[1648] 687292 was a Wost company. Its President was Stolzenberg and all ownership decisions were made by Stolzenberg.[1772] The public corporate records clearly indicated that Stolzenberg was a director and officer of this company.

Artificial improvements of liquidity and undisclosed restricted cash

[1649] Castor's liquidity was artificially improved in the 1990 consolidated audited financial statements as a result of the following elements:

- The maturities used in notes 2, 3 and 4;
- The 100 million debenture transaction;
- The undisclosed restricted cash in the amount of $58 million ($50 US).

Liquidity improvements (notes 2, 3 and 4)

Positions (in a nutshell)

Plaintiff

[1650] Plaintiff argues that:

- The Notes 2, 3 and 4 to the 1990 consolidated audited financial statements were materially misleading and disclosed a false picture of liquidity matching and solvency.
- The maturity notes conveyed to the reader that there was good maturity matching but in reality, it was the opposite. There was no reasonable expectation that the loans included as "current" would be, or could be, repaid during the current year.
- The maturity dates of various assets (loans receivable) and liabilities (loans payable) were altered during the audit; changes, unsupported by audit evidence, were accepted by C&L to the maturity dates. By advancing the due date of various receivables before their actual due dates and by extending the due date of various liabilities beyond their actual due dates, Castor improved its apparent liquidity position.

[1771] Prychidny, October 15, 2008, p. 156.

[1772] O'Connor, January 14, 2009, pp. 61-70, 79-80; R. Smith, September 5, 2008, p. 179; Prychidny, October 15, 2008, p. 157; PW-292.

Defendants

[1651] Defendants argue that:

- Plaintiffs' experts have misread the notes to the financial statements.
    - Vance and Rosen have asserted that these notes were misleading because they were possibly incorrect with respect to the amounts shown as maturing in future years, and because they misled the reader into believing that Castor was going to receive as much as 70-80% of its revenue in cash within the next year, whereas in reality, Castor's assets were not that liquid.
    - Rosen described the mismatch as being between long-term lending and short-term borrowing.
- Plaintiffs' experts are attempting to read something into the financial statement notes that is not there, nor required to be there. Rosen and Vance confused the concepts of "maturity" and "liquidity".
- Plaintiff failed to demonstrate that the disclosures as to contractual maturity dates made in the 1990 financial statements were not materially correct.

Maturity changes made in 1990

[1652] $98.8 million of maturity date changes were made by C&L in 1990[1773]. All changes concerned CHIF notes payable to Bristol and Tara. The maturity on the Bristol note in the amount of $ 87.7 million (£39,193,721) was changed from 1991 to 1992; the maturity on the Tara notes in the amount of $11 million was changed from 1991 to 1994.

Specific additional evidence

Bristol Note

[1653] The maturity listing showed the Bristol note to be maturing on March 31, 1991.[1774]

[1654] The photocopy of the confirmation letter contained in the files of C&L indicates a maturity date of March 31, 1991 and the signed confirmation[1775] by Bänziger on behalf of Bristol also includes a March 31, 1991 maturity date.

[1773] PW-1053-71-3
[1774] PW-1053-88-5, sequential page 100
[1775] PW- 1134, bates #2561

[1655] On working paper AA-51[1776], a notation is made that according to Mr. Gross, there were no long-term loans, other than the one to Hertel.

[1656] However, in a letter of February 8, 1990 requesting changes to maturity dates for the 1989 audited financial statements, Bänziger had stated that the Bristol deposit was connected to a receivable from Marketchief maturing only in 1992 and that, consequently, it could not be called for earlier.

Tara Notes

[1657] The inscription relating to the Tara notes in the maturity listing[1777] is 99.99.99, which indicates an amount without a fixed maturity date, and payable on demand.

[1658] The unsigned confirmation letter in respect of the Tara notes payable in the file of C&L[1778] indicates a maturity date of 31.12.90, the fiscal year-end.

[1659] Throughout the Tara deposit folders, starting from the inception of the deposits, all documentation refers to "call deposits", deposits due on demand.

[1660] Gross observed that the Tara notes that he was shown were not drawn in the usual Castor format[1779].

Experts' opinions

[1661] Vance opined that C&L should not have accepted the changes since no corroborative audit evidence supported the reclassification of the maturity dates, while the evidence obtained supported the original maturity dates.

[1662] In the Bristol case, Selman opined that the available agreements were not sufficiently unclear[1780] for C&L to require a legal opinion before accepting the right to offset.

[1663] In the case of the Tara notes, unless the notes shown to Gross were not signed notes in the hands of the White[1781], Selman was not prepared to accept that their 1994 maturity dates were wrong.

Conclusions

[1664] Given Castor's global situation, including the purposes and the content of notes 2, 3 and 4, Vance's opinions prevail. The analysis developed and the conclusions

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[1776] part of PW-1053-88-4
[1777] PW-1053-88-5, sequential page 116
[1778] PW-1053- 82-1
[1779] Gross, pp.588-590
[1780] PW-2214-A and PW-2115
[1781] D-327 and D-329

enunciated on this topic in the 1988 and 1989 financial statements sections of this judgment apply *mutatis mutandis*.

Liquidity improvements (100 million debentures)

[1665] In 1990, Stolzenberg signed the confirmation letter to C&L for the Morocco loan and on behalf of Morocco.

[1666] The analysis developed and the conclusions enunciated on this topic in the 1988 and 1989 financial statements sections of this judgment apply *mutatis mutandis*.

Undisclosed restricted cash

[1667] Castor had an unclassified balance sheet in its 1990 financial statements which included the heading "*Cash in bank and short-term deposits*".

[1668] GAAP required that «*cash subject to restrictions that prevent its use for current purposes*» be excluded from current assets.[1782]

[1669] Without any note disclosure, a reader of the financial statements would assume that the amount shown under the heading "*Cash in bank and short-term deposits*" was all available and usable for general purposes[1783]. It was not the case.

Positions (in a nutshell)

Plaintiff

[1670] Plaintiff argues that $58 million ($50 US) of restricted cash resulted from the transactions that took place at year-end involving CHIF, Fitam and two branches of Bank Gotthard and should have been disclosed as such in the consolidated audited financial statements.

Defendants

[1671] If the Court finds there was a valid pledge in place at December 31, 1990, Defendants agree it should have been disclosed.

[1672] However, Defendants allege that the circumstances of this pledge were unusual and lead to a serious doubt as to whether it was valid and in place as at December 31, 1990 or whether it was back-dated.

- It appears that Gambazzi signed the document on Castor's behalf, which is very unusual. Although he frequently signed on behalf of Castor's customers, he did

[1782] PW-1419-2, section 3000 "cash"
[1783] PW-1419-2, section 3000; Vance, March 13, 2008, p.29.

not have signing authority for commitments of this nature, nor was he a recognized signatory for the transactions between Castor and Bank Gotthard generally[1784].

- The ostensible authorization for this transaction is not found in a Board resolution, but in a December 24, 1990 letter to Bank Gotthard in Lugano, signed by Stolzenberg alone, purporting to give Gambazzi the authority to sign on behalf of both CHIFNV and Castor[1785].

- Confirmation replies signed by two vice-presidents from Bank Gotthard in Nassau and in Lugano do not refer to a pledge[1786].

Additional evidence relating to restricted cash in 1990

[1673] In late 1990, Castor deposited $50 million with Bank Gotthard at its Nassau branch. A General Pledge and Assignment with respect to US$50 million of cash was signed to secure a loan made by Bank Gotthard to Fitam Établissement[1787], a company controlled by Marco Gambazzi[1788].This pledge was not found in Castor's records but it was obtained through an examination on discovery in the Bank Gotthard's file[1789].

[1674] In a letter dated December 24, 1990 addressed to Bank Gotthard in Lugano and signed by Stolzenberg, Castor confirmed Gambazzi's authority to sign on behalf of both CHIF and Castor.[1790]

[1675] Gambazzi remembered he had met with Mordasini from Bank Gotthard.[1791]

[1676] Only 2 persons had the authority to sign on behalf of Fitam Établissement: Gambazzi and his employee Conti.[1792]

[1677] Gambazzi acknowledged that a loan agreement between Bank Gotthard and Fitam, for the amount of US$50 million and dated December 24, 1990, had been signed by his employee Conti[1793] on behalf of Fitam.

[1678] At the beginning, Gambazzi was denying that the signature on the pledge, on behalf of CHIF, was his signature,[1794] but he became doubtful as counsel was showing

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[1784] D-659 (re: 4.5.10.17) A
[1785] D-659-1 (re 4.5.10.17) B)
[1786] PW-1134 bates 2523 and APG-5-27B
[1787] PW-1053-87-23-1
[1788] Gambazzi, February 26, 1996, p.109
[1789] Gourdeau, Jan. 31, 2008, p. 43-47; Vance, June 6, 2008, p. 68-69;
[1790] D-659-1 (re 4.5.10.17B)
[1791] Gambazzi, February 10, 1998, p.216
[1792] Gambazzi, February, 26, 1996, p.111 ; Gambazzi, February 10, 1998, p.223
[1793] Gambazzi, February 10, 1998, pp.217-218
[1794] Gambazzi, February 10, 1998, pp.218-219

him further documents. He even said "*Il est possible que ce soit la mienne*" and "*Ça ressemble à la photocopie de ma signature ça, il n'y a pas de doute* »[1795]. Denial of signature by Gambazzi is found neither credible nor reliable.

[1679] Gambazzi signed a confirmation on behalf of Fitam that there was a US$ 50 million deposit of Fitam with CHIF.[1796]

[1680] Confirmation requests were sent to both branches of Bank Gotthard, Lugano and Nassau. Replies were signed by two vice-presidents from Bank Gotthard, one in Nassau and one in Lugano[1797]. The confirmation form sent to Nassau was a statement of open position. The vice-president of the Nassau branch confirmed that the information appearing on the statement of open position was accurate, but he did not refer to a pledge since it was not mentioned and since he was not required to set out any pledge or encumbrances on the deposits held by the Bank.[1798]

[1681] On January 28, 1991, the US$ 50 million deposit was cashed and used by CHIF to repay Fitam.

Experts' evidence

[1682] Vance opined there was a misstatement as a result of the non-disclosure of restricted cash in the amount of US$ 50 million. Vance explained that C&L should have been able to determine that said cash was restricted if they had followed proper audit procedures, controlled the confirmation process and sent a proper bank confirmation form.[1799]

[1683] In his report, Defendants' expert Selman described the transaction as follows:

> «In my view, the transaction has all the earmarks of a classic instance of window dressing – to show an improved cash position by borrowing and holding the loan proceeds as cash on deposit.»[1800]

[1684] Selman opined that if a pledge was in force on December 31, 1990, there was a restriction on the cash on deposit at the Nassau branch of Bank Gotthard which should have been noted in the consolidated audited financial statements of Castor.[1801]

[1685] Defendants' expert Levi agreed that there were a misstatement and a disclosure failure with respect to Bank Gotthard,[1802] and concluded that the failure to disclose same resulted in the financial statements being misleading[1803].

[1795] Gambazzi, February 10, 1998, pp. 219-225
[1796] PW-1134, bates 2533
[1797] PW-1134 Bates 2523 and APG-5-27B
[1798] PW-1134 Bates 2523
[1799] PW-2908, Vol. 1, p. 6-32; Vance, March 13, 2008, pp. 46-47, 59-61
[1800] D-1295, p. 340, para. 6.12.24.
[1801] D-1295, p. 340, paragraph 6.12.25

[1686] Levi takes the position that the bank acted to conspire with Stolzenberg to inflate the cash position at year-end 1990 with the intent «*to deceive the investors as well as the auditors*» because it failed to confirm to the auditors that the funds were restricted.[1804]

[1687] As admitted by Levi, the effect of undisclosed restricted cash would be to artificially improve the liquidity position of Castor, a matter which «*would be of utmost importance to investors and creditors*».[1805]

Conclusions

[1688] The Court concludes that Gambazzi signed a pledge on behalf of Castor to the benefit of Bank Gotthard and that such pledge was in place as of December 31, 1990.

[1689] The US$50 million pledged by Castor to secure a loan by Bank Gotthard to Fitam[1806] was restricted cash and had to be disclosed as such on Castor's audited financial statements for 1990.

[1690] This transaction artificially inflated Castor's cash position as at December 31, 1990 and constituted a material misstatement.

Undisclosed Capitalised interest and inappropriate revenue recognition

[1691] In its 1990 brochure, Castor described its business in the same fashion as it had during the previous years.[1807] In reality, Castor's business was quite different.

[1692] The books and records provided to C&L, in Montreal and overseas, again disclosed the nature of Castor's loans and the fact that very little cash – if virtually no cash – was being paid by Castor's borrowers.

[1693] Again in 1990, a huge amount of capitalized interest was unplanned capitalized interest further to non-compliance with loan covenants which were nevertheless recognized as revenue.

[1694] The analysis developed and the conclusions enunciated on this topic in the 1988 financial statements section of this judgment apply *mutatis mutandis*.

[1695] Disclosure of capitalization of interest should have taken place and a huge amount of capitalized interest should not have been recognized as revenue.

[1802] Levi, January 28, 2010, pp. 38–39; February 2, 2010, p. 97.
[1803] Levi. January 28, 2010, pp. 37-38.
[1804] D-1347, pp. 181–182.
[1805] D-1347, p. 170.
[1806] PW-1053-87-23-1.
[1807] PW-1057-3

Understatement of LLP and overstatement of carrying value of Castor's loan portfolio and equity

[1696] In 1990, Castor represented a carrying value of loans (investments in mortgages, secured debentures and advances) of $1,689, 973 in its audited financial statements: it represented that the figure of $1,689, 973 was the lower of estimated realizable value and cost.

[1697] At December 31, 1990, could the carrying value of loans, at the lower of estimated realizable value and cost, be $1.689, 973 or an amount close enough to $1,689, 973 to avoid a material misstatement?

[1698] The obvious conclusion is that it could not be, taking into account the facts as they unfolded, as they shall be viewed and analyzed in the context of the relationships that existed between Castor and YH and Castor and DT Smith.

[1699] Assessing the exact quantum of any LLP that might have been required for 1990 is neither achievable nor necessary. This litigation is not about what the precise content Castor's financial statements for 1990 should have been – it is about whether or not C&L's 1990 audited financial statements of Castor presented fairly the financial position of Castor in accordance with GAAP, as they purported to do.

Positions in a nutshell

[1700] Plaintiff and Defendants positions, summed-up in the 1988 audited financial statements section of the present judgment, apply *mutatis mutandis*.

[1701] Plaintiff argues that a minimum LLP of $331.5 million[1808] should have been taken.

[1702] Plaintiff argues that it was clear and known to Castor and to C&L that the Canadian and American economies were at least going through a slowdown, if not a recession. Plaintiff adds that Castor and C&L had to take that factor into account to properly assess LLPs.

[1703] Defendants argue that there was no need for a LLP.

[1704] Defendants add that one needs to be very careful not to use hindsight to assess the 1990 situation. They plead that it was neither known to Castor and to C&L nor forecasted by them that the Canadian and the American economies were in recession in 1990. At best, Castor and C&L felt there was a temporary slowdown. They maintain that the market turned only in 1991.[1809]

[1808] This is the lowest figure mentioned by Froese while his proposed LLP (mi-point) is in the amount of $382.7 million – see PW-2941-4

[1809] Defendants' written submission July 8, 2010, pp.205-208

Experts' figures

[1705] Taking into account an amount of 7.7 million of LLP recognized by Castor, Vance proposes a total minimum LLP of $454.8 million. His total figure of $462.5 million (before LLP recognized by Castor) breaks down as follows[1810]:

Project/Category	Vance's proposed minimum LLP
MLV	73 million
YH Corporate loans including the "nasty nine"	165.8 million
MEC	65 million
TSH	51.5 million
CSH	32 million
OSH	19.2 million
DT Smith	56 million

[1706] Vance also mentions that his LLP would have been reduced to $328.3 million if the capitalized interest and placement fee revenue, in the amount of $126.5 million, had been reversed.[1811]

[1810] PW-2908, volume 1, page S-10
[1811] PW-2908, volume 1, page S-10

[1707] Rosen proposes LLP ranges between $ 447 million and $ 672 million, breaking down as follows[1812]:

Project/Category	Approach A - Low	Approach A- High	Approach B- Low	Approach B- High
MLV	75.7 million	94.2 million	115 million	115 million
YH Corporate loans including the "nasty nine"	171 million	210 million	171 million	210 million
MEC	67.1 million	84.1 million	143.1 million	147.8 million
TSH	43.3 million	51.3 million	63.3 million	71.3 million
CSH	22.8 million	33.4 million	34.8 million	45.4 million
TWTC	62 million	78 million	62 million	78 million
Meadowlark	5 million	5 million	5 million	5 million

[1708] Froese proposes LLP ranged between $331.5 million and $433.9 million, breaking down as follows[1813]:

Project/Category	Low	High
MLV	62.1 million	62.1 million
YH Corporate loans	90 million	96.1 million
The "Nasty nine"	40 million	40 million
MEC	14.9 million	74.5 million
CSH	21.2 million	36.1 million
TSH	57.8 million	76.1 million
DT Smith	45.5 million	49 million

[1812] PW-3033, volume 2
[1813] PW-2941-4; PW-2941, volume 1, p. 25

[1709] Goodman opines that no LLP was needed.

[1710] Goodman applied his 5 step methodology (previously described).

[1711] Again, the more serious dispute between Plaintiff's' experts and Goodman is with respect to the value used for step 1 and the proper application of step 5 under GAAP, given Castor's reality and the realities of Castor's borrowers.

Evidence – State of the Canadian and the American economies at the end of 1990

[1712] Defendants presented expert evidence on this topic through their expert witness Alain Lapointe ("**Lapointe**"). Plaintiff cross-examined Lapointe and elected not to call an expert witness in rebuttal.

Lapointe

Who's who

[1713] In 1967, Lapointe obtained a Bachelor's degree in economics from Laval University. In 1969, he obtained a Master's degree in economics from the same University.[1814]

[1714] In 1971, Lapointe obtained a Master's degree in economic science from Harvard.[1815]

[1715] In 1978, Lapointe obtained a Doctorate in economic science from the University of Toulouse, France.[1816]

[1716] From 1978 onwards and until he retired from teaching in 2006, Lapointe occupied various teaching positions with various universities and business schools.[1817]

[1717] During his career, Lapointe has been consulted by various companies and institutions on various topics relating to the economy.[1818]

[1718] Lapointe has published numerous articles, research and books relating to economy and he has been invited as speaker at numerous professional events.[1819]

[1719] However, before he was asked by Defendants to opine in this case, Lapointe had never acted as an expert witness on the topic of the economic environment of the real estate market in Canada during the relevant years (1988, 1989 and 1990).[1820]

[1814] D-1342, p.1
[1815] D-1342, p. 1
[1816] D-1342, p. 1
[1817] D-1342, pp. 1-2
[1818] D-1342, pp. 2-5
[1819] D-1342, pp. 5-12

Objections and judgement rendered on December 7, 2009

[1720] On October 13, 2009, further to representations made by counsel for the Plaintiff and for the Defendants, and subject to the "objection sous réserve # 84", the Court authorized Lapointe to express opinions as follows during his testimony:

> Communiquer dans le cadre de son témoignage des avis relativement à l'évolution historique et à l'environnement macroéconomique du marché immobilier pour les années 1985 à 1992, et plus spécialement pour les années 1990 et 1991, début de l'année, et à présenter les prévisions des analystes sur l'économie et le marché immobilier pour cette même période.[1821]

[1721] On October 13, 2009, Plaintiff's counsel objected to a part of Lapointe's written report and the objection was noted as "objection sous reserve # 85".[1822]

[1722] On December 7, 2009, the Court rendered judgment on these two objections.

- Objection sous réserve # 84 was maintained in part and Lapointe was not allowed to opine on the Castor Bankruptcy and its causes.[1823]
- Objection sous réserve # 85 was maintained in part the contested extract of the written report not being in evidence for the purpose of establishing a comparison between Castor's situation and what other institutions did in 1992.[1824]

Expert Evidence

[1723] Lapointe's knowledge of the actual evidence before this Court and of Castor's business and affairs during the relevant years (1988, 1989 and 1990) is very limited.[1825]

[1724] Lapointe testified that Canada had gone through an exceptional period of growth that lasted seven years (1983-1989) after the recession of 1981-1982 and before the recession of 1990-1991.[1826] During that seven year period, investments in real estate were stimulated by an exceptional increase in a demand for space and high expectations with respect to inflation and appreciation of property values.

[1725] Lapointe opined that most of the analysts and economists did not anticipate the 1990-1991 recession. At most, said Lapointe, they foresaw a slowdown or slackening of

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[1820] Lapointe, October 13, 2009, pp.50-51
[1821] Transcription October 13, 2009, p.98
[1822] Transcription, October 13, 2009, pp. 100-107
[1823] Trial minutes of December 7, 2009 and transcription of December 7, 2009, pp.12-13; see also trial minutes and transcription of October 13, 2009
[1824] Trial minutes of December 7, 2009 and transcription of December 7, 2009, pp. 12-13 ; see also trial minutes and transcription of October 13, 2009
[1825] Lapointe, October 13, 2009, pp. 51 and following
[1826] Lapointe, October 13, 2009, p. 136

economic activity which, for many, was to have been of short duration and followed by a rapid return to a situation of strong growth.

[1726] Lapointe wrote that analysts had not foreseen the seriousness of the real estate crisis that took place at the beginning of the 90s.[1827] The confidence of consumers remained very high until 1988 while the unemployment rate and interest rates were in a state of reduction or decrease. Afterwards, the index started to diminish to reach in 1990 its lowest level since the 1982 recession. Even though the confidence of consumers diminished, Lapointe said that of the business sector remained high.[1828]

[1727] Concerning the Canadian economy, Lapointe opined that there was generally an underestimate of growth in a period where there was growth of economic activity and an overestimate in a period of slowdown. [1829] He based his comments on review and combination of the following information:

- The December economic forecast for the following year covering a dozen Canadian organisms published by the newspaper La Presse.
- The January forecast of the Canadian Business Review further to its own investigation covering on average some fifteen organisms.

[1728] In the October 1990 edition of its publication, the Conference Board recognized that the Canadian economy was in recession.[1830]

[1729] Lapointe testified that the real estate market is influenced by general economic conditions.

[1730] Lapointe explained that during the greatest part of the 80s, property values in Canada were positively influenced by the flow of capital coming from foreign investors and institutions such as insurance companies and pension funds. Real estate was perceived as a long-term investment which permitted a matching of assets to long-term liabilities.[1831]

[1731] After a period of growth, the value of properties reduced substantially in all categories of real estate but particularly for office space, mixed occupancy and hotels.[1832]

[1827] D-1341, p. 4
[1828] D-1341, pp. 11-12
[1829] D-1341, pp. 13-15
[1830] D-1341, p. 17
[1831] D-1341, p. 24
[1832] D-1341, p. 26

[1732] Lapointe commented specific real estate markets of Montreal, Toronto, Calgary and Vancouver.

Toronto

The values of properties constantly progressed and peaked in 1989-1990. Thereafter, they gradually lowered as of the second quarter of 1990.[1833]

Montreal

The Montreal market generally followed the pattern of the Toronto market, but the ups and downs were less pronounced. There was progressive plus-value gains between 1985 and 1990 but in the second quarter of 1990, the values started to fall.[1834]

Calgary

The behaviour of the Alberta market differed considerably from that observed in Quebec and Ontario. Economic activity, as a whole, was closely tied in to the performance of the gas and oil sector where prices fell sharply until 1986. Large companies had to restructure themselves which resulted in massive lay-offs with the consequence that real estate property values decreased until 1991.[1835]

Vancouver

The value of properties in British Columbia suffered the same fate as that observed in Ontario and Quebec but it was less pronounced and with some delay. Values progressed until 1990 and the decreases observed subsequently were relatively modest.[1836]

[1733] In cross-examination, Lapointe acknowledged that he had not considered the quality and other characteristics of the Castor properties and he reiterated that he was not opining on their values.[1837]

[1734] Lapointe acknowledged that the C&L publication dated February 3, 1988[1838] constituted a warning to all C&L professionals, a certain form of needed conservatism.[1839]

[1833] D-1341, p. 28
[1834] D-1341, p. 31
[1835] D-1341, p. 34
[1836] D-1341, p. 36
[1837] Lapointe, October 14, 2009, pp.7 and following
[1838] PW-1420-1D
[1839] Lapointe, October 14, 2009, pp. 18 and following

[1735] Lapointe admitted that C&L were economic observers after being asked to look at another C&L publication to all professionals, exhibit PW-1420 (T&T 155) dated July 23, 1990, where they had written:

> "Realizable values for real estate have dropped sharply in many areas of the country over the last several months. In many cases, this represents the reversal of a boom market and affect both (inaudible) values and the values for developed real estate whether intended for a resale or as a revenue producing properties. The real estate market problem affects not only developers and other direct investors in real estate, but also those who have made loans secured by real estate, those who have made loans to enterprises whose principal assets are real estate and those who are holding real estate as a result of default on loans.
>
> This is a time to be careful and conservative in assessing real estate values. One (1) of the lessons of the mil neuf cent quatrevingt- deux (1982) - mil neuf cent quatre-vingt-cinq (1985) (sic) real estate market was that it is difficult for investors and creditors to accept not only that values are depressed but that they could go even lower.

[1736] Lapointe also acknowledged that the tool he had used, the Russell index, was essentially composed of first quality properties ("*propriétés institutionnelles*") which might not be affected in a recession scenario as negatively as other kinds of properties.[1840]

[1737] Lapointe was shown a third document prepared by C&L for the benefit of all its professionals, exhibit PW-1420 (AM-50) dated December 31, 1982 and revised on December 12, 1990, and was asked if its content made him change or qualify the views he had previously expressed. In said exhibit, C&L had written the following:

> 1. Economic conditions similar to those that arose in 1982 are again having significant impact on the real estate industry. (...) In this environment, several areas of accounting and financial statements disclosure should be carefully considered in all assignment where real estate investments are significant.
>
> 2. This memorandum discusses the valuation issues associated with real estate investment and the generally accepted accounting principles that must be now applied to this area.

[1840] Lapointe, October 14, 2009, pp. 29-30

[1738] Lapointe answered that the document had no impact on his expert report or comments but he added in the same sentence that at the end of 1990 it was quite clear that Canada was in a recession. Lapointe testified in French and his specific words were the following:

> Non, ça change pas mon expertise et le sens de mon expertise. On fait référence à la situation de quatrevingt-deux ('82). Et comme je vous mentionnais tout à l'heure, la récession de quatre-vingt-deux ('82)... quatre-vingt ('80) - quatre-vingt-deux ('82) était plus sévère que celle de quatre-vingt-dix ('90) - quatre-vingt-onze ('91). Et révisé en décembre... au douze (12) décembre, c'est que déjà le douze (12) décembre on a une bonne idée... Vous savez que la récession de quatre-vingt-dix ('90) - quatre-vingt-onze ('91) a débuté au deuxième trimestre de quatre-vingt-dix ('90). Et à la fin de quatre-vingt-dix ('90), on sait... on a une bonne idée que le Canada est en récession.
>
> Alors donc, c'est de règles de prudence vis-à-vis des vérificateurs... qu'on distribue aux vérificateurs des compagnies.[1841]

[1739] In cross-examination, Lapointe was also shown a memorandum signed by Whiting, dated September 11, 1990 concerning the fair market value of the MEC and where Whiting had written to Wersebe the following[1842]:

> I have no certainty of any buyers interested in the property at any price, let alone this value range. The uncertainties in the marketplace, the recession with the retail and real estate sectors already hard hit. Interest rates, political stability will have an impact.[1843]

[1740] Lapointe acknowledged that his report and comments were based on the information that had been available to him, namely the Russell index, and that they had to be looked at and taken for what they were, nothing else.[1844]

[1741] Lapointe was also shown the following noted comment from Goulakos in C&L's audit working papers of 1990 (dated February 2, 1991) :[1845]

> "As per S. Goulakos, the increase in rates is due to the deterioration of the economy over the past year and the difficulty faced by the real estate market."[1846]

[1841] Lapointe, October 14, 2009, pp.35-36
[1842] Lapointe, October 14, 2009, pp.37-39
[1843] PW-1159-6
[1844] Lapointe, October 14, 2009, pp.39-40, pp. 43 and following
[1845] Lapointe, October 14, 2009, p. 40
[1846] PW-1053-13, sequential page 222

[1742] Lapointe agreed that there had been a deterioration of the economy, as Goulakos had said, and a recession in Canada since the second quarter of 1990.[1847] Lapointe acknowledged that the situation of the properties that were part of the Russell index could be quite different from the situation of the Castor properties.[1848]

[1743] In cross-examination, Lapointe was shown various articles and publications of 1990 and he admitted that analysts and economists had anticipated the recession.[1849]

[1744] Finally, Lapointe said he had not looked at the specific market of hotel properties where he could however attest that there had been a serious crisis from 1988 onwards.[1850]

Lay witness evidence

[1745] Prychidny testified namely of the following in relation to the actual economic situation surrounding the hotel properties financed by Castor:

- Asked to describe the general state of affairs of the Skyline hotels (Toronto, Calgary and Ottawa) and of the MLV complex in the fall of 1990, Prychidny said :

> **Topven Holdings or the Skyline Airport** was incurring significant operating loses to the tune of ten (10) million dollars or more during that period of time. Again, with respect to... they're still having problem meeting certain obligations and payments that are summarized in this memorandum as well. So there's cash flow reporting to Castor Holdings at that particular time indicating that Topven Holdings and Skyline Airport **still needed cash to survive**.
>
> **The Skyline Calgary**, at that time, again **the market was turning to even, you know, worst than nineteen eighty-nine (1989)**. So, again, it's experiencing larger amounting losses during the year nineteen eighty-nine (1989) and nineteen ninety (1990). And it still required the financial support with respect to paying ongoing expenses as well as paying the interest coverage that existed on that entity.
>
> **The Skyline Ottawa** I guess it's **the same story**, it's just a continuing **spiral in losses in this case as well.** The lease was still outstanding. And actually, at that point in time, the consideration was to purchase the interest from Campeau Holdings and that was being conducted by George Dragonas on behalf of Mr. Stolzenberg during this period of time. As we

[1847] Lapointe, October 14, 2009, p.41
[1848] Lapointe, october 14, 2009, pp. 41 and following
[1849] PW-3073, PW-3074, PW-3075, PW-3076
[1850] Lapointe, October 14, 2009, p.74

> referred to earlier, the lease as it existed in its current state was uneconomical, it produced annual operating losses. So the plan would be to have Castor related entity or Stolzenberg related entity approach Campeau with a view of acquiring the real estate associated with that property.
>
> **Maple Leave Village** we continued our attempts to try to sell the hotel at that particular time. But again, at this point in time, there is monthly... Castor had control of the bank situations, signing cheques and there was, again, **constant call for cash with respect to property tax arrears and ongoing operating expenses**. [1851] (our emphasis)

- Asked to describe the economic environment of 1990, Prychidny made the following comments:

> The reality in nineteen ninety (1990) is the market was in fact turning[1852]
>
> In June of nineteen ninety (1990), the barn... the horse had left the barn. We were in a downturn at that particular time, so there was no positive feedback that I was able to receive to present actual... an offer to Stolzenberg for that particular... during that June of nineteen ninety (1990) to September ninety-one ('91). (...)There was more interest in the eighty-eight ('88) years, as opposed to the later years.[1853]
>
> the context of this one arrived in June of nineteen eighty-five (1985), it was obvious that the hotels were over leverage, that we went through eighty-five ('85), eighty-six ('86), eighty-seven ('87), was the last year that you'll see any audit done in our groups... ... so it was obviously if the owners of York-Hannover cannot support it, the only strategy would be potentially to sell the hotels, since they weren't being supported and renovated by the current owners and/or lenders.
>
> Nineteen eighty-eight (1988) was the best year, we've talked about that in the market, so I was... I was pushing to actually sell the hotels during nineteen eighty-eight (1988) in some form or fashion because it was going, the hotels were already losing thirty (30) to forty (40) million dollars a year in aggregate. So to continue on didn't make sense, so we have to look at the exit strategies to sell, and that form is a genesis of these discussions.

[1851] Prychidny, October 14, 2008, pp.238-239
[1852] Prychidny, October 15, 2008, p.22
[1853] Prychidny, November 3, 2008, pp.270-271

> Well, the approach, the critical approach that you'll see in going through here nineteen eighty-eight (1988) was Von Wersebe's sale and leaseback, he was adamant on the leaseback proposal which, in my opinion, didn't make sense, one because of the terms he wanted and he wanted the Skyline brand, he didn't want the York-Hannover Hotels to manage.
>
> These are a series of properties, if you look back, have underperformed because of York-Hannover, because of that minding, because of so many things. So going forward is obvious that Von Wersebe wasn't really a player with the team to say, yes, let's set the hotel and put it in new hands of a new (inaudible) position.
>
> That, and he also had his minimax concept, as we discussed earlier in our testimony as well, which is a Von Wersebe operating strategy, which encompassed taking the fruit... just concentrating York-Hannover just do the rooms, and actually sever the food and beverage operations and give that to a third-party operator.
>
> We tried it, it didn't work. To this day that concept doesn't exist with any hotel, service hotel, company, it didn't make sense, it was impractical. So our efforts in sale were hampered by one, his adamancy on the leaseback scenario, his adamancy on maintaining the Skyline brand and pushing this minimax concept that try and get for six (6) months, it didn't work and it never did work, I thought we should get out of that and on to something different. (...)
>
> So that hampered the strategy going forward.[1854]

> Not appreciably largely related to the timing, we're now at the end of nineteen eighty-nine (1989), we missed the market going into ninety ('90), it got worse, so I'd have to say timing is one or time frame is one category, how it categorizes to get your high value; another one is market conditions, the peak is gone (...).[1855]

[1746] Regarding the actual economic situation of 1990 surrounding some of the properties financed by Castor, Ron Smith testified as follows:

- The economy in California and the DT Smith projects:

> I was aware of the market conditions as a result of visiting the projects, as a result of various information provided by various

[1854] Prychidny, November 4, 2008, pp.75-77
[1855] Prychidny, November 4, 2008, pp.244-245

publications in Southern California which were sent to our offices and with meetings that we held with the D.T. Smith representatives and others in Southern California. (...)

The R word was the short name for "recession" and that was starting... they hadn't hit by then but by August of nineteen ninety (1990), the economy in California was starting to go sideways and there was talk that they were heading towards a recessionary period.[1856]

the prices were starting to increase dramatically, but particularly from nineteen eighty-five (1985) onwards, and prices... we noted that prices peaked in late eighty-nine ('89) for the projects that we were working on and started to go... softened in early nineteen ninety (1990) and as well construction activity was slowing down at that point in time as well. So it is an accurate statement that we noted in our projects as well.[1857]

that was happening in all of the D.T. Smith projects through to early nineteen ninety (1990) and it actually led to the point where we had to entertain voluntary auctions in all of the construction loan projects in the fall of nineteen ninety (1990) in order to stimulate the sales of the properties.[1858]

we'd had a very strong price rise all the way through the nineteen eighty-nine (1989), by the third quarter, all of a sudden we noticed that it just had peaked and in nineteen ninety (1990), it was going sideways, and then in the late nineteen ninety (1990), it started to actually slide downwards.[1859]

By nineteen ninety (1990), really, the market had shifted on us.[1860]

[1856] Ron Smith, June 10, 2008, pp. 46-47; see also exhibit PW-1113F
[1857] Ron Smith, June 10, 2008, p. 48
[1858] Ron Smith, June 10, 2008, p. 49
[1859] Ron Smith, June 10, 2008, p.62
[1860] Ron Smith, June 11, 2008, p.10

- the MEC project and its opening in November 1990:

> The tragedy of it all is that the market was changing on us in nineteen ninety (1990) and the project finally opened up in a very difficult retail market, such that not only did we miss the fall and a good part of the Christmas market for nineteen ninety (1990), we also opened up in a period where the retail market was crumbling on us, and instead of opening up with about eighty percent (80%) occupancy, we ended up opening only with about a sixty-seven percent (67%) occupancy and a lot of turmoil with the various tenants that were supposed to occupy the project. So, the delays not only cost more for the project in cost overruns, it ate up all of the forty-two (42) million dollars bonus that we thought we were going to get from the pad, and it delayed the opening of the project such that the project opened up in probably the most disadvantaged time that it could open up, and unfortunately, it never recovered from that while I was employed with Castor.[1861]

- the TWTC project and its condominium portion:

> But in nineteen ninety (1990), the market turned a bit and some of the condo purchasers started to renegotiate their positions. And that's when the market started to turn a bit on the condos.

[1747] Simon said:

> Well, nineteen ninety (1990), there was, you know, some developments in the Canadian economy, real estate, markets, both in some areas of Canada and some areas of the United States were experiencing some setbacks,[1862]

[1748] Numerous publications were expressing concerns about a slowdown or a recession, either in Canada or in the State of California.[1863]

[1861] Ron Smith, September 15, 2008, pp.122-123
[1862] Simon, April, 27, 2009, p.130
[1863] See the Wells Fargo Economic Monitor (August 7, 1990 - PW-1113F; November 14, 1990 – PW-1113H; February 14, 1991 – PW-1113I); PW-2908, volume 2, p. H-57; Lapointe, D-1341

C&L minimal knowledge as of December 31, 1990

[1749] In relation to the actual economic situation of 1990 and to their work as auditors for 1990, and as it appears from C&L's own professional material, from their audit working papers of 1990 or from the valuation letters they issued, C&L knew that :

- Realizable values for real estate had dropped sharply in many areas of the country over the months preceding July 23, 1990.[1864]
- This real estate market problem affected not only developers and other direct investors in real estate, but also those who had made loans secured by real estate, those who had made loans to enterprises whose principal assets were real estate and those who were holding real estate as a result of default on loans.[1865]
- There had been a slowdown in the real estate market of North America.[1866]
- Economic conditions similar to those that had arisen in 1982 were again having significant impact on the real estate industry.[1867]
- It was difficult for investors and creditors to accept not only that values were depressed but that they could go even lower.[1868]
- They should not underestimate the pressures on companies to stretch earnings or report a favourable financial condition particularly in light of the current credit crunch.[1869]
- It was of first importance to obtain sufficient appropriate audit evidence, not to "*audit by conversation*" and to exercise sufficient professional skepticism. They had to step back and ask themselves "*Does it make sense?*[1870]
- They were alerted to pitfalls:
    - They were asked to make sure receivables that were supported by real estate as collateral reflected the softening of the market. [1871]

[1864] PW-1420 (T&T 155) dated July 23, 1990
[1865] PW-1420 (T&T 155) dated July 23, 1990
[1866] PW-6-1 (C&L valuation letter dated September 28, 1990)
[1867] PW-1420 (AM-50) dated December 31, 1982 and revised on December 12, 1990; see also PW-1053-13, sequential page 222
[1868] PW-1420 (T&T 155) dated July 23, 1990
[1869] PW-1420 (T&T 163) dated January 30, 1991
[1870] PW-1420 (T&T 163) dated January 30, 1991
[1871] PW-1420 (T&T 163) dated January 30, 1991

- They were told that increases in the allowance for non-collectibles may be needed. [1872]

- They were asked to maintain an attitude of objectivity and professional skepticism and not to assume that the accounts or the client explanations were right.[1873]

- They were told to question, to challenge and to compare new information with what was already known about the client and its business in general.[1874]

- Several areas of accounting and financial statements disclosure had to be carefully considered in all assignments where real estate investments were significant.[1875]

- It was time to be careful and conservative in assessing real estate values.[1876]

Road map

[1750] The loans looked at by experts are largely the same but Plaintiff's experts and Goodman used different groupings depending on the conclusions they reached as to the ownership of some properties or entities.

[1751] The discussion of the LLP issue is done, in light of the burden of proof that rests on Plaintiff, by using Plaintiff experts' groupings and the following sub-headings: MLV, YH Corporate loans, MEC, TSH, CSH, OSH, TWTC, Meadowlark and DT Smith.

MLV

Experts' positions

[1752] Plaintiff's experts opined that a LLP was required for MLV in 1990 and they proposed the following minimum LLP:

- Vance : $73 million[1877]
- Froese : $62.1 million[1878]
- Rosen: a range of $75.7 million to $115 million[1879]

[1872] PW-1420 (T&T 163) dated January 30, 1991
[1873] PW-1420 (T&T 163) dated January 30, 1991
[1874] PW-1420 (T&T 163) dated January 30, 1991
[1875] PW-1420 (AM-50) dated December 31, 1982 and revised on December 12, 1990
[1876] PW-1420 (T&T 155) dated July 23, 1990
[1877] PW-2908
[1878] PW-2941-4

[1753] Vance opined that the total value used to assess the MLV project should not have been more than $93.7 million including the hotels value figure of $ 67.7 million and the mall and amusement park figure of $26 million.[1880]

[1754] For his LLP, Vance used that figure of $93.7 million. However, he mentioned that an appraisal dated January 14, 1991 by Lincoln North & Company Limited ("**Lincoln**")[1881] had established the mall and amusement park value between $2.4 and $4 million only. Therefore, using the Lincoln appraisal would have brought down the total value of the entire project at $70 million.

[1755] Froese used the total value figure of $101.6 million: $67.7 million for the hotels, $ 26 million for the mall and amusement park, $1.476 million for current assets and $6.46 million for the amusement park rides.[1882]

[1756] Rosen took into account the information hereinabove mentioned and discussed by Vance.[1883]

[1757] Goodman used a total value of $141.7 million, which included a value of $40 million for the mall and the amusement park land, a value of $104 million for the hotels and the wax museum and a value of $6.5 million for the amusement park rides.[1884]

[1758] Goodman assessed the prior ranking creditors Great-West Life and National Bank at $24.9 million and Castor's exposure at $134 million.[1885]

[1759] Goodman calculated a deficiency of $26 million,[1886] but he opined that no LLP was needed for MLV. He even said that neither Castor nor C&L should have recognized a $5 million LLP on MLV as they did.[1887]

Additional evidence specific to MLV

[1760] Late in 1989, FICAN had commenced judicial proceedings before the Superior court of Ontario to appoint a receiver to the MLV project.[1888] FICAN had asked C&L Toronto to act as the receiver for the project.[1889]

[1879] PW-3033, vol.2
[1880] PW-2908, vol. II, p. A-35
[1881] PW-1129
[1882] PW-2941-4
[1883] PW-3033, vol. 2, Appendix D
[1884] D-1312, p. 351
[1885] D-132, p. 351
[1886] D-1312, p. 351
[1887] Goodman, October 9, 2009, pp.14, 205-210
[1888] PW-1070F-18A; PW-2845
[1889] Ron. Smith, May 15, 2008, p. 245; May 16, 2008, pp. 36 and following; PW-1070F-18A

[1761] Castor intervened and settled the situation with FICAN.[1890] Castor' exposure to MLV increased. Castor even paid the account sent by C&L to FICAN for services rendered in connection with "*professional services rendered with respect to the Bank's position with regard to Maple Leaf in the amount of $2,855*".[1891]

[1762] The operations of MLV continued to encounter serious financial difficulties and the survival of the MLV project was wholly dependent on Castor's ongoing financial support.[1892]

[1763] Again, the terms and conditions of the commitment letters and extension letters as well as the loan documentation in connection therewith called for the payment of monthly interest, annual fees and the supply of financial information. The borrowers were in chronic breach of all of such covenants.

[1764] Castor consulted its lawyers for information on the process it would have to follow should it wish to appoint a receiver and manager to the assets and undertakings of MLVII.[1893]

[1765] By the end of 1990, the connection that was one of the main assumptions of the 1989 Jones McKittrick appraisal relating to the Mall had not yet been constructed.

[1766] As at December 31, 1990, MLVII's 1990 financial statements disclosed accounts payable of $ 3.9 million and bank indebtedness of $ 5.8 million. Note 3 to the financial statements provided the following details of mortgages and loans payable provided by third parties and of a receivable from and a payable to YHDL:

Loans payable provided by third parties:

- National Bank (1st mortgage) : $15.74 million
- Fican : $2.73 million
- Great-West Life (1st mortgage) : $ 9.45 million
- Capital leases: $ 1.85 million.[1894]

Receivable from and payable to YHDL:

- A receivable from shareholder of $33.473 million, offset by a payable to YHLP of $38.603 million (a net payable of $ 5.2 million).[1895]

[1890] PW-1077-A
[1891] Ron Smith, May 16, 2008, p.45
[1892] See PW-1070F and PW-1070G
[1893] PW-490
[1894] PW-478I

[1767] Castor recorded a $5 million allowance for loan losses in relation to its exposure to MLV. In their audit working papers, C&L wrote "*C&L considers that an additional reserve could be in order for that project*".[1896]

[1768] In its Montreal audit planning memo for the 1990 audit, C&L identified MLV as an audit concern.[1897]

[1769] The completed questionnaires indicated that interest and repayment terms were being met even though the loan covenants called for payment of interest and interest was capitalized.[1898]

[1770] The staff member who did the investment section of CHL wrote in his MLV loan notes "*client did not allow C&L to photocopy MLV inc. F/S as at Dec 31/12/90.* [1899] He, however, traced to the client's copy and reproduced some numbers of those financial statements, namely:

- The MTG and loans for 1990 of $36.3 million
- The bank indebtedness for 1990 of $5.8 million
- The account payable and accrued liabilities for 1990 at $3.9 million
- The 1988 accumulated deficit of $3.3 million and the net loss for 1988 of $4.27 million
- The 1989 accumulated deficit of 6.9 million and the net loss for 1989 of $3.34 million
- The 1990 accumulated deficit of $11.5 million and the net loss for 1990 of $4.78 million[1900]

[1771] The loan information questionnaires ("**LIQ**") in C&L's working papers (relating to CHL) showed Castor's evaluation of a number of MLV loans as being "*high risk nature*".[1901]

[1895] PW-478I
[1896] PW-1053-15-10, sequential page
[1897] PW-1053-16, sequential pages 260 and 267
[1898] PW-1053-15-2, PW-1053-15-12
[1899] PW-1053-15, sequential page 161
[1900] PW-1053-15, sequential pages 161-162
[1901] PW-1053-15, sequential pages 138, 140, 142, 144, 146, 148, 150, 152,154, 156, 158, 160

[1772] Under the subheading "*auditor's additional comments*", on one of the Loan Evaluation Questionnaires ("**LEQ**") relating to MLV, C&L wrote:

> Conclusion
>
> Client view this loan as a high risk nature but took a reserve a 5M$. C&L considers this loan to be still risky after recording the reserve (...)[1902]

[1773] Quesnel, the senior auditor responsible for the investment section in the 1990 CHL audit, namely wrote the following in his AWPs, on page E-65b:

> MLVII (Maple Leaf Village)
>
> As per E 90 last appraisal done in 89 was below Total loan value by ~2 400 000$
>
> C&L considers that an additional reserve could be in order for that project. [1903]

[1774] To say the least, the overseas working papers relating to MLV are incomplete.[1904] The following annotations are written relating to loans and to increase in loans:

> Dr. Marco Gambazzi sign all documents in trust for: Runaldi, Trade Retriever, Charbocean[1905]
>
> *Castor Mtl interest*, *NV Interest* and *Commission*[1906]

[1775] At the year-end meeting with Wightman, Stolzenberg agreed to place loans to borrowers connected to the MLV project on a non-accrual basis effective January 1, 1991.[1907]

[1776] In his handwritten notes from his year-end meeting with Stolzenberg, Wightman inscribed the following:

> The margin on this loan is very thin and W.O.S. has undertaken to do the following ion 1991:
>
> 1. Capitalize no more interest or fully reserve
>
> 2. Create additional reserves of no less than 1% above this year and above capitalized interest.
>
> 3. Aggressively pursue the sale of part or all of position"[1908]

[1902] PW-1053-15, sequential page 160
[1903] PW-1053-15, sequential page 128
[1904] PW-2908, vol. 2, pp. A-31 and A-32
[1905] P-1053-87-2 (B39)
[1906] PW-1053-87-2 (B40)
[1907] PW-1053-12, sequential page 76

Loans as of December 31, 1990

[1777] At the end of 1990, Castor's total exposure was in excess of $ 130 million.[1909]

Owed to CHL

- Loan 1105 to MLVII: $6.4 million[1910]
- Loan 1126 to MVII : $4.8 million[1911]
- Loan 1136 (re Fican) : $6 million[1912]
- Loan 1048 to YHLP : $14 million[1913]
- Loan 1125 to KVWI: $7.2 million[1914]
- Loan 1011: $3 million[1915]
- Loan 1012: $2 million[1916]
- Loan 1013: $4 million[1917]
- Loan 1014: $7.5 million[1918]
- Loan 1015: $5 million[1919]
- Loan 1016: $2.4 million[1920]
- Loan 1017: $3 million[1921]
- Loan 1018: $2.3 million[1922]
- Loan 1019: $ 2.2 million[1923]

[1908] PW-1053-12, sequential page 76
[1909] Ron Smith, May 15, 2008, p. 204
[1910] PW-1053-15, sequential pages 155-156
[1911] PW-1053-15, sequential pages 157-158
[1912] PW-1053-15, sequential page 134
[1913] PW-1053-15, sequential pages 163-164
[1914] PW-1053-15, sequential pages 258-259
[1915] PW-1053-15, sequential pages 137-138
[1916] PW-1053-15, sequential pages 139-140
[1917] PW-1053-15, sequential pages 141-142
[1918] PW-1053-15, sequential pages 143-144
[1919] PW-1053-15, sequential pages 145-146
[1920] PW-1053-15, sequential pages 147-148
[1921] PW-1053-15, sequential pages 149-150
[1922] PW-1053-15, sequential pages 151-152

Owed to CHIF

- Loan 770001/0009 to Runaldri – 5.4 million [1924]
- Loan 26100/0004 to Charbocean Trading – 10.8 million [1925]
- Loan 385005/3010 to Gebau Overseas - 11.9 million[1926]
- Loan 385009/3005 to Gebau Overseas –3.3 million[1927]
- Loan 385009/0003 to Gebau Overseas – 6.1 million[1928]
- Loan 38500/0008 to Gebau Overseas – 0.9 million[1929]
- Loan 38500/0004 to Gebau Overseas – 4.7 million[1930]
- Loan 441004/3010 to Harling International – 5 million[1931]
- Loan 441004/0008 to Harling International – 12.1million[1932]
- Loan 890000/0010 to Trade Retriever – 7.5 million[1933]
- Loan MLV Treasury – (6 million)[1934]

Revenue recognition – capitalized interest

[1778] Castor recognized $10,550,803.20 of capitalized interest as revenue.[1935]

Conclusions

[1779] Taking into account the state of the Canadian economy at the end of 1990, the history of the MLV project and the additional facts of 1990, it is obvious that the value figures mentioned by Plaintiff's experts were the value that C&L had to use to comply with GAAP.

[1923] PW-1053-15, sequential pages 153-154
[1924] PW-1053-87, sequential pages 32, 126, 135-136, 143-147
[1925] PW-1053-87, sequential pages 32, 126, 135-136, 143-147
[1926] PW-1053-87, sequential pages 32, 126, 135-136, 143-147
[1927] PW-1053-87, sequential pages 32, 126, 135-136, 143-147
[1928] PW-1053-87, sequential pages 32, 126, 135-136, 143-147
[1929] PW-1053-87, sequential pages 32, 126, 135-136, 143-147
[1930] PW-1053-87, sequential pages 32, 126, 135-136, 143-147
[1931] PW-1053-87, sequential pages 32, 126, 135-136, 143-147
[1932] PW-1053-87, sequential pages 32, 126, 135-136, 143-147
[1933] PW-1053-87, sequential pages 32, 126, 135-136, 143-147
[1934] PW-1053-87, sequential pages 32, 126, 135-136, 143-147
[1935] PW-1075A

[1780] Had Goodman used those values instead of the ones he took into account, he would have come to a deficiency of at least $66 million, [1936] very comparable to the ones calculated by Plaintiff's experts.

[1781] Conclusions reached under the subheadings MLV of the 1988 and the 1989 financial statements sections of this judgment apply *mutatis mutandis*.

YH Corporate loans (excluding the "Nasty nine loans")

[1782] The loans which are part of the YH Corporate loans for 1990, which are looked at by Plaintiff's experts, are those described under the subheading "YH Corporate loans" of the 1988 and 1989 financial statements sections of this judgment.

[1783] As it appears from his report, Rosen looked at loans[1937] that neither Vance nor Froese looked at, which fact explains the difference between their respective suggested minimum LLPs.

Experts 'positions

[1784] All Plaintiff experts opined that huge LLPs were required for 1990.

- Vance: $125.8 million[1938]
- Froese : $90 to $96.1 million[1939]
- Rosen: $131 to $170 million[1940]

[1785] Goodman opined that no LLPs were required.

Events of 1990

[1786] In a letter dated January 25, 1990, from Wersebe to Ron Smith, Wersebe set out his guarantees included in commitment letters to Castor as follows:

- $10 million in connection with an increase of a loan elated to MEC;
- $10 million in connection with an increase in the KVWI loan facility;
- $6.125 million in relation to a loan facility to YHDL.[1941]

[1936] his deficiency of $26 million plus the difference between his total value ($141 million) and Froese's total value ($101 million)
[1937] Namely In 1990 : $24.3 million of loans to Harling made by CHIF
[1938] PW-2908, vol. III, section 2, page 7
[1939] PW-2941-4
[1940] PW-3033, vol.2, section C, pages 3 and 4

[1787] In the same letter, Wersebe requested that Castor confirm that :

- The personal guarantees would be released on or before April 30,1990.
- They would not be enforced before April 30.
- They would be executed by him only after review by legal counsel and receipt of his opinion that the limitations and release provisions noted were satisfactory in form and substance.[1942]

[1788] A commitment letter dated March 16, 1990, related to Castor loan 1137 to YHHHL included a personal guarantee of Wersebe "*limited to his interest in the shares owned of the Borrower*".[1943]

[1789] YHDL prepared a "pro forma Balance sheet", as of September 30, 1990 and dated January 25, 1991.[1944] In said pro forma Balance sheet:

- YHDL assumed the sale of MEC for an amount equal to its debts.
- The receivables from parent/affiliates that had grown to $196,557,000 were eliminated, namely through write-offs of $80.7 million.

[1790] YHDL issued unaudited consolidated financial statements as at September 30, 1990.[1945]

[1791] A commitment letter dated October 22, 1990, related to Castor's loan 1081 to YHDHL included, under the security subheading, "*personal guarantee of Karsten von Wersebe to remain at $15 million.*"[1946]

[1792] A commitment letter dated December 6, 1990 related to Castor's loan 1123 to KVWI described the security as "*personal guarantee of Karsten von Wersebe remains at $12.5 million*".[1947]

[1793] KVWI issued unaudited financial statements as of August 31, 1990[1948], which showed that its deficit had increased to $70.5 million from a deficit of $ 41.1 million as at August 31, 1989. In note 5 of these financial statements, KVWI explained as follows why it had included advances from subsidiaries in equity rather than as liabilities:

[1941] D-215-2-A
[1942] D-215-2-A
[1943] PW-1062-3
[1944] PW-1171-1
[1945] PW-1137-5
[1946] PW-1054-15
[1947] PW-1058-7
[1948] PW-1136-5A

> Advances from subsidiary companies are unsecured, bear interest at rates depending on prime and are without specific terms of repayment. In the absence of the ability to repay or refinance these advances, they have been characterized as a component of capital although no formal plan exits to implement reciprocal shareholdings.[1949]

[1794] During 1990, KVWI assumed the YH $20 million loans to CFAG.

[1795] There were only three loans receivable recorded in the financial statements of CFAG at December 31, 1990 amounting to an aggregate of $20,910,000. Confirmation requests were sent out and received by C&L for the two loans totalling $910,000. In C&L's overseas AWPs, there is the following notation under CFAG "*KVWI- no confirmation sent*".[1950]

[1796] No financial statements were available for YHLP for the year ended December 31, 1990.

[1797] Froese evaluated the combined deficit of KVWI, YHDHL and YHLP at approximately $185.5 million as of December 31, 1990.[1951]

Loans as of December 31, 1990

[1798] As of December 31, 1990, Castor's exposure to YH Corporate loans amounted to at least $ 109.6 million (in relation to the following loans):

- Loan 1081 to YHDHL : $35 million[1952]
- Loan 1137 to YHHHL : $10 million[1953]
- Loan 1123 to KVWI : $27 million[1954]
- Loan 1092: $10.1 million[1955]
- Loan 1090: $ 7.5 million[1956]
- Loan 1153: $ 0.466 million[1957]
- CFAG loan (158504) : $20 million[1958]

[1949] PW-1136-5A
[1950] PW-1053-71-6, sequential page 165
[1951] PW-2941, vol.4, page 47, paragraph 2.129
[1952] PW-1053-15, sequential pages 232-233
[1953] PW-1053-15, sequential pages 296-297
[1954] PW-1053-15, sequential pages 260-261
[1955] PW-1053-15, sequential pages 230-231
[1956] PW-1053-15, sequential pages 228-229
[1957] PW-167 and PW-2941, vol. 4, pp. 31-32, paragraph 2.82

Conclusions

[1799] All the comments made under the subheading "YH Corporate loans" in the 1988 and 1989 financial statements sections of this judgment apply *mutatis mutandis*.

[1800] As of December 31, 1990, Wersebe's guarantees were limited to $12.5 million for loan 1123, $15 million for loan 1081 and to value of shares for loan 1137. In all cases, they were limited to Wersebe's interests in North America.

[1801] The events that took place during 1990 strengthen again, as did the 1989 events, the conclusion regarding the personal guarantees granted by Wersebe: they were worthless to Castor in that they were limited to Wersebe's interests in entities, which were fully leveraged and insolvent.

[1802] Plaintiff experts' opinions must prevail: a huge LLP in relation to the YH Corporate loans was required in 1990.

The "Nasty nine"

Events of 1990

[1803] Evidently, at the end of 1990, growth in security values in the existing YH projects could not support the additional 1990 YH debt.

[1804] Reallocation to existing projects was unthinkable.

[1805] Annual restructuring negotiations with YH ensued, with Castor attempting to secure Wersebe's guarantee. As of December 31, 1990, those negotiations were unsuccessful.

[1806] Castor had to deal with $40 million of interest that had accrued on various YHDL loans. It reallocated that $40 million into nine new loans to companies that were incorporated or taken off the shelf at Castor's request by McLean & Kerr.[1959]

1958

[1959] See the testimony of Alksnis

[1807] In late December 1990, Castor disbursed funds to McLean & Kerr[1960] as follows: $10 million on each of December 18 and 19, $8.2 million on December 27, and $11.8 million on December 28. These funds were returned to Castor and recorded as payments of interest, fees and principal on various loans.[1961] All of these transactions were recorded in Castor's accounting books and records.

[1808] The payments to McLean & Kerr and related cash received from McLean & Kerr were recorded by Castor as follows:[1962]

Castor's disbursements ($40 million)		
Date	Borrower and loan number	Amount
Dec. 18, 1990	Loan 1173-Bioworld Holdings	$5,000,000
Dec. 18, 1990	Loan 1174–Canont Holdings	$5,000,000
Dec. 19, 1990	Loan 1172–Blacking Holdings	$4,800,000
Dec. 19, 1990	Loan 1171–Farl Properties	$5,200,000
Dec. 27, 1990	Loan 1168–Ptero Holdings	$3,800,000
Dec. 27, 1990	Loan 1167–Pustul Properties	$4,400,000
Dec. 28, 1990	Loan 1176-Serotine	$4,200,000
Dec. 28, 1990	Loan 1169–Truncal Holdings	$3,600,000
Dec. 28, 1990	Loan 1175–Tesia Holdings	$4,000,000

[1960] PW-1056D-1A; PW-1056D-7; PW-1056D-1-T; PW-1056D-1C and PW-1056D-1D.
[1961] PW-1056D
[1962] PW-1056-D

Castor Receipts ($40 million)			
Date	Loan number	Debtor	Amount
Dec. 18, 1990	Loan 1153	YHDL	$484,450
Dec. 18, 1990	Loan 1081	YHDHL	$7,719,927
Dec. 18, 1990	Loan 1125	KVWI	$1,504,247
Dec. 18, 1990	Loan 1022	223356	$291,376
Dec. 19, 1990	Loan 1153	YHDL	$7,974,126
Dec. 19, 1990	Loan 1123	KVWI	2,025,874
Dec. 27, 1990	Loan 1153	YHDL	4,067,994
Dec. 27, 1990	Loan 1123	KVWI	3,682,679
Dec. 28, 1990	Loan 1153	YHDL	12,249,327

[1809] McLean and Kerr received no communication and no instructions from YHDL, Wersebe or Whiting.[1963] All instructions came from Castor.[1964]

[1810] The companies were incorporated and the transactions documented by Castor's lawyers and under exclusive instructions from Castor while negotiations were taking place with Wersebe.[1965]

[1811] No negotiations took place with YH as to the content of the commitment letters (amounts, interest rates, etc.).[1966]

[1812] Castor did not want Whiting to intervene on this situation before an agreement had been reached with YH and Wersebe:

> And the reason that Mr. Dragonas wanted that idea was that he was worried about Mr. Whiting holding him up at the audit confirmation process, that Mr. Whiting would seek extra concessions from Castor Holdings when we went to get

[1963] Alksnis, February, 7, 2006, pp.181-182; Alksnis, February 8, 2006, p.66
[1964] Alksnis, February, 7, 2006, pp.181-182; Alksnis, February 8, 2006, pp.80, 84, 89, 106, 107-109, 165
[1965] Ron Smith, September 17, 2008, pp.8-10, 169-170, 202-
[1966] Ron Smith, September 17, 2008, p. 212

those audit confirmations signed by Mr. Whiting. And, secondly, that he thought that Mr. Whiting would not sign off on those loans and that he would, you know, try to negotiate other positions.

So, Mr. Dragonas decided on the five (5)-million dollar positions. And that's the instructions I got was then to book the nine (9) different loans.[1967]

The reason why they were put with a different ownership was not to go to Mr. Whiting, it was to go around Mr. Whiting.[1968]

[1813] No further money was advanced to the YH group.[1969]

[1814] Negotiations between Castor and YH were on-going.

The decision was made to put them outside of it, out of Mr. Whiting's area of control and to keep negotiating with Mr. Whiting and Mr. Von Wersebe as to where it was going to end up.

Whether it was going to end up and parked in the York-Hannover empire with Raulino Canada or Raulino offshore or with Mr. Von Wersebe or any of his other companies or whatever guarantees he was going to get, those negotiations were ongoing.[1970]

[1815] As of December 31, 1990, nothing had been agreed to between Castor, YH and Wersebe. Castor did not have Wersebe's guarantees for the $40 million.

Q- And would you also agree that, by the end of nineteen ninety (1990), Mr. Von Wersebe was still bucking at providing his personal guarantee for the reallocations?

A- Yes, that was quite evident in the negotiations of the nine companies, Mr. Dragonas made it very clear to us that he did not have the guarantee of Mr. Von Wersebe at that point in time.[1971]

Q- So at the year-end, as I understand it, you still did not have Mr. Von Wersebe's agreement to provide a guarantee for any of that forty (40) million dollars, is that correct?

A- That's what Mr. Dragonas informed me.[1972]

[1967] Ron Smith, September 17, 2008, p. 206
[1968] Ron Smith, September 17, 2008, p. 208
[1969] Alksnis, February 8, 2006, p.86
[1970] Ron Smith, September 17, 2008, p. 207
[1971] Ron Smith, September 22, 2008, p. 70 (see also p. 93)

[1816] Promissory notes and guarantees were prepared by McLean & Kerr sometimes in January 1991, probably close to January 24, 1991.[1973]

[1817] Promissory notes and commitment letters were signed by three lawyers of the firm of McLean and Kerr: Harold Blake, Christine Renaud and Soo Kim Lee.[1974]

[1818] On February 11, 1991, Stolzenberg sent to Alksnis, in draft form and for comments, a letter he was planning to send to Wersebe.[1975]

[1819] On February 12, 1991, Ron Smith met with the audit staff member of C&L, who was handling the investment section. At that date, Smith "*didn't know where the loans are going to end up, whose guarantees we were going to get and I did not indicate that they were tied to York- Hannover or Mr. Von Wersebe.*"[1976]

[1820] Before the audit came to an end, Ron Smith was never told that Wersebe would have signed guarantees for the $40 million. The first time he heard about the fact that some guarantees would have been signed was some time after the audit, from Dragonas.

> I was advised sometime after the audit by Mr. Dragonas that the guarantees had come in, **that Mr. Wightman had been advised that the guarantees had been obtained.** I never saw the documentation package, actually, until... I'd believe it was nineteen ninety-two (1992).[1977] (our emphasis)

[1821] Mackay, who had to deal with the interests to be paid on these nine loans, sustained that he was never made aware that YH or Wersebe was responsible.

> So just to summarize, you weren't aware yourself of any evidence that the loans were collectible?
>
> A- That the loans were collectible? At the time, in ninety ('90) and ninety-one ('91), I didn't know what... how the loans would be worked out to the future. I mean, I didn't know... Like these were loans made as they were and I know the identity of the borrower, okay, obviously, but they were just nine (9) loans picked and names picked. And the ultimate collection of those loans, as I understood it, would have been a York-Hannover workout later on where they would have realized on those loans.
>
> And, that was it.[1978]

[1972] Ron Smith, September 22, 2008, p. 96
[1973] Alksnis, February 8, 2006, p.66, 70, 141-143
[1974] See their testimonies which are in evidence before the Court : Blake,June 18, 2009; Renaud, January 26, 2006; Lee, January 25, 2006.
[1975] Alksnis, February 8, 2006, pp. 143-148;
[1976] Ron Smith, September 22, 2008, p. 136
[1977] Ron Smith, September 22, 2008, pp. 124-125
[1978] Mackay, August 26, 2009, pp. 186-187

[1822] Before he was shown some documents during his examination in 2006, Alksnis, the partner responsible for the Castor files at McLean & Kerr, had never seen personal guarantees signed by Wersebe in relation to these nine loans.[1979]

[1823] From the available evidence, and as of February 15, 1991, the Court finds that Castor had not obtained Wersebe's guarantee.

[1824] Eventually, Wersebe distanced himself from these loans.[1980]

[1825] None of the Nasty Nine loans were selected by C&L for confirmation. As a matter of fact, no unsecured loans appear to have been selected for confirmation.[1981]

[1826] C&L were told that these loans represented new business opportunities with people known to Castor. C&L were told that the loans were unsecured.[1982]

[1827] The loan files for the nine loans disclosed minimal documentation, with no evidence to support the ultimate collectability of the loans.[1983]

[1828] The loan commitment letters for the nine loans disclosed that:

- the borrowers had some addresses in common;
- three persons signed as borrower representatives for the nine loans;
- some of the borrowers had addresses that were not consistent with the address of the person signing for the loan.[1984]

[1829] Letters dated February 7, 1991 were sent by Castor to Harold J. Blake, Christine Renaud and Soo Kim Lee requesting them to sign, as authorized signing officers, the loan commitments and promissory notes.[1985]

[1979] Alksnis, February 8, 2006, pp.137-138, 141
[1980] Alksnis, February 8, 2006, pp. 91-92, 96
[1981] PW-1053-15, sequential pages 13 and 134
[1982] PW-1053-15, sequential pages 130-131 (see also Quesnel's transcription)
[1983] See the "red files" relating to PW-1064-1 to PW-1064-9
[1984] PW-1064-1 to PW-1064-9;
[1985] PW-1064-1-D-1; PW-1064-2-D-1; PW-1064-3-D-1; PW-1064-4-D-1; PW-1064-5-D-1; PW-1064-6-D-1; PW-1064-7-D-1; PW-1064-8-D-1; PW-1064-9-D-1

[1830] The loan files disclosed the following borrower addresses and borrower signatures:

Name of borrower	Borrower's address	Borrower's signature
Truncal Holdings Ltd.	McLean & Kerr / Toronto	Christine Renaud
Farl Properties Ltd.	McLean & Kerr / Toronto	Soo Kim Lee
Bioworld Holdings	Gravenor Keenan / Montreal	Harold J. Blake
Tesia Holdings Ltd.	Gravenor Keenan / Montreal	Christine Renaud
Pustul Properties Ltd.	Gravenor Keenan / Montreal	Soo Kim Lee
Blacking Holdings Ltd.	Gary Cooper / Edmonton	Harold J. Blake
Serotine Developments	Gary Cooper / Edmonton	Christine Renaud
Ptero Holdings Ltd.	KHB Investments Ltd. / Toronto	Soo Kim Lee
Canont Holdings Ltd.	Wolfgang Kyser / Toronto	Harold J. Blake

[1831] The result was that Castor's loans were increased on its balance sheet by $40 million and accrued and unpaid capitalized interest was reduced on the balance sheet by $40 million.

[1832] The official corporation's records of the nine entities, produced by Defendants and which include various official stamps of reception, namely as of February 21, 1991, establish that Wersebe's name was neither mentioned nor publicized.[1986]

[1986] PW-1064-1-3 (see stamp on page 51); PW-1064-2-3 (see stamp on page 53) ; PW-1064-3-6 (see stamp on page 52); PW-1064-4-3 (see stamp on page 52); PW-1064-5-5 (see stamp on page 53); PW-1064-6-4 (see stamp on page 53) ; PW-1064-7-3 (see stamp on page 53); PW-1064-8-3 (see stamp on page 52) and PW-1064-9-3 (see stamp on page 57)

[1833] Quesnel, the senior auditor responsible for the investment section in the 1990 audit, namely wrote the following in his AWPs:

- On page E-65b:[1987]

  Doubtful accounts (as per C&L)

  For which no reserve was taken in 1990 or reserve was not enough (as per C&L)

  See list (next page) of all the loans only secured by Prom note (no MTG as collateral)

  Those loans represent ~ 17.5% (133 m$) of total loans as at Dec 31, 1990 (760m$). 40M$ of that amount was lended in the last ~ 20 days of December.

- On page E-65c:[1988]

  - That the total of loan unsecured was of $133 416 051.
  - That the unsecured loans represented 17.5%.
  - That $40 million of unsecured loans, representing 5%, had been issued in December 1990.

- On pages E-65d and E-65e

  Mr. Smith was asked about all the loans with only a prom Note as collateral: all the ones who were issued before december 1990 are operating line of credit loans, mostly, with companies who also have other loans secured by MTG with CHL. So CHL investment are secured by the fact that client won't take any chances regarding the unsecured loans because of MTG on other loans with CHL regarding the same properties.[1989]

  For all the loans secured only by Prom note and issued in December 1990,Mr. Smith said that:

  -loans only given to companies that have already done business with CHL (they know those companies very well)

  -loans will serve as a starting point for a business investment. Those companies will eventually need (in the near future) additional loan. CHL will renegotiate the agreement and loans should be secured by MTG."

[1987] PW-1053-15, sequential page 128
[1988] PW-1053-15, sequential page 129
[1989] PW-1053-15, sequential page 130

- On page E-134:

  Note: C&L expresses uncertainty over nature of collateral (prom note for the same $ as loan) [1990]

[1834] Quesnel, who prepared the working papers E-65b and E-65c, described as follows the circumstances surrounding those inscriptions:

> Q.-Décembre '90, une flèche. Ce sont les neuf (9) prêts, si je comprends bien, qui ont été faits à la fin de l'année 1990, est-ce que c'est exact?
>
> R La colonne, le petit signe comptable indique que ces prêts-là ont été émis en décembre '90.
>
> Et pourquoi avez-vous noté le fait que neuf (9) prêts ont été émis à la fin de l'année? Quel était le but de cette indication? /
>
> Le but, en tant que tel, c'est simplement que ces prêts-là ont été émis vers la fin de l'année '90, et j'avais noté, à l'époque, ces prêts-là, initialement, comme vous constatez, c'est tous des prêts dont l'ordre de grandeur est moindre que certains qu'on a regardés depuis le tout début, il y en a certains de quarante millions ($40,000,000), cinquante millions ($50,000,000) un peu arrondis, là. Ces prêts l'ordre était d'un ordre de grandeur moindre, mais j'avais constaté, à l' époque, il y a presque cinq (5) ans, que tous ces prêts-là avaient été émis sur une période de temps, bon, peut-être deux (2) semaines, si on peut – pour parler d'une façon comme ça , à la fin de l'exercice '90:
>
> J'avais tout simplement rempli certaines - fait un certain travail, rempli certaines feuilles dans le dossier parce que je constatais que c'était une situation qui était .un petit peu, peut-être pas bizarre, mais un peu – qui valait la peine un peu d'être regardée. [1991]

[1835] Quesnel had no recollection of reviewing financial statements for the nine borrowers, and he could not remember why he had not completed the second page of the Loan Information Questionnaires for these nine loans.[1992]

[1836] Ron Smith's explanations noted on page E-65e of the AWPs were accepted at face value with no audit procedures documented in the audit working papers.

[1837] The nine companies were incorporated in December 1990.[1993] Therefore, Castor had never done business with any of them earlier.

[1990] PW-1053-15, sequential page 207 (see also sequential pages 208 to 215 since the note appearing on page 207 also applies to loans discussed on pages 208 to 215)
[1991] Quesnel, November 24, 1995, pp. 7-8
[1992] Quesnel, November 24, 1995, pp. 172-179
[1993] Alksnis, February 7, 2006, pp.184 and following; Alksnis, February 8, 2006, pp. 18 and following

[1838] Hunt, the audit supervisor responsible for audit work related to the allowance for the doubtful accounts and loan loss provisions in the 1990 audit, was not aware that Quesnel had identified doubtful accounts:

> "Q. I would refer you now to page E65B of the audit working papers, which is a page prepared by Mr. Quesnel dealing with doubtful accounts. Were you aware of the fact that Mr. Quesnel had prepared this page?
>
> A. No.
>
> Q. Were you aware of the fact that Mr. Quesnel had identified doubtful accounts?
>
> A. No.
>
> Q. Were you aware of the fact that he had identified doubtful accounts which were not on the list of provisions that you had analyzed at page E300 and following?
>
> A. No.
>
> Q. What was your understanding when you were working on the section dealing with provisions as to what a doubtful account was?
>
> A. I don't recall my specific thought process about what a doubtful account was.
>
> Q. But at the time did you understand, as an auditor, what a doubtful account was?
>
> A. I believe so, yes.
>
> Q. And what was your understanding at the time?
>
> A. An account on which the collectability of that account, or the realization of that account would be doubtful.
>
> Q. And how would that doubtful account be reflected in a financial statement?
>
> A. If it was considered necessary provision would be made against that account.
>
> Q. Under the heading "Doubtful Accounts" Mr. Quesnel wrote:
>
> > "Accounts for which no reserve was taken in 1990 or reserve was not enough as per C&L".
>
> How were you able to prepare your section on investment provisions without being aware of Mr. Quesnel's conclusions on doubtful accounts?

A. I don't know how I was able to make my conclusion without that. That would be pulled together – as I had no knowledge of this that would be pulled together by the manager.

Q. You assumed that it would be pulled together?

A. It was not – yes.

Q. But you had no personal knowledge as to whether it was pulled together or not?

A. No.

Q. Now, on that page reference is made to nine loans made at year end 1990 in the aggregate amount of forty million dollars ($40,000,000). Were you aware of the existence of those nine loans?

A. Not that I recall, no.

Q. And you did not consider those nine year end loans in your assessment of the reasonability of loan loss provisions taken by management?

A. I don't recall any knowledge of those loans, so no.

Q. In doing your work on provisions did you consider any loans that were unsecured?

A. I don't recall considering any.

Q. For purposes of loan loss provisions did you consider that the capacity of a borrower to pay the loan was relevant?

A. I don't recall specifically considering that.[1994]

[1839] Quintal, the audit manager, acknowledged that the only audit work performed by C&L, in addition to Quesnel's discussions with Ron Smith, was to review the Loan Agreement file.

498. Q. What I see on E-65E is what Mr. Smith told Mr. Quesnel. It says "Mr. Smith said that" and there are two (2) paragraphs of what Mr. Smith said.

A. Yes.

499. Q. What work was done by you or your staff in connection with any kind of independent verification of that which Mr. Smith said?

[1994] Hunt, March 28, 1996, pp. 98-100

A. Well for those specific loans there is – the additional work that is specifically documented consisted of a review of the Loan Agreement file."[1995]

[1840] Quintal recognized that $40 million was an important amount of money (a material amount). Nevertheless, to be satisfied of the collectability of the $40 million loans, C&L had relied only on the client's representations.

510. Q. It's a material amount.

A. Forty million dollars ($40,000,000) is an important amount of money.

511. Q. And to satisfy yourself that this forty million ($40,000,000) was collectible, is it my understanding that you relied on those two (2) paragraphs and the information contained in the Loan Questionnaire?

A. That's correct. And I depend on the representation of the client.

512. Q. Where – what representation are you referring to now?

A. Well, I'm referring to his representations or his discussions on E-65E, as well as on the overall Letter of Representation.[1996]

[1841] Quintal did not recall whether he viewed these nine loans differently pursuant to the loans being made in the last month of the year.[1997]

[1842] Wightman was provided working papers E65c. Wightman expected that the loans were listed by C&L audit staff, specifically because they were loans issued in December 1990.[1998]

[1843] Wightman was aware of the $40 million in new unsecured loans that Castor had advanced in December 1990, and he discussed them with Stolzenberg in the year-end wrap-up meeting for the 1990 audit.

201. Q. And with respect to the new loans of December 1990, what was the discussion that took place?

A. I just said that we had noted that there were a number of new loans in December of 1990, and that they appeared to be unsecured, what was the – what was Castor's view of these loans and what was the nature of them, and so on and so forth.

202. Q. And what was the response which was received?

[1995] Quintal, December 1, 1995, p. 141
[1996] Quintal, December 1, 1995, p. 145
[1997] Quintal, December 1, 1995, p. 151
[1998] Wightman, September 29, 1995, pp. 71-79

A. The response that I recall was that they were to – several people at Castor knew well that they were the start of new business that Castor was going to obtain from these people, that they felt it was a breakthrough in their business.

203. Q. And did you ask who they were?

A. No.

204. Q. And did you ask whether Castor had done business with any of these people before?

A. No, I think Smith volunteered that they had done business with some of the people before or knew them well. I'm not sure whether it was "knew them well" or "had done business with them".

205. Q. And was there anything said by W.O. Stolzenberg on this issue?

A. No.

206. Q. Is there anything that you recall other than what you just said?

A. No.

212. Q. With respect to the new loans that you referred to in December, did you ask why these loans were made in December?

A. No, not particularly.

213. Q. Are year-end transactions or transactions made during the last month of the fiscal year, the object of particular scrutiny during an audit?

A. I presume that's why they were noted down and listed.

214. Q. And could you point to a place in the MAPs where they were listed?

A. Not in the MAPs but in the sheets to the file, which I believe I had at the time....It's E-65C on Castor Holdings Ltd., Part 4 of 5, December 31, 1990.

215. Q. This page, are you saying that this was included as part of the MAPs?

A. I believe that it was part of the papers that I had with me.

216. Q. Are you sure?

A. I'm quite certain, yes.

217. Q. In your list of ten (10) points that you prepared in your own handwriting, is there any mention of the loans mentioned on E-65C?

A. No.

218. Q. Why not?

A. I didn't think it was – it wasn't brought forward as being a problem or anything like that, it was to give me some general information about the portfolio, about the increase in the loans and to be able to discuss the circumstances in a knowledgeable way.

219. Q. So you consider that the loans referred to on page E-65C were not brought forward as a problem?

A. That's correct.

220. Q. What's the total amount of the loans on page E-65C?

A. (Witness looking through documents) On the total of the loans it's one hundred and thirty-three million ($133,000,000), Prom. Notes one hundred and fifty-four million ($154,000,000) and on issued in December 1990 it was forty million ($40,000,000).

221. Q. And you considered that it wasn't a problem?

A. I was not aware of any problem.

222. Q. You were not aware of any problem?

A. No.

223. Q. I refer your attention to page E-65B, the preceding page ...

224. Q. And what is the heading on that page?

A. Doubtful accounts.

225. Q. So it says doubtful accounts "as per Coopers & Lybrand".

A. Hmm, hmm. Yes.

226. Q. And under that what does it say?

A. "For which no reserve was taken in 1990 or reserve was not enough as per C&L."

227. Q. And what's the first item right after that?

A. See next page.

228. Q. And you consider under the heading of doubtful accounts where Coopers & Lybrand considers that there was no reserve taken or the reserve was not enough as per Coopers & Lybrand, that this is not a problem?

> A. I asked about these loans generally with Smith and I was told what was happening about particularly the new loans. That they were to solicit new business for Castor, that Castor was very confident that it was going to result in a lot more business for Castor, and they felt it was fine.
>
> 229. Q. Could you show me where one word of that is reflected in your notes?
>
> A. No, I didn't note that.[1999]

[1844] Wightman did not know who owned the nine companies, whether or not they related to specific projects, or what other businesses those borrowers may have had with Castor.

Loans as of December 31, 1990

[1845] The nine loans made to the nine companies were identified by C&L in the AWPs with a tick mark underlying the fact that they had been issued in December 1990. [2000] In each completed first page of the LIQ, Quesnel had also used tick marks underlying he had looked at the loan file.

- Loan 1167–Pustul Properties[2001]
- Loan 1168–Ptero Holdings[2002]
- Loan 1169–Truncal Holdings[2003]
- Loan 1171–Farl Properties[2004]
- Loan 1172–Blacking Holdings[2005]
- Loan 1173-Bioworld Holdings[2006]
- Loan 1174–Canont Holdings[2007]
- Loan 1175–Tesia Holdings[2008]
- Loan 1176-Serotine[2009]

[1999] Wightman, September 29, 1995, pages 71-79
[2000] PW-1053-15, sequential page 129
[2001] PW-1053-15, sequential page 210
[2002] PW-1053-15, sequential page 211
[2003] PW-1053-15, sequential page 207
[2004] PW-1053-15, sequential page 212
[2005] PW-1053-15, sequential page 214
[2006] PW-1053-15, sequential page 215
[2007] PW-1053-15, sequential page 213
[2008] PW-1053-15, sequential page 208

Experts positions

[1846] All experts acknowledged the following facts:

- The "Nasty nine loans" loans were part of a circular transaction of $40 million relating to the treatment and the payment (so that it could be included as revenue for Castor) of capitalized interests owed to Castor by the YH Group.
- That $40 million of capitalized interest was recognized by Castor as revenue in its 1990 consolidated audited financial statements.
- The $40 million loans were part of Castor's assets as disclosed in its 1990 consolidated audited financial statements.

Vance

[1847] Vance opined that a $40 million LLP had to be taken:[2010] the nine entities had no assets and the loans were clearly uncollectible.

[1848] Vance acknowledged that the hardest form of fraud to detect was a fraud that involved collusion between management and third parties.[2011]

[1849] Asked if there was an issue of fraud in relation to the "Nasty nine loans" and if he had taken that into account, Vance said the issue could be raised but it had no impact:

> Well, again, I guess I should comment with respect to the nine (9) year-end loans, I certainly... management was not forthright with the auditors, they raised the issue and I think the answers given to the auditors were not correct. But **notwithstanding that, the auditor put his finger on it, identified them for follow-up**, which is all a junior auditor can do, and that is where they should have been dealt with, at the upper levels, between the senior people on the engagement team, the manager or partner with the client, and they were not, so while **I think there was certainly an aspect of fraud** with respect to those nine (9) year-end loans, **it should have been uncovered by the auditors** at the point when that hit, and that was a misstatement that... as I said, that's the one area where I think certainly there's connotations of fraud, in that nine (9) year-end loans, although that was identified by the auditors for proper action, and **such action was not taken**.[2012] (our emphasis)

> I did not find very many examples of concealment because **all of the information was clearly in the books and records that were available to the**

[2009] PW-1053-15, sequential page 209
[2010] PW-2908, vol. 1, S-10
[2011] Vance, May 12, 2008, p. 87
[2012] Vance, March 5, 2008, pp.165-166

> **auditors**. The one that I think characterizes having... probably being the closest was the nine year-end loans because Mr. Smith was not forthright with the auditors and I think that probably would fit the handbook definition, and the diversion of fees was certainly a fraud upon the company, but I don't think there was sort of getting very fine, **but it wasn't a fraud upon the auditors. Once again, all of the information was clear in the accounting record.**[2013] (our emphasis)

[1850] In the case of the "Nasty nine loans", Vance opined that C&L should have uncovered the situation and should have realized it had been a cash circle of $40 million just looking at Castor's accounting books and records.[2014]

> A.-**Most certainly, they should have uncovered it.** They may not have uncovered all of the intimate details that you're... that have been put forward in evidence, but they should have been able to determine that the forty (40) million dollars went to Toronto, to Maclane & Kerr, and that was noted, and they did note that in the working papers, and just a quick review of the cash receipts journal would have shown exactly forty (40) million dollars coming back from the Toronto bank account, and then another five hundred thousand (500,000) from York-Hannover.
>
> Q- The Toronto bank account of who?
>
> A- Of Castor. Coming into the Toronto bank account on virtually the same day.
>
> Q- Okay. But you...
>
> A- **That, to me, is enough for an auditor to put on the brakes and say... and look at the substance**, forty (40) million dollars is not petty cash, it has a significant impact on the loan portfolio, and then the next step that I think a prudent auditor would have done would have been to start seeking out answers from the attorneys that were involved as to the nature of the disposition of these funds that were sent to them to confirm it was the same money coming back, and once you have that, you don't need any of the other details.[2015] (our emphasis)

Froese

[1851] Froese opined that a $40 million LLP had to be taken[2016] : the nine entities had no assets and the loans were clearly uncollectible.

[1852] Froese said that if someone was to look seriously at the loan files of the "nasty nine loans", one would see "*there's common addresses, common owners*". In the circumstances that prevailed at the end of 1990 and without a proper disclosure as to

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[2013] Vance, April 16, 2008, p. 171
[2014] Vance, May 13, 2008, p.35
[2015] Vance, May 13, 2008, pp.39-40
[2016] PW-2941-4

who the nine borrowers really were, while supposedly well known to Castor, it constituted a "red flag" to the auditor.[2017]

[1853] Froese opined that C&L had not complied with GAAS[2018] : they approached the audit with insufficient professional scepticism considering that the loans were unsecured, all made at the year-end and signed by the same three persons from different locations. While C&L initially expressed uncertainty about those loans, C&L failed to appropriately address such finding thereafter.[2019]

Rosen

[1854] Rosen opined that a $40 million LLP had to be taken: the nine entities had no assets and the loans were clearly uncollectible.

[1855] In his supplemental report,[2020] Rosen discussed the issue of fraud.

[1856] Rosen opined that the evidence of failures to comply with GAAP and GAAS was overwhelming and that, in such circumstances, it could not be said that C&L had been "victims" of fraud, it could not be that C&L could excuse itself alleging fraud.[2021]

> There' s just so many places where Castor management made the evidence fully available, and yet, it was ignored by Coopers & Lybrand.[2022]

[1857] For the $40 million loans, Rosen said that C&L had picked up the problem but that they failed to pursue the matter as they had to.

> Coopers & Lybrand, in essence, picked up the problems with the forty (40) million dollars.
>
> What I objected to in my writings was that it just was not handled well from that point on because these are clearly non-cash loans; they're fake loans in so many words. So that having them trying to be passed on to York-Hannover, well, most of them are out of York- Hannover to start with in the sense that interest was recorded as revenue when it not to have (inaudible), and something as to be done with it. So it's sitting in in York-Hannover to start with. And all they're doing is allocating that. So it would not have a major impact on the fraud angle simply because I think the evidence was there long beforehand.[2023]

[2017] Froese, December 2, 2008, p. 125
[2018] PW-2941, vol. 4, p. 184
[2019] PW-2941, vol.4, p. 158
[2020] PW-3034
[2021] PW-3034
[2022] Rosen, March 24, 2009, p. 35
[2023] Rosen, March 26, 2009, pp. 142-143

Selman

[1858] Selman opined that the "nasty nine" loans were without substance and should have been reversed.[2024] He initially testified that the reversal of the $40 million of loans would have no apparent effect on the 1990 balance sheet or on the statement of changes in net invested assets.[2025] However, he ultimately admitted that, if YH could not pay the $40 million of interest owing to Castor, "investments in mortgages, secured debentures and advances" would be reduced by $40 million, "general and administrative" costs on the income statement would increase from $33,731,000 to $73,731,000 and the $31,200,000 of net earnings would become a loss of $8,800,000.[2026]

[1859] If this Court concluded that the $40 million of "nasty nine" loans should have been written off, that alone would render the audited financial statements for 1990 materially misstated, said Selman:

> «Q- Now, assuming that the Court concludes that the forty (40) million dollars of loans should have been written off, would that one circumstance in and of itself render the audited financial statement for nineteen ninety (1990) materially misstated?
>
> A- Yes.»[2027]

Levi

[1860] Levi stated that «*one of the most devious examples of the circular transactions has been referred to as the "Nasty Nine" transaction*», and that the purpose of the "nasty nine" loans was to make it appear that YHDL, YHDHL, KVWI, 223356 Alberta Limited and MLVII were in a position to make payments on their indebtedness to Castor.[2028]

[1861] Levi further opined that Castor's 1990 financial statements would not have been issued had C&L been aware of Castor's true financial situation: Castor's financial statements would be misstated and misleading.[2029]

[2024] D-1295, p. 366.
[2025] Selman, May 25, 2009, pp. 209-210.
[2026] Selman, May 25, 2009, pp. 211-214.
[2027] Selman, May 25, 2009, pp. 215.
[2028] D-1347, p. 85.
[2029] Levi, January 28, 2010, pp. 38-39, 46-47.

Goodman

[1862] Goodman opined that these loans were made for a valid business purpose and were not misstated on the audited consolidated financial statements of Castor.[2030]

[1863] Goodman's position is that there was nothing questionable about the "Nasty nine" loans:

> «Q- Is there anything whatsoever in the evidence that you have seen or considered that makes you question the legitimacy of the nine (9) year-end loans described as the nasty nine (9)?
>
> A- From a GAAP perspective, no. I found that, My Lady, the loans had an amount that was stated at cost in the books, they were identified in the books. The loans, as I understand them from my reading of the testimony, were secured. And from my perspective, My Lady, there was nothing that I saw that indicated to me that a loss was either probable or estimable.»[2031]

[1864] Goodman testified that C&L were wrong to characterize those loans as doubtful accounts, and even claimed that they should have been characterized as good loans.[2032]

[1865] Goodman's opinion is based on his belief that the "Nasty nine" loans were guaranteed by Wersebe.[2033]

[1866] Goodman did not reconsider his opinion, even while admitting in his cross-examination that:

- nothing in the loan commitment documents or the correspondence file suggested that the "Nasty nine" loans were guaranteed;
- no such guarantees were provided by Wersebe at December 31, 1990;
- in other circumstances where Wersebe did provide a guarantee, the commitment letters referred specifically thereto.[2034]

[1867] Goodman continued not to reconsider his opinion,[2035] even when advised, *inter alia* that:

- Wersebe was not a director or shareholder of Pustul (one of the borrowers);[2036]

[2030] Goodman, September 22, 2009, pp. 97-98; October 9, 2009, pp. 113, 156, 160-171.
[2031] Goodman, October 9, 2009, pp. 189-190.
[2032] Goodman, October 26, 2009, pp. 271-272.
[2033] Goodman, October 26, 2009, p. 256. See also D-1312, p. 516, note 989.
[2034] Goodman, October 26, 2009, pp. 260-262, 273-287. See PW-1054-3 in connection with loan 1081.
[2035] Goodman, October 26, 2009, pp. 263-271.

- the resolution authorizing Pustul to enter the loan transaction made no reference to Wersebe or to any guarantee;[2037]
- the promissory note was not signed by Wersebe or anyone associated with the YH Group;[2038]
- subsequent documents were not signed by Wersebe.[2039]

Conclusions

[1868] The nine entities were off the shell corporations with no assets. The loans were unsecured. Without guarantees, those loans were clearly not collectible.

[1869] Quesnel, a C&L staff member, made an initial assessment that the $40 million in loans advanced in December 1990 may have required reserves. He realized that it was the case even though he was a very junior auditor (student) with no prior experience in auditing loans.

[1870] Hunt, the Audit Supervisor, responsible for auditing the allowance for doubtful accounts, was not aware of Quesnel's working papers concerning possible doubtful accounts. He was the person who had to consider the implications of Quesnel's working papers, and he obviously failed to do so.

[1871] Quintal, the Audit Manager, did not know if the audit staff had looked at borrowers' financial statements. Regardless of the extent of audit work his staff had performed, he did not view the loans differently, as they were issued in December, and he accepted the explanation provided by Ron Smith.

[1872] No initial work had been performed to test the collectability of these loans other than discussions with management. No further audit work was performed to verify those management representations.

[1873] The $40 million of capitalized interest and fees, which was the origin of the creation of these nine loans, should never have been recognized as revenue.

[1874] Once the loans were made, a LLP of $40 million was required.

[2036] See PW-1064-1-3, pp. 35-37.
[2037] See PW-1064-1-3, p. 48.
[2038] See PW-1064-1-3, p. 52.
[2039] See PW-1064-1-3, p. 53.

MEC

Events of 1990

[1875] Virtually, all the second mortgage security position held by Castor on the MEC project had, in turn, been assigned to Castor's own lenders.[2040]

[1876] The PAD was sold for $42 million. The costs of the changes required by the new project design consumed all the sale proceeds, and the PAD added no value to the project itself[2041], a fact Goodman acknowledged in that he ascribes no added value to the collateral once the PAD was sold.

[1877] The market was changing.

[1878] Just to cover its debt service, MEC needed 44.1 million per annum while it only generated about 18.2 million of revenue. [2042]

[1879] By November 1990, the MEC was substantially completed from the point of view of the retail centre, and it was operational, but remained to be covered the development of the tunnel, the completion of the PAD and the lease-up position.[2043]

[1880] On November 4, 1990, MEC opened in a very difficult and crumbling retail market. As of November 1990, "*the market was going downhill*".[2044]

[1881] Instead of opening up with about eighty percent occupancy, the MEC ended up opening only with about sixty-seven percent occupancy and a lot of turmoil with the various tenants.[2045] The project opened up in the most disadvantaged time that it could open up, a situation it never recovered from[2046].

[1882] By the end of 1990, the project was coming to substantial completion and the Bank of Montreal was concerned about the actual performance of the project to support the loan interest on their debt. At that point in time, they came back to Castor and to the borrowers and indicated to them that they wanted an additional undertaking from Castor to cover any interest shortfalls on the project, due to a lack of income being generated by the project[2047].

[1883] The owners were not putting up the funds[2048].

[2040] PW-1053-14, seq. pp. 154-155.
[2041] Ron Smith, September 15, 2008, p. 123.
[2042] Ron Smith, September 15, 2008, p.183
[2043] Ron Smith, September 15, 2008, p.182
[2044] Ron Smith, September 15, 2008, p.195
[2045] Ron Smith, September 15,2008, p.122
[2046] Ron Smith, September 15, 2008, p.123
[2047] Ron Smith, September 15, 2008, pp.165
[2048] Ron Smith, September 15. 2008, p. 166

[1884] Because it was apparent that the project would not generate sufficient net income to cover the interest obligations on the $125 million first mortgage loan, Castor was compelled to provide an interest shortfall guarantee in favour of BMO.[2049] On December 17, 1990, Smith calculated the Castor shortfall guarantee at $7,636,592.[2050] As appears from such calculation, the total annual net revenue of the MEC (before expenses) was only $10,281,408 and the interest expense payable on the first mortgage alone was $17.5 million.

[1885] Castor had to support the project until its sale could be completed, which was the only way Castor could realize its money back at that point in time[2051].

[1886] As at December 31, 1990, according to report number 37 from Helyar and associates[2052], the revised budget for MEC was in excess of $304 million[2053].

[1887] Towards the end of the year, there were a lot of activities to try to sell the MEC.[2054]

Loans as of December 31, 1990

[1888] Castor's exposure to the MEC project, as of December 31, 1990, amounted to a minimum of $180 million[2055]

- Loan 1042: $29 million[2056]
- Loan 1095: $10 million[2057]
- Loan 1145: $43.2 million[2058]
- Loan 1100 : $ 60 million[2059]
- Loan 1101: $8.9 million[2060]
- Loan 1103: $7.7 million[2061]

[2049] PW-1104-11.
[2050] PW-1104-12.
[2051] Ron Smith, September 15, 2008, p.166
[2052] PW-1106-C
[2053] Ron Smith, September 15, 2008, pp.195-196
[2054] Ron Smith, September 15, 2008, p.197-198
[2055] D-1312, p. 147 (Goodman calculated $182.4 million)
[2056] PW-1053-15, sequential pages 253-254-255
[2057] PW-1053-15, sequential pages 134 and 294
[2058] PW-1053-15, sequential pages 251-252
[2059] PW-1053-15, sequential pages 241-242
[2060] PW-1053-15, sequential pages 247-248
[2061] PW-1053-15, sequential pages 249-250

- Loan 1109: $ 4 million[2062]
- Loan 1158 : $0.3 million[2063]
- Loan 1163: $6.8 million[2064]
- Loan 1146: $3 million[2065]
- Loan 701,0001/2001 : $7.5 million[2066]

[1889] More than $ 117 million was due to Castor's prior ranking creditors.[2067]

Appraisal

[1890] On September 11, 1990, Whiting advised Wersebe that reasonable cases could be made for valuations of MEC in the range of $225 to $275 million with the following cautionary note: «*I have no certainty of any buyers interested in the property at any price let alone this value range.*»[2068]

[1891] Similarly, Whiting informed Wersebe that there was no value in the MEC to support a $5 million loan increase at year-end 1990.[2069]

[1892] Whiting's assessment of the value of the MEC was confirmed by the Royal LePage appraisal prepared for the first mortgage lenders on or about September 1, 1990, which established the 1990 MEC value at $241 million[2070]. Ron Smith testified that although Castor had not received a copy of such a revised appraisal until after the 1990 audit, it had been received by the first mortgage lender and was later obtained by Castor in May 1991.[2071]

Experts' opinion

Vance

[1893] Vance opined that a minimum LLP of $65 million should have been recorded in 1990. To calculate his LLP, Vance started from the appraisal value of $241 million (mid-point) established by Royal LePage in its appraisal as of September 1, 1990.

[2062] PW-1053-15, sequential pages 243-244
[2063] PW-1053-15, sequential pages 245-246
[2064] PW-1053-15, sequential pages 134 and 245
[2065] PW-1053-15, sequential page 134
[2066] PW-1053-87, sequential page 121
[2067] PW-2941, vol. 4, p.181 ($117.8 million) ; D-1312, p. 135 ($120.7 million)
[2068] PW-1159-6.
[2069] PW-1185.
[2070] PW-1108B; Ron Smith, September 15, 2008, p.209;
[2071] R. Smith, September 15, 2008, pp. 208-209.

Froese

[1894] Froese calculated a range from $14.9 to $74.5 million and opined that a LLP should have been recorded in 1990.

[1895] To arrive at those figures, Froese used a range of starting values for the MEC project (from $232 to $285 million).

Rosen

[1896] Rosen calculated a range from $66 to $ 83 million and opined that a LLP should have been recorded in 1990.

[1897] To arrive at those figures, Rosen used a range of starting value figures for the MEC project, all from the Royal LePage appraisal as of September 1, 1990 ($232 to $249 million).

Goodman

[1898] Goodman opined that the MEC had an estimated realizable value of $350 million at December 31, 1990 and he assessed the value of the Palace II Theatre property at $11 million. He therefore used a total combined value of $361 million.

[1899] Based on this assumed valuation, Goodman asserted that a surplus was available to the co-owners of the MEC that could serve to offset loan deficiencies on other loans in the Castor portfolio.

[1900] Although Goodman originally opined that the loan surplus for the MEC was of $79.7 million as at December 31, 1990, he subsequently amended and reduced such a figure to $57.5 million, and finally to $42.5 million, to correct calculation errors.[2072]

[1901] Based on his $361 million value figure, assuming it was accurate, Goodman further testified and acknowledged that only $11.6 million of the alleged surplus would accrue to YHDL.[2073]

Conclusions

[1902] Plaintiff experts' opinions prevail. As of December 31, 1990, the value of MEC was in the neighbourhood of $ 241 million, clearly not in the range of $300 to $350 million. Using the figure of $241 million does not constitute hindsight: had C&L insisted on receiving an updated appraisal, as they should have in the circumstances that were prevailing in the market and the economy, this information would have been available.

[2072] D-1312, Table CB.3, p. 52; D-1312-1, Tab 4; D-1312-6; Goodman, November 30, 2009, pp. 157-158; December 2, 2009, p. 97.

[2073] D-1312-3; Goodman, November 30, 2009, pp. 157-160.

[1903] Therefore, a LLP of approximately $ 65 million should have been taken.

[1904] Goodman's theory assumes that Castor would not only achieve its full "asking price" of $350 million, but that the proceeds received, net of all brokerage costs, closing costs and related expenses, would be at least $350 million. Such an assumption is totally unrealistic and inconsistent with the reality of the situation. It also ignores the enormous costs that Castor would need to incur before this presumed sale would ever be finalized and closed.

[1905] In fact, even C&L did not adopt the approach advocated by Goodman. In the year-end notes of Wightman for the 1990 audit,[2074] he indicated that «*new appraisal coming which is expected to show 300-350 mill based on 11% disc. cash flow.*» The only appraisal that C&L actually relied upon, however, was the Royal LePage appraisal of 1988 in the sum of $275 million.

[1906] Any theory which would assume Castor enforcing its security and taking over the project by way of "*dation en paiement*", would have to further assume that Castor would need to repay the first mortgage lenders in an amount up to $125 million as well as the assignees of the second mortgage debt in an amount in excess of $57 million.[2075] Castor could not make such payments[2076] and had no intention of enforcing its security against the MEC property.

TSH

Experts' positions

[1907] All of Plaintiff's experts came to the conclusion that a LLP was required, their minimum LLP being:

- Vance : $51.5 million[2077]
- Froese: $57.8 to $76.1 million[2078]
- Rosen: $43.3 to $51.3 million[2079]

[1908] All of Plaintiff's experts also concluded that the loans should have been placed on a non-accrual basis.[2080]

[2074] PW-1053-12, seq. p. 79.
[2075] Goodman, November 18, 2009, p. 116; PW-1053-14, seq. pp. 154-155.
[2076] In 1990, Castor disbursed in several tranches because it did not have access to more than $5 million in cash. See Goodman, November 2, 2009, pp. 188-189.
[2077] PW-2908, Vol. 1, page S-10
[2078] PW-2941, vol.1, p.25 and PW-2941-4
[2079] PW-3033, Vol. 2, Appendix A, p. 3.
[2080] PW-2908, Vol. 1, p. 4-I-18 to 4-I-19; PW-2941, vol.2 p. 4; PW-3033, Vol 2. Appendix A, p.34

[1909] Plaintiff experts opined that the value of the TSH was certainly much lower than $93 million. However, it is by using the $93 million figure that the Plaintiff experts came to their minimum LLP. To calculate his high end figure of $76.1 million, Froese used the Jones McKittrick appraisal of 1991 acknowledging that it was not yet available in Castor's files: however, he opined that C&L should have asked for an update of the appraisal in 1990, taking account of the state of the economy. The Court agrees.

[1910] With respect to the TSH loans, other than the Lambert loans totalling $40.1 million, Goodman concluded that a $2.8 million deficiency existed at the year end.[2081] Had he taken account of the Lambert loans, Goodman would have identified a minimum deficiency of $42.9 million.

[1911] Again, Goodman overcame the deficiency through his theory of off-set.

[1912] To conclude as he did, Goodman valued the TSH at $93 million including surplus land. He subtracted current liabilities of $0.3 million and property taxes due at $ 4.4 million. He opined that the value available to Castor was of $ 88.3 million.[2082]

1990 events

[1913] Stolzenberg had initiated discussions in 1989, which resulted in the management of the hotel being transferred away from YHHL to a new entity called Transamerica in 1990.[2083]

[1914] Prychidny agreed to move from YH to Transamerica, as president of this entity. Transamerica provided management support for the TSH (similar to what was in place for the MLV). All decisions for Transamerica were made by Stolzenberg, and all the money was provided by Castor.[2084]

[1915] On-going demands for funds to meet operating expenses as well as business and tax arrears were made.[2085] Castor tolerated the situation because the attempts to sell the hotel or to restructure the TSH had not been successful, leaving Castor with no choice but to hold the property.[2086]

[1916] In June 1990, the City of Etobicoke demanded payment in full of the outstanding 1988 to 1990 business taxes.[2087]

[1917] By November 5, 1990, the TSH year-to-date cash flow shortfall totalled $1.6 million, prior to interest payments on Topven's debt.[2088]

[2081] D-1312, p. 399
[2082] D-1312, pp. 399-400
[2083] PW-248D; see also PW-249 and PW-434A; see also PW-442 and PW-439
[2084] R. Smith, September 3, 2008, pp. 107–109.
[2085] For example, PW-447; PW-174G; PW-1080-14.
[2086] R. Smith, September 3, 2008, p. 43.
[2087] PW-447A-1, PW-447

[1918] The grid note loan increased to $26.4 million with the advances disclosed on the loan cards as interest related to the TSH first and second mortgages, interest on the $30 million grid note, taxes and payments to Johnson Control.[2089]

[1919] By year-end of 1990 the hotel was recording a loss before debt and the debt itself was "snowballing." [2090]

[1920] The total accumulated deficit of Topven, Topven (88) and Lambert as of December 31, 1990 exceeded $90 million.[2091]

[1921] In January 1991, Castor advanced Transamerica $5 million under a $20 million grid note. The advance was directed to pay the 1990 management fee to Topven (88), of which $1.5 million was paid to Castor. [2092] Approximately $3.3 million was paid to CHIF as interest and fees on the $20 million second mortgage loan.[2093]

Loans as of December 31, 1990

[1922] At December 31, 1990, and excluding advances or loans to Transamerica, Castor's exposure to loans relating to the TSH was in excess of $ 125 million.

Owed to CHL

- Loan 1107: $40 million[2094]
- GL066/loan 1148 : $26.4 million[2095]

Owed to CHIF

- Loan 576000/3002: $33 million[2096]
- Loan 576000/3009: $7.1 million[2097]
- Loan 888002/2003: $20 million[2098]

[2088] PW-434B
[2089] PW-167D
[2090] R. Smith, September 3, 2008, pp. 41-43; PW-1084A, PW-1084B and PW-1084C: Summary of Annual Interest Obligations Based on Loans Outstanding (PW-424, p. 9, PW-429, p. 14 and PW-430, p. 11, respectively).
[2091] PW-2941, vol. 2, p.46 (see also footnotes 73 and 74)
[2092] PW-440
[2093] PW-440A
[2094] PW-1053-15-13
[2095] PW-1053-15-13
[2096] PW-1053-87, sequential pages 126, 135, 148, 157-158
[2097] PW-1053-87, sequential pages 126, 135, 148, 157-158
[2098] PW-1053-87, sequential pages 121, 136

[1923] The accrued interest on Castor's loans were of $4.7 million[2099]

[1924] In 1990, Castor also made a loan to Transamerica. The balance owed to Castor at year-end was $5.5 million. In his computation of the LLP, Froese took that loan into account since he opined that by financing Transamerica Castor was in fact financing the TSH operating losses.[2100]

[1925] Again, cash circles were used to pay interest on the Lambert loans.[2101]

Appraisal

[1926] An appraisal of the TSH, done by Jones McKittrick Services Limited and dated May 17, 1991, was forwarded to Smith at the request of Prychidny. The appraised value of the TSH, including excess land, was $85.2 million assuming completion of renovations estimated to cost between $8 and $13 million. It did not include the parking area in the excess land calculation. The excess lands were valued at $2.9 million as compared to $10 million in the 1988 Mullins appraisal.[2102]

Conclusions

[1927] The comments and analysis made under the subheading relating to the TSH in the 1988 section of the present judgment apply *mutatis mutandis* to 1990.

[1928] The indebtedness increased and the value of the TSH decreased. At best, the market value of the TSH was $93 million, but the evidence shows it was probably closer to $75 to $80 million.

[1929] Taking into account the best possible scenario as to market value (at $93 million), and the various figures proposed by all experts (excluding the financing to Transamerica), Castor should have recorded a LLP of at least $42.9 million.

CSH

Experts' positions

[1930] No dispute between the experts that there was a material loss exposure in connection with the CSH in 1990. The dispute is whether GAAP required that a loan loss provision be taken.

[1931] The Plaintiff's experts identified the following minimum LLP on the assumption that one could rely on the appraisal of the CSH:

[2099] D-1312, p. 395, footnote 715
[2100] PW-2941, vol.2, p. 39
[2101] Froese, January 27, 2009, pp. 66 and following; Levi, January 14, 2010, pp. 81 and following
[2102] D-825

- Vance: $ 32 million[2103]
- Froese: $21.1 to $36.1 million[2104]
- Rosen: $22.8 to $33.4 million[2105]

[1932] Plaintiff's experts agreed that the loans should have been placed on a non-accrual basis and that $9.6 million should have been reversed.[2106]

[1933] Given the state of the economy and the condition of the hotel, Vance used the low point of the appraisal rather than the midpoint that he had used in 1988 and 1989.

[1934] Using a property value of $55.6 million to which he deducted $1.3 million to cover renovations, [2107]Goodman calculated a loan deficiency of $23.4 million.[2108] However, and as he had concluded in 1988 and 1989 and for the same reasons, Goodman opined that there was no need to record a LLP in 1990.

1990 events

[1935] The CSH was overburdened with debt and that, together with double-digit interest rates, was the principal cause of the cash deficiencies that dogged the hotel.[2109]

[1936] Loan 1154 was created in February 1990. As a result of capitalization of interest and fees, the loan increased to a balance of $9.3 million as of December 31, 1990. Loan 1154 was an unsecured loan.

[1937] The cash reserve deposit for renovations decreased through charges to the deposit account for capitalization of interest and an annual fee charged on the second mortgage.[2110] The planned renovations were not done.[2111]

[1938] The management contract between Skyview and YHHL was terminated.[2112]

[1939] The loan covenants were not complied with and interest continued to be capitalized.

[2103] PW-2908, vol.1, p. S-10
[2104] PW-2941-4
[2105] PW-3033, Vol. 2, Appendix G, p.3, Approach A (unadjusted figures).
[2106] PW-2908, vol. 1 page S-10
[2107] D-1312, p. 423
[2108] D-1312, p. 429
[2109] Prychidny, October 14, 2008, p. 45; October 15, 2008, pp. 195-196; Ron Smith, October 2, 2008, pp. 59-60.
[2110] PW-167S
[2111] PW-467F, bates 15. PW-2941, vol. 2, page 160, paragraph 3.81
[2112] PW-476D

[1940] The unaudited financial statements of Skyview for the year ended December 31, 1990, disclosed income before taxes, interest and depreciation of $ 1.9 million and a net loss of $ 8.2 million.[2113] Skyeboat incurred a net loss of $ 1.5 million[2114] and 321351 Alberta a net loss of $1.7 million.[2115] The combined net losses for 1990 were $11.4 million.[2116]

[1941] Interest expense recorded in the financial statements of Skyview, Skyeboat and 321351 Alberta amounted to approximately $12.2 million.[2117] The shortfall in income to cover debt charges was thus in excess of $10 million while the 1987 PKF appraisal had projected income from $4.8 million (in 1988) to $5.9 million (1991).

[1942] In their AWPs, C&L "*expressed uncertainty about collateral*" in relation to loan 1154 of $9.3 million.[2118] C&L put that loan on a list of "*doubtful accounts (as per C&L)*".[2119]

Loans as of December 31, 1990

[1943] Castor's exposure to loans relating to the CSH amounted to more than $79 million as of December 31, 1990.

- Loan 1097: $25 million[2120]
- Loan 1154: $9.3 million[2121]
- Loan 1143: $15.5 million[2122]
- Loan 1147: $13.6 million[2123]
- Loan 790002/2005: $16 million[2124]

[2113] PW-467E
[2114] PW-466C
[2115] PW-465B
[2116] PW-2941, vol.2, p. 164
[2117] PW-2941, vol.2 , p. 162
[2118] PW-1053-15, sequential page 286
[2119] PW-1053-15, sequential pages 128-129
[2120] PW-1053-15, sequential pages 134, 337; PW-1053-15-14
[2121] PW-1053-15, sequential pages 129, 134, 285-286, 338
[2122] PW-1053-15, sequential pages 134, 289-290
[2123] PW-1053-15, sequential pages 134, 287-288, 339
[2124] PW-1053-87, sequential pages 121, 136; PW-1087-3A

Conclusions

[1944] The comments and analysis made under the subheading CSH in the 1988 section of the present judgment apply *mutatis mutandis* to 1990.

[1945] The indebtedness increased and the value of the CSH did not.

[1946] Taking account of the various figures proposed by all experts, Castor should have recorded a material LLP relating to the CSH in 1990, of at least $21.1 million.

OSH

Experts' positions

[1947] Vance opined that a minimum LLP of $19.2 million should have been recorded in 1990. He also opined that all interest and fee revenue on the OSH loans should have been reversed: in 1990, the amount of $3.2 million.[2125]

[1948] For the OSH, Goodman acknowledged that there was a deficiency in Castor's loan position of $6.3 million in 1988 and of $3.9 million in 1989.[2126]

[1949] In his initial Report, Goodman had opined that there was also a deficiency for 1990: a deficiency of $7.9 million.[2127]

[1950] In his updated Report for trial (D-1312), Goodman no longer provided any opinion for 1990 since he had changed his view and no longer considered 687292 to be part of the YH Group. This being the case, Goodman acknowledged that there would be no right of offset if the Court was to conclude that there was a deficiency in connection with the OSH loans.

Events of 1990

[1951] In March 1990, 687292 Ontario Ltd. ("**687292**") purchased from Skyline 80 all the assets related to the operations of the OSH for $1 and assumed the debt.[2128]

[1952] Loan 1166 was granted as of March 23, 1990. In the first year of the loan, $1.4 million of interest was capitalized to the principal balance.[2129]

[2125] PW-2908, page S-10
[2126] D-1312, ES-28.
[2127] Goodman, November 30, 2009, pp. 176-182.
[2128]
[2129] PW-1053-15-15

Loans as of December 31, 1990

[1953] Castor's exposure to the OSH amounted to $19.2 million as of December 31, 1990.

- Loan 1165 : $6.5 million[2130]
- Loan 1166 : $ 12.7 million[2131]

Conclusions

[1954] Vance's opinion prevails. A LLP of $19.2 million should have been recorded in 1990.

TWTC

Events of 1990

[1955] In December 1989, Coldwell Banker had been mandated to attempt to sell the office tower lands for the sum of $145 million.

[1956] It became apparent, however, that such amount could not be achieved.

[1957] In a February 21, 1990 memorandum, the situation was described as "doom and gloom".[2132] The conclusion was that the reduced value of the land was $70 to $90 a square foot rather than the $100 per square foot referred to in PW-1069-10.

[1958] Later, it became apparent that the market value of the lands was more in the range of $65 per square foot.[2133]

[1959] C&L determined that loan 1149 was of a high risk nature and that a reserve could be taken on the loan for 1990.[2134]

> C&L judge this loan as risky as loan o/s as at Dec 31/1990 and interest receivable are 15 092 215.96 (interest being capitalized each month after their consider as receivable) and Prom note is only $ 15 000 000
>
> C&L judge that CHL could take a reserve on this loan. Also C&L expresses uncertainty over the nature of the collateral (only a Prom note) but still there are

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[2130] PW-1053-15-2
[2131] PW-1053-15-2; PW-1053-15-15 (E-195-196)
[2132] PW-1161-31.
[2133] Whiting, February 14, 2000, p. 105
[2134] PW-1053-15, sequential pages, 128, 129, 224-225

> other collaterals (see bottom of 149) which are hard to value. So for these reasons C&L considers this loan as high risk nature[2135]

Additional evidence

[1960] In his analysis for trial, Whiting estimated a loss to Castor as at September 30, 1990, of $27 million for the TWTC loans and of $5.6 million for the TWTC option loan.[2136]

Experts' positions

[1961] For the reasons previously explained[2137], Vance did not recommend a LLP for the TWTC.

[1962] Froese did not opine on the TWTC situation.

[1963] Rosen opined that a minimum LLP of $62 million should have been recorded.

[1964] Goodman concluded that there was a surplus available that could be used to offset deficiencies of the YH Group.

Plaintiff's argument

[1965] In his written submission, and even though the expert Vance did not recommend a LLP for the TWTC, Plaintiff argues that the Court should recognize a minimum LLP of $30 million namely for the following reason:

> C&L characterized the "best" TWTC loan made by Castor as being of a high risk nature in 1990.[2138] The reason this loan was the "best" is that it was made to the parent of the project entities as opposed to the grand-parents being YHDL and TWDC. Consequently, any monies which would flow to the owners (after the payment of all prior ranking debt) would first flow to TWTCI before it could possibly get to the shareholders of TWTCI. Once C&L determined (correctly) that the TWTCI loan was of a high risk nature, GAAP required that all of the TWTC loans be placed on a non-accrual basis and that no further interest be recognized until reasonable assurance of collectability existed.[2139]

Conclusions

[1966] The situation of the TWTC project did not improve in 1990, on the contrary. In those circumstances, a LLP might have been needed to comply with GAAP.

[2135] PW-1053-15, sequential page 225
[2136] PW-1186A.
[2137] See the TWTC sections relating to the 1988 and 1989 financial statements in this judgment
[2138] PW-1053-15, seq. pp. 224-225.
[2139] Plaintiff's written submissions July 8, 2011, p.76

[1967] However, given the Court's conclusions, she feels it is not necessary to elaborate further on that topic.

Meadowlark

Experts' positions

[1968] Rosen calculated a LLP equivalent to Castor's exposure to Meadowlark since he concluded that the property had not a greater value than the amount that was due to prior ranking creditors.

[1969] Goodman calculated a deficiency of $0.1 million taking into account a market value of $22.4 million and prior ranking debts of 17.4 million.[2140]

Events of 1990

[1970] Castor continued to fund the taxes owed by Meadowlark as well as operating expenses and mortgage payments to BMO so that the property would not be lost.

[1971] By August 1990, Castor understood that if the property was sold as is «*in the presently depressed real estate market*», the entire 2nd mortgage of $7 million would have to be written off.[2141]

[1972] In January 1991, BMO put the project into default and claimed about $16.1 million in principal and interest due as at December 31, 1990 from the owners of Meadowlark (Leeds, Raulino Canada and YHDL).[2142]

[1973] A few months later, Meadowlark was sold for the purchase price of $11 million[2143]and Castor took a complete loss on its loans.

[1974] Quesnel, the senior auditor responsible for the investment section in the 1990 audit, namely wrote the following in his AWPs, on page E-65b:

> Meadowlark Park Shopping Center (see E110)
>
> Shopping Mall located 2KM away from West Edmonton Mall in ALTA
>
> CHL W/D 2 000 000 on this loan in 1990
>
> R. Smith said that appraisal could be around 20M$ actually (Total value of loans 19 700 000). Since appraisal is not based on an independent study C&L judges

[2140] D-1312, pp. 260-261
[2141] PW-1112-18.
[2142] PW-1112-19.
[2143] PW-1112-20.

> that appraisal could be even lower. (West Edmonton Mall is expending every year). Additional reserve would be in order.[2144]

Loans as of December 31, 1990

[1975] Castor's exposure was of $5 million further to a LLP of $ 2 million taken in 1989.

Conclusions

[1976] Probabilities are that a LLP should have been taken for Meadowlark in 1990 given the state of the economy and the history of that mall and of its immediate competition.

[1977] However, given the Court's conclusions, she feels it is not necessary to elaborate further on that topic.

DT Smith

Positions in a nutshell

Plaintiff

[1978] Plaintiff argues that by December 31, 1990 and during the months of January and February, 1991, the slow-down in sales and absorption rate, and the depressed selling prices, particularly for the higher priced homes as the DT Smith homes, was notorious and readily available from information published in the newspapers, from promoters, sales agents, and even other accounting firms.

[1979] Plaintiff submits that loan loss provisions in excess of $50 million should have been disclosed for the loans extended to the DT Smith Group.

Defendants

[1980] For the year ended December 31, 1990, Defendants acknowledge that Strassberg came to the conclusion that the DT Smith Group had to record a huge LLP in its financial statements. However, they argue that Strassberg came to such a conclusion with the benefit of hindsight, and only in February 1992, rather than in February 1991.

[1981] Defendants submit that at the end of 1990, and without using hindsight, Castor had a security surplus on its loans to the DT Smith group.

[2144] PW-1053-15, sequential page 128

Evidence

Prior to 1990

[1982] David T. Smith set up a number of companies whose sole purpose was to develop and sell residential real estate projects in Southern California. Each of these companies was nominally capitalized.

[1983] The projects were either development/construction projects, or land held for future construction projects expected to be initiated in a very short time.

[1984] CHIO began lending money to the various D.T. Smith entities in 1987, and continued to do so throughout 1988, 1989 and 1990. Castor never analyzed the creditworthiness of the DT Smith group of companies but merely relied on Stolzenberg's knowledge of DT Smith.[2145]

[1985] The DT Smith group was financially totally dependent on Castor for its liquidity needs.[2146]

[1986] All the CHIO loans to the D.T. Smith entities were extended, administered and monitored out of Castor's Montreal offices. Ron Smith, the Senior Vice President of mortgages, was the individual responsible for administering and monitoring those loans.

[1987] For each construction project, the loans by CHIO to each of the D.T. Smith entities were structured as follows:

- There was a first mortgage loan commitment letter and loan agreement between CHIO and the D.T. Smith entity, with terms and conditions obliging the borrower to put up a certain amount of equity for the purchase of land, placement fees, pre-development costs, general and administrative expenses, etc.[2147]

- Concurrently, CHIO and the D.T. Smith entity would sign a second mortgage loan commitment letter and loan agreement, whereby CHIO undertook to pay all the sums which the borrower was itself committed and obliged to pay according to the first mortgage loan agreement[2148].

[1988] Therefore, and in fact, Castor was financing 100% of pre-development and construction costs (hard and soft costs), cost overruns and interest and fees.

[1989] The D.T. Smith Companies ran no risk of losing anything and the entire risk for the D.T. Smith projects vested with Castor.

[2145] R. Smith, June 10, 2008, p. 31.
[2146] D-1324.
[2147] For example see PW-1115-2B
[2148] See for example PW-1115-3B

- the D.T. Smith Companies were nominally capitalized;
- the D.T. Smith Companies had no assets other than the title to the projects;
- Neither David T. Smith personally, nor anyone else, invested any capital into any of the D.T. Smith projects, or injected any funds;
- Any profit would accrue to the D.T. Smith borrower, but any loss would be borne by Castor.

[1990] David T. Smith and his wife, Norma, each owned a 50% interest in each of the D.T. Smith entities[2149]. David T. Smith personally guaranteed each of the CHIO loans to a D.T. Smith entity.

[1991] Each and every one of the loan agreements between Castor and the DTS borrowing entities contained a covenant obliging the borrower and guarantor, David T. Smith, to furnish to Castor their respective financial statements within 120 days of fiscal year-end (December 31*).*[2150]

[1992] The audited combined financial statements of the DT Smith Companies, with the audit opinion of Rogoff & Company, were furnished to Castor for each of the 1987, 1988 and 1989 fiscal years, and were kept in C&L's Montreal files.[2151]

[1993] As at year end 1987, CHIO's exposure to the D.T. Smith Group of Companies was $57,000,000 (Canadian Funds), out of Castor's total portfolio of $773,000,000[2152], or 7.4%[2153].

[1994] As at year end 1988, CHIO's exposure to the D.T. Smith Group of Companies was $103 million, out of Castor's total portfolio of $1,000,600.00, or 10.2%[2154].

[1995] As at year end 1989, CHIO's exposure to the D.T. Smith Group of Companies was $218 million, out of Castor's total portfolio of $1,424,000.00, or 15.3%[2155].

[1996] During 1988 and, for the most part of 1989, the residential real estate market in Southern California was hot; it started to cool off in the latter part of 1989, and continued its slowdown into the spring of 1990.

[1997] DT Smith had signed agreements with Eton Properties, whereby 50% of the profits realized from the DT Smith projects would be paid over to Eton.[2156] The

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[2149] PW-2324 to PW-2336-1; Moscowitz, March 10, 2000, at pp. 2323-2347
[2150] See, for example, PW-1115-2B.
[2151] R. Smith, June 10, 2008, p. 38; PW-1113D; PW-1113E.
[2152] This amount includes the $100 million debentures
[2153] This % represents a minimum (taking account of the $100 million debentures)
[2154] This % represents a minimum (taking account of the $100 million debentures)
[2155] This % represents a minimum (taking account of the $100 million debentures)

agreements were dated June 14, 1989, but most were effective from late 1988 and early 1989, depending on the property. Those agreements provided that, in the event that Eton Properties advanced funds to a project that DT Smith did not match, DT Smith's equity in the project would be reduced to a minimum of 32.5%.[2157]

[1998] David Smith testified that the Eton Properties' agreements were entered into at the request of Stolzenberg and in the following context:

> A. There came a time in early 1989 when Mr. Stolzenberg approached me in one of his visits, and asked me to -- I shouldn't say asked me – told me that the way he was financing it now, the 100 percent financing that he was giving to me, he didn't think was acceptable anymore, and that he wanted a larger interest in the projects, that he wanted to take a 50- percent interest in the ongoing projects. And he told me that if I would not be amenable to that, that there were lots of other people who would want to be financed, and that he would not be able to continue financing us under these terms. I told him, after some thought, that I would be amenable to doing that, but that I would like to get off the guaranties. If I'd be able to get off the personal guaranties, I would be amenable to that.
>
> Q. These are the personal guaranties for what?
>
> A. For Castor.
>
> Q. Whose guaranties?
>
> A. My personal guaranties. That if I was not responsible for those guaranties any longer, that I would do that. And he said that that was acceptable to him, that this new entity, which eventually was called Eton, would be responsible for putting up the necessary capital, if there was ever a call made for capital. And if there was a call made for capital, then Eton would put up the sufficient monies so a call wouldn't be made; and if I didn't put up my pro rata share of the monies that were called, then my interest would fall from a 50 percent interest to a 32.5 percent interest. So in the worst case scenario, I would still have a 32 and a half percent interest. After reflecting upon that, I thought it was a wonderful transaction for me. I no longer had personal guaranties that would be called upon, I was getting 100 percent financing, more than 100 percent financing, because they not only financed the property, but they also financed our general and administrative expenses so that I was getting basically 110 percent financing, and only had an upside and didn't have any down side. I also asked him that if he was taking such a large interest now in the entity, not only was he now getting the fees, but now he's getting a 50-percent interest. I asked him whether or not he can – he would return a portion of the fees to me as well. And he said he would think about it and that he would -- eventually he said he would return a portion of the fees on an ongoing basis."[2158]

[2156] PW-1398, PW-1404, PW-1405 to PW-1411.
[2157] See PW-1409, sections 4.2 and 5.1
[2158] David Smith, March 14, 2000, pp. 94-97

[1999] Strassberg, DT Smith auditor, explained those agreements with Eton Properties as follows:

> Mr. Moscowitz had informed me that they were making arrangements to take on a partner who was going to guarantee them some financing in exchange for 50 percent of the profits...
>
> Mr. Moscowitz, who gave these to me, just informed me that they were doing this to protect their financing.[2159]

[2000] The Tennis Villas agreement stated namely:

> Upon the terms and conditions contained herein, the Company hereby retains and engages Eton to, and Eton hereby agrees to, provide sufficient funds to the Company to prevent the Company from being in a monetary default under the terms of the Loan Agreements.[2160]

[2001] Out of the profits realized from the Tennis Court Project, an amount of $1.4 million was paid to Eton Properties[2161].

[2002] Castor's development loans to the DT Smith properties in California were characterized by delays and cost overruns.

1990

[2003] As at December 31, 1990, DT Smith had seven projects under development and seven properties for future development. One project, the Tennis Court Villas, had been completed, at a profit.

- The seven remaining development projects were: Chino Hills, Dove Canyon 1, Dove Canyon II, Wood Ranch II, San Marcos, Laguna I and Laguna II.
- The seven properties for future development were: Ritz Pointe, Rancho California, Rancho Parcel 2, Rancho Parcel 5, Walker Basin and Bonanza Homes.

[2004] As it had been the case in previous years, the DTS group furnished Castor with data that included cash flows prepared monthly for each of the D.T. Smith Projects, as well as information with respect to the number of sales and the sale prices, all of which was in Castor's files.

[2159] Strassberg, November 27, 2000, pp. 706-707
[2160] PW-1409, section 2
[2161] D-430.

[2005] By May, 1990, there was a significant number of unsold homes in the various D.T. Smith construction projects. To sell off the standing inventory, David T. Smith decided to proceed with voluntary auctions.

[2006] An auction was held in six D.T. Smith construction projects. For the first two auctions, the auctioned units realized close to the projected results, and the inventory of unsold houses was reduced; however, succeeding auctions proved to be considerably less successful.

- The auction at Laguna II took place on August 26, 1990. 20 units were sold at an average price per unit, net of commissions and other selling costs, of $ 278,000.[2162]

- The auction at San Marcos took place on September 9, 1990. 45 units were sold at an average price per unit, net of commissions and other selling costs, of $199,000.[2163]

- The auction at Dove Canyon I took place on October 6, 1990. 14 units were sold at an average price per unit, net of commissions and other selling costs, of $230,000.[2164]

- The auction at Dove Canyon 2 took place on October 6, 1990. 21 units were sold at an average price per unit, net of commissions and other selling costs, of $269,000.[2165]

- The auction in Chino Hills took place on October 13, 1990. 36 units were sold at an average price per unit, net of commissions and other selling costs, of $243,000.[2166]

- The auction in Wood Ranch II took place on October 21 1990. 44 units were sold at an average price per unit, net of commissions and other selling costs, of $171,000.[2167]

[2007] The auctions had a negative impact on the remainder of the D.T. Smith construction projects, particularly on the sale prices realized for the D.T. Smith homes, at sales post auctions.

[2008] By late 1990, projects were in breach of the loan covenants as a result of cost over-runs.[2168]

[2162] PW-1116-12
[2163] PW-1116-11
[2164] PW-1114-14
[2165] PW-1114-14
[2166] PW-1119-11
[2167] PW-1118-12; Ron Smith, June 11, 2008, pp. 41-42

[2009] The market conditions were poor and deteriorating throughout 1990 and the status of the DT Smith projects was precarious; Ron Smith testified to that[2169], and so did David Smith[2170], Moscowitz[2171] and Strassberg[2172], who were all personally involved with the loans to the DT Smith Group, and the status of the DT Smith projects, throughout 1990 as well as January and February, 1991.

[2010] The real estate market continued to deteriorate throughout 1990. By December 31, 1990, home prices in Southern California were dropping significantly, particularly in Orange County, where the D.T. Smith projects were located; those that were hit the hardest were the high-priced homes.

[2011] Talk of a recession was prevalent, and experts were predicting, publicly, that the residential real estate market in California would take months to recover. Several articles from the Wells Fargo Monitor retained in Castor's files in Montreal[2173] and many extracts from the Los Angeles Times, real estate section attested to those deteriorating conditions[2174].

[2012] C&L was aware of the deteriorating conditions of the real estate market prevailing in North America in 1990.

- In their "Tips & Tidbits" number 155, dated July 23, 1990, under the heading "Valuation of Real Estate", C&L specifically addresses the «*real estate market problems*», that it is «*inappropriate to assume an imminent recovery in real estate values*" and that "*we are in one of those periods where it is even more than usually important to put an objective and professional approach to*

[2168] See for example: PW-1117-5 and PW-1114-11

[2169] R. Smith, June 10, 2008, pp. 61-62, 65, 154-156, 176-177; June 11, 2008, pp. 88-89, 154-155; *Construction Projects*: Re: Dove Canyon II – June 10, 2008, pp. 82-84, 88-90; Re: Dove Canyon I - June 10, 2008, p. 187, pp.201-202, 210-211; Re: Laguna II – June 10, 2008, pp. 216-219; Re: San Marcos (The Fairways) – June 11, 2008, pp. 8-12, 32-34, 37-38; Re: Wood Ranch II (Village on the Green) – June 11, 2008, pp. 41-42, 63-65, 67-69; Re: Chino Hills (Galloping Hills) – June 11, 2008, pp. 74-75, 84-85; *Pre-Development Projects*: Re: Rancho California Miramosa – June 11, 2008, pp. 91-95, 103; Re: Rancho Parcel 2 – June 11, 2008, pp. 120-122; Re: Rancho Parcel 5 – June 11, 2008, pp. 127-128, 136-137; Re: Ritz Point – June 11, 2008, pp. 148-151; Re: Circle R. Ranch – June 11, 2008, pp. 136-137; Re: Walker Basin – June 11, 2008, p. 156.

[2170] DT Smith, March 14, 2000, pp. 168-175; March 17, 2000, pp. 778-780; October 31, 2000, pp. 1853-1858, 1881, 1883, 1958-1959, 1975-1977, 1984-1986, 1998-1999, 2063-2064, 2080-2081.

[2171] Moscowitz, December 14, 1999, pp. 202-203, 205-209, 236-237, 242-243; December 15, 1999, pp. 463, 526-528; March 8, 2000, p. 1793; March 10, 2000, pp. 2349-2350.

[2172] Strassberg, November 1, 2000, pp. 123-124; November 2, 2000, pp.228-232, 256, 259-266; November 27, 2000, pp. 556-557; November 28, 2000, p. 896-897, 901; December 1, 2000, p. 1544-1545, 1550-1552, 1555-1556; February 6, 2001, p. 1910-1911, 1913.

[2173] The Wells Fargo Monitor Publications were produced by Plaintiffs as PW-1113F, PW-1113H, PW-1113I; Defendants produced additional publications of the Wells Fargo Monitor as D-177, D-178, D-179, D-181, D-183 and D-183-1. See also R. Smith, June 10, 2008, p. 46.

[2174] PW-2908, vol.2, page H-57; Strassberg, November 28, 2000, pp. 899-905

valuation matters above maintaining the best possible relationship with clients.»[2175]

- In the same vein, in C&L's Accounting and Auditing Memorandum, AM50,[2176] C&L cautioned its auditors that «*the company may make a reasonable case that declines in value are temporary and write-downs are unnecessary. However, this approach should be accepted only if it appears that the company can maintain itself financially for the expected period until prices recover*».

[2013] As at December 31, 1990, each and every one of the DT Smith construction projects was far behind schedule: houses were not selling at the rate projected, (if at all), the prices achieved at the auctions were well below expectations, the series of auctions had lowered the sale prices that could be achieved post auction, and the residential real estate market in Southern California was bad, and getting worse.[2177]

[2014] By December 31, 1990, the Ritz Pointe project for which CHIO loan balances amounted to $30.7 million, was still in a pre-development holding stage and no improvements to the project site had yet begun.[2178] Moreover, the City had limited the density of the project (154 units instead of 191).[2179]

> by August of nineteen ninety (1990), nothing had happened, we agreed not to start the project and that was further extended over to September of nineteen ninety-one (1991).[2180]

[2015] For Ritz Pointe, two appraisals reports had been obtained:

- a January 12, 1990 report from White appraisal with an "as is" value (mass graded) as of January 3, 1990 of $26 million;[2181]
- a Clarion Appraisal Group Inc.[2182] report dated April 27, 1990 with two values:[2183]
  - an "as is" value of $29 million.
  - a value as if finished site, with finish grading and finished lots, ready for construction of houses of $35 million.

[2175] PW-1420, Tab 29.
[2176] PW-1420, Tab 33.
[2177] Ron Smith, June 10, 2008; Ron Smith, June 11, 2008; Ron Smith, September 24 2008; Ron Smith, March 27, 2009
[2178] Goodman, October 29, 2009, pp. 19-20
[2179] Ron Smith, June 11, 2008, pp.146 and following; Goodman, October 29, 2009, pp. 21-22
[2180] Ron Smith, June 11, 2008, pp.149-150
[2181] PW-1124-6
[2182] Based in Florida
[2183] PW-1124-8

- With respect of the market conditions under which they were reporting, Clarion which is a company from Florida, wrote:

> "The market for land for residential development is currently in a pronounced inflationary condition and recent demand for housing has been very strong in the Dana Point, California area. There is no way for the appraiser to estimate how long this condition will continue..."[2184]

[2016] By December 31, 1990, the Rancho California project was also in a pre-development stage and no improvement on the site had yet begun.[2185] Moreover, there were environmental issues not yet solved.[2186]

> At that point, December thirty-first (31st), nineteen ninety (1990), we had loans outstanding of twenty-one point one hundred fifty-three thousand (23.153) and we still had a long way to go to even mass-grade the lots. We hadn't even started that at that point in time. [2187]

[2017] An appraisal report dated February 12, 1989, prepared by Investors Appraisal & Realty Inc. provided the following market values:

- "As is" value: $13 million.
- As if improved with rough grading, ready for final site preparation for finished lots, ready for construction: $33.2 million.[2188]
- With respect of their proposed value of $33.2 million, the appraisers however wrote:

> Because there is not enough data determining the scope of the work to rough grade, especially since the topography of a substitutable property is indeterminate, the appraiser cannot possibly calculate more than very approximately what those costs might be. As a result, several developers were questioned as to what those costs might typically be. These costs were compared to those estimated and adjustments made accordingly. As a result, the estimated value of the land rough graded, is only furnished approximately, and with the necessarily limited accuracy a limiting condition."

[2018] As at year end 1990, CHIO's exposure to the D.T. Smith Group of Companies was $237,000,000 out of Castor's total portfolio of $1,690,000.00, or 14%.

[2184] PW-1124-8
[2185] Ron Smith, June 11, 2008, pp. 89 and following; Goodman, October 29, 2009, pp. 19-20
[2186] Goodman, October 29, 2009, p.22
[2187] Ron Smith, June 11, 2008, p.93
[2188] PW-1120-6

[2019] At the end of 1990 and the beginning of 1991, the projected unit cost for the projects where auctions had taken place exceeded the average unit sale prices achieved to date:

- As at January 3, 1991, DT Smith and Castor projected that the total costs of the Wood Ranch II project, 156 units, would be $35.4 million, or an average per unit of $227,000[2189].

- As at January 31, 1991, DT Smith and Castor projected that the total costs of the Chino Hills project, 136 units, would be $38.3 million, or an average per unit of $282,000[2190].

- As at February 1, 1991, DT Smith and Castor projected that the total costs of the San Marcos project, 126 units, would be $37.4 million, or an average per unit of $297,000[2191].

- As at February 5, 1991, DT Smith and Castor projected that the total costs of the Dove Canyon I project, 116 units, would be $36.2 million, or an average per unit of $312,000[2192].

- As at February 5, 1991, DT Smith and Castor projected that the total costs of the Dove Canyon 2 project, 106 units, would be $39.3 million, or an average per unit of $371,000[2193].

- As at February 4, 1991, DT Smith and Castor that projected the total costs of the Laguna II project, 111 units, would be $40 million, or an average per unit of $361,000[2194].

[2020] Moscowitz described the economic environment of the DT Smith projects in 1990 as follows:

> The first quarter slowed down tremendously, and we started considering alternative methods of marketing. And it got worse from that point on. The second quarter was even slower, and by the third quarter of 1990, we were losing more sales than we were gaining. So we were in a negative sales volume position. People were dropping out of contracts they had in place even the quarter before, because prices were coming down. And by the time of January and February 1991, which we're working on in 1990 as accountants for the company, it was very obvious that we were in a severe recession and there was no market that existed at that point.

[2189] PW-1118-16
[2190] PW-1119-14
[2191] PW-1117-8
[2192] PW-1115-13
[2193] PW-1114-19
[2194] PW-1116-17

> Now, we were hopeful and always hopeful that it was going to be short and we would immediately go back to large volumes and great sales prices. We were hopeful, but the reality was it didn't happen (...)
>
> ... And as we move through '90, the auctions become less and less successful. Our last auction, I think, was at Dove Canyon, or the second to last auction was our Dove Canyon property, and we had to pull some of the houses out of the auction because there wasn't enough interest in auctions even at that point.
>
> And so during this process going down from spring of 1990 to December of 1990, the prices are going down and down and down. Once we've had these auctions, the real negative -- the answer to your question is that we were never really able to sell a house at an increased price over that auction price which was somewhere around 50 or 45 percent under what we were asking for those houses. So it was a significant impact in pricing.[2195]

[2021] Actual results to mid-February, 1991, disclosed that DT Smith was not achieving its anticipated numbers of closings or its projected cash flows.[2196]

[2022] During February, 1991, Strassberg completed his audit field work for the year ended December 31, 1990. In a meeting with management (DT Smith and Moscowitz), he advised same that, in view of the poor results of the auctions, of the lower than anticipated sale prices, of the slowdown in the rate of sales, and of the decline in the residential real estate market, he had concluded that the combined financial statements of the DT Smith Group of companies must disclose a loan loss provision of US$40 to 60 million.

[2023] Strassberg explained as follows what triggered his concerns:

> The trigger for my concern was the fact that they weren't selling homes at a rate that remotely approached their own forecast. The fact that they sold at auctions doesn't by itself cause a trigger, because the auctions could have been very successful and they could have sold double the amount of homes they were projecting at prices far in excess of what they hoped to get. When that didn't happen and they sold these homes at significantly lower prices, the fact that they sold them at lower prices would cause my concern. The fact that in between the periods from the end of '89 until the end of 1990, that for the most part the only home sales they did have were at auction and that they were at significantly lower prices than they hoped to get, would also cause me to have some concern about their ability to sell homes at a profit on a going forward basis.[2197]

[2195] Moscowitz, December 14, 1999, pp. 205, 206 and 209

[2196] For example, see: PW-1119-15 (Chino Hills); PW-1114-19 (Dove Canyon II); PW-1117-8 (San Marcos); PW-1116-17 (Laguna II)

[2197] Strassberg, November 28, 2000, pp. 896-897 (see also Strassberg, November 2, 2000, p. 261)

[2024] Strassberg, of Rogoff & Company, who was the partner in charge of the audit of the D.T. Smith Group of Companies, considered the D.T. Smith entities and projects to be in serious financial difficulties. He refused to sign, or issue, an audit opinion for the financial statements of the D.T. Smith Group, unless they disclosed a loan loss provision in the range of US$40 to US$60 million.

[2025] Strassberg,[2198] DT Smith[2199] and Moscowitz[2200] all support the assertion that Strassberg reached this conclusion in February, 1991, and the Court finds those testimonies credible and reliable.

[2026] At the request of David Smith and Moscowitz, who both hoped that the real estate market conditions would improve in 1991, the David T. Smith Group combined financial statements for December 31, 1990 were not finalized. Their hopes did not materialize; the residential real estate market in Southern California did not improve in 1991, and the results remained far below projections.

[2027] The audited combined financial statements of the DT Smith Companies for 1990, with the audit opinion dated February 2, 1992,[2201] were not finalized and issued until February 1992. These financial statements disclosed a net loss of US$56,135,673 and the independent auditor's report by Rogoff & Company raised "*substantial doubt about the company's ability to continue as a going concern.*"

[2028] At the end of May or at the beginning of June, 1991, and for the very first time, David T. Smith prepared and forwarded to Castor a personal statement of net worth.[2202] One of the assets listed was a house, having a stated value of $12,500,000.00; such house was not the property of David T. Smith, but rather that of his wife, Norma. Cash listed in the amount of $6,450,000.00 was restricted and therefore, not available to creditors (including CHIO) of David T. Smith.

Loan as of December 31,1990

[2029] Castor's total exposure to DT Smith loans as of December 31, 1990 amounted to US $217.6 million:

- Laguna I – U.S. $1.6 million[2203]
- Laguna II – U.S. $ 18.6 million[2204]

[2198] Strassberg, November 2, 2000, pp. 261-263, 265-266, 271-272; November 28, 2000, pp. 801-803, 819, 830-831, 863-864, 931-932; November 29, 2000, pp. 1143, 1152; December 1, 2000, p. 1631; February 6, 2001, pp. 1910, 1913; February 9, 2001, pp. 2608-2609.

[2199] DT Smith, March 14, 2000, pp. 189-191.

[2200] Moscowitz, December 14, 1999, pp. 193, 198-200, 217; December 17, 1999, pp. 1053-1055; March 9, 2000, pp. 2114-2115; March 13, 2000, p. 2458.

[2201] PW-2319, bates p. 000003.

[2202] D-175; D-175-1 D-175-2

[2203] PW-1053-81, sequential page 79

- San Marcos – U.S. $17.5 million [2205]
- Wood Ranch 2 – U.S. $ 16.2 million[2206]
- Dove Canyon 1 – U.S. $ 16.2 million[2207]
- Dove Canyon 2 – U.S. $ 20.6 million[2208]
- Chino Hills – U.S. $ 17.7 million[2209]
- Ritz Point – U.S. $ 30.7 million[2210]
- Rancho Parcel 2 – U.S. $ 9.9 million[2211]
- Rancho Parcel 5 – U.S. $ 10.2 million[2212]
- Rancho California – U.S. $20.2 million[2213]
- Circle "R" Ranch – U.S. $ 13.1 million[2214]
- Walker Basin – U.S. $ 11.5 million[2215]
- Bonanza Homes – U.S. $ 1.6 million[2216]

Experts' opinions

Vance and Froese

[2030] According to Vance, the minimum loan loss provision for the loans extended to the DT Smith Companies was CDN$47.7 million for the DT Smith construction projects, plus CDN$8.3 million for the Rancho California pre-development loans. The details are noted in the following charts, in US$[2217]:

[2204] PW-1053-81, sequential page 79
[2205] PW-1053-81, sequential page 79
[2206] PW-1053-81, sequential page 79
[2207] PW-1053-81, sequential pages 78, 79,
[2208] PW-1053-81, sequential pages 78, 79A
[2209] PW-1053-81, sequential pages 78, 79A
[2210] PW-1053-81, sequential pages 78, 81
[2211] PW-1053-81, sequential pages 81
[2212] PW-1053-81, sequential pages 78, 81
[2213] PW-1053-81, sequential pages 78, 80
[2214] PW-1053-81, sequential pages 79
[2215] PW-1053-81, sequential page 80
[2216] PW-1053-81, sequential page 79
[2217] Conversion : Cdn. at 1.16 (PW-2908, vol.5)

Construction projects (in US$)			
Project	Total net proceeds (per Vance)	Total costs with Castor's financing costs included (per Vance)	Minimum Surplus (deficiency)
Laguna II[2218]	$34 million	$40 million	($6 million)
San Marcos[2219]	$29 million	$37.5 million	($8.5 million)
Wood Ranch II[2220]	$29.5 million	$33.4 million	($3.9 million)
Dove Canyon I[2221]	$29.2 million	$36.2 million	($7 million)
Dove Canyon II[2222]	$27.8 million	$39.4 million	($11.6 million)
Chino Hills[2223]	$34.6 million	$38.4 million	($3.8 million)

Development projects (in US$)			
Project	Value of Castor's collateral (per Vance)	Loan balances owed to CHIO	Surplus (deficiency) (low, mid-point and high)
Rancho California[2224]	$13 million	$20.1 million	($7.1 million)

[2218] PW-2908, vol. 3 pp.75 and following
[2219] PW-2908, vol. 3 pp.65 and following
[2220] PW-2908, vol. 3 pp.58 and following
[2221] PW-2908, vol. 3 pp.68 and following
[2222] PW-2908, vol. 3 pp.71 and following
[2223] PW-2908, vol. 3 pp.61 and following
[2224] PW-2941, vol.5, p.79

[2031] Froese opined that the estimated security shortfall for the loans to the DT Smith entities, as at December 31, 1990, ranged from a low of CDN$48 million, to a mid-point of CDN$56 million, to a high of CDN$63 million.[2225] The details are enunciated in the following charts, but in US$:

Construction projects (in US$)			
Project	Total net sales proceeds (per Froese)	Total costs no Castor's financing costs included	Minimum Surplus (deficiency)
Laguna I	Not discussed by Froese		
Laguna II[2226]	$32.7	$39.3	($6.6)
San Marcos[2227]	$27.1	$36.2	($9.1)
Wood Ranch II[2228]	$27.9	$33.7	($5.8)
Dove Canyon I[2229]	$28.1	$34.1	($6.0)
Dove Canyon II[2230]	$28.1	$36.7	($8.6)
Chino Hills[2231]	$34.2	$37.4	($3.2)

[2225] PW-2941, vol. 5, pp. 58 and 100
[2226] PW-2941, vol. 5 p. 97
[2227] PW-2941, vol. 5, p. 89
[2228] PW-2941, vol.5, p. 83
[2229] PW-2941, vol. 5. p. 73
[2230] PW-2941, vol.5, p. 78
[2231] PW-2941, vol.5,

Development projects (in US$)			
Project	Value of Castor's collateral (per Froese)	Loan balances owed to CHIO	Surplus (deficiency) (low, mid-point and high)
Bonanza Homes	Not discussed by Froese		
Circle "R" Ranch[2232]	Acquisition price July 1989 $11.4 million (no appraisal)	$13 134,540	No final conclusion reached
Rancho California[2233]	Appraisal "as is" value $13 million	$20,153,604	$7.2
Rancho Parcel II[2234]	Appraisal "as is" value $9.8 million	$9,897,060	---
Rancho Parcel V[2235]	Appraisal "as is" value $ 10 million	10,242,269	---
Ritz Point[2236]	Two appraisals "as is" $26 $29	30,743,316	$1.7, $3.2, $4.7
Santiago Ranch	Not discussed by Froese		
Walker Basin[2237]	No appraisal	$11,539,715	No conclusion reached

[2232] PW-2941, vol.5, pp. 121-123
[2233] PW-2941, vol. 5, pp.110-113
[2234] PW-2941, vol. 5, pp. 114-117
[2235] PW-2941, vol.5, pp. 118-120
[2236] PW-2941, vol.5, pp.104-109
[2237] PW-2941, vol.5, pp. 124-125

[2032] Froese's loan loss provisions were predicated *«on the assumption that CHIO would also place the loans secured by these projects on a non-accrual basis (no longer recognizing capitalized interest as income), and disclosing the extent of non-performing loans in the notes to the financial statements.* »[2238]

[2033] To determine if a loan loss provision was necessary, Vance opined that each project had to be considered separately. Given the facts as they unfolded, Vance said that GAAP did not permit a loss on one project to be offset against the profit on another distinct project.[2239] C&L's own internal materials are consistent with Vance's opinion.[2240]

[2034] Because of the unique circumstances of these DT Smith loans where there was common ownership and a common guarantor and a precedent for the application of a surplus, it was Froese's view that it was arguable that surplus from one project could be offset against the deficiency on another.[2241]

[2035] Both Vance and Froese opined that because the loans to the DT Smith Companies were impaired and clearly required massive write-downs in 1990, all the capitalized interest and fees in connection with such projects for 1990 should have been reversed.[2242] The required reversals of revenue for 1990 amounted to $16.5 million.[2243]

Goodman

[2036] In his report, and based on the alleged values and ability to offset a deficiency on one DT Smith project against a surplus on another, Goodman opined that no additional loan loss provisions were required under GAAP in respect of these loans[2244].

[2037] Based on the figures reproduced in the following charts, Goodman concluded that there was a surplus of US$9.3 million on the construction projects and a surplus of US$17.5 million on the development projects:

[2238] PW-2941, Vol. 5, p. 58.
[2239] Vance, April 12, 2010, pp. 255-256.
[2240] PW-1420, Tab 33.
[2241] PW-2941, Vol. 5, pp. 3-4.
[2242] PW-2941, Vol. 5, p. 7.
[2243] PW-1485-2-90-2.
[2244] D-1312, p. ES-30.

Construction projects (in US$)			
Project	Value of Castor's collateral (per Goodman)	Loan balances owed to CHIO	Surplus (deficiency)
Laguna I	$1.8	$1.6	$0.2
Laguna II	$18.8	$18.8	-
San Marcos	$16.7	$17.5	($0.8)
Wood Ranch II	$17.7	$16.2	$1.5
Dove Canyon I	$18.1	$16.2	$1.9
Dove Canyon II	$23.0	$20.6	$2.4
Chino Hills	$21.5	$17.5	$4

Development projects (in US$)			
Project	Value of Castor's collateral (per Goodman)	Loan balances owed to CHIO	Surplus (deficiency)
Bonanza Homes	$1	$1	-
Circle "R" Ranch	$14.7	$13.1	$1.6
Rancho California	$23.4	$20.2	$3.2
Rancho Parcel II	$9.4	$9.9	($0.5)
Rancho Parcel V	$9.9	$10.2	($0.3)
Ritz Point	$32.6	$30.7	$1.9
Santiago Ranch	$14.6	$12.6	$2.0
Walker Basin	$11.8	$11.5	$0.3

Differences between experts

[2038] The difference in value attributed to the remaining unsold units in various projects significantly explains the differences between the value of Castor's collateral security determined by Goodman and those determined by Vance or Froese.

[2039] The following chart illustrates some of those differences, in US$:

Project	Average as at December 31, 1990 (per unit and including auction pricing)	Vance's figures (per unit)	Froese's figures (adjusted auction pricing and per unit)	Goodman's figures (net proceeds and per unit)
Chino Hills	$273,111[2245]	$255,000[2246]	$254,514[2247]	$287,000[2248]
Dove Canyon 1	$272,796[2249]	$252,000[2250]	$247,464[2251]	$289,000[2252]
Dove Canyon II	$233,059[2253]	$263,000[2254]	$278,026[2255]	$345,000[2256]
Wood Ranch II	$197,129[2257]	$189,000[2258]	$178,955[2259]	$217,000[2260]
San Marcos	$227,444[2261]	$227,000[2262]	$209,789[2263]	$298,000[2264]
Laguna II	$311,581[2265]	$306,000[2266]	$293,000[2267]	$351,000[2268]

[2245] PW-2941, vol. 5, p.64
[2246] PW-2908, vol. 3, pp. 61-62
[2247] PW-2941, vol. 5, p.64; D-1312, p.632 (auction pricing at $242,000 net)
[2248] D-1312, p. 632 (average calculated as follows : net proceeds of $29,568 divided by 103 units), p.684
[2249] PW-2941, vol. 5, p.73
[2250] PW-2908, vol.3, pp.68-69
[2251] PW-2941. Vol.5, p.73
[2252] D-1312, p.678
[2253] PW-2941. Vol.5, p.78
[2254] PW-2908, vol. 3, pp.71-72
[2255] PW-2941. Vol.5, p.75-76
[2256] D-1312, p.681
[2257] PW-2941. Vol.5, p.83
[2258] PW-2908, vol. 3 pp. 58-59
[2259] PW-2941. Vol.5, p.83
[2260] D-1312, p. 675, 700
[2261] PW-2941, vol 5. p.89
[2262] PW-2908, vol. 3, pp.65-66
[2263] PW-2941, vol 5. p.89
[2264] D-1312, p.600 and 604 (average calculated as follows : net proceeds of $19,694 divided by 66 units), p.672
[2265] PW-2941, vol.5, p.97
[2266] PW-2908, vol. 3 p.78

[2040] Had Goodman used figures closer to the ones proposed by Vance and Froese, Goodman would have found also that Castor had to take a significant (material) LLP in 1990.

[2041] Another difference between the conclusions of Vance, Froese and Goodman relates to the inclusion, or exclusion of future interest payable to Castor during the period of completion of the DT Smith projects, in the calculation of the costs to complete.

- Vance includes future interest income on the basis that it forms part of the costs to complete the projects, as shown on the cash flow projections.

- Froese concludes that: *« it is appropriate for the best estimate of the probable loss related to the D.T. Smith loans to include, at a minimum, future interest payable by Castor on its loan to BVAG and BHF Bank.»*[2269]

- In his 2008 report, Goodman acknowledges that he used the same methodology as Vance and Froese for his 1998 report.[2270] By reversing his opinion from his 1998 report, to his 2008 report, and eliminating future interest income from the cost to complete the DT Smith projects, and eliminating future interest income from the cost to complete the DT Smith projects, Goodman has increased his best estimates of value by approximately $16 million.[2271]

Conclusions

[2042] The real estate market conditions in California were deteriorating.

[2043] As at December 31, 1990 (more than two months after the last of the auctions), the prices achieved at the auctions of the construction projects reflected the then current market conditions, a fact that Strassberg (DT Smith's auditor) recognized and acknowledged.

[2044] It would not have been reasonable under GAAP for an auditor to accept Goodman's suggested average net proceeds per unit for the construction projects.

[2045] Taking into account the content of the available appraisals and the testimony of Ron Smith relating to the state of those projects, it would not have been reasonable either under GAAP to value the Rancho California project at $23.4 million and the Ritz Pointe project at $32.6 million, as Goodman did.

- The value of $13 million had to be used for Rancho California.

[2267] PW-2941, vol.5, p.97
[2268] D-1312, p.669
[2269] PW-2941, Vol. 5, p.7.
[2270] 1998 Report of R. Goodman, p. 574.
[2271] D-1312, p. 658

- The value of $26 million was applicable to Ritz Pointe.

[2046] Had Goodman used these figures, he might have had a deficiency instead of a US$17.5 million surplus for the development projects.

[2047] Plaintiff expert's opinions prevail.

- Castor should have taken a huge LLP (at least CDN$40 to $50 million).
- Future interest payable had to be included in the computation, at least up to the amounts that Castor would have had to pay to its own lenders, as suggested and calculated by Froese.

Diversion of fees (1988, 1989 and 1990)

[2048] Above and beyond the previous detailed reasons, the consolidated audited financial statements of Castor for 1988, 1989 and 1990 were also materially misstated as a result of a diversion of fees.

Positions (in a nutshell)

Plaintiff

[2049] Plaintiff alleges that $15.1 million of commissions or fees payable to CHIO were diverted to Stolzenberg, David Smith, and Gambazzi's and Bänzinger's related corporations, during 1988, 1989 and 1990.

[2050] Plaintiff argues that had C&L performed their audits in accordance with GAAS, they would have discovered the situation and questioned the good faith of management.

[2051] Plaintiff mentions that no evidence establishes that there would have been a fee sharing arrangement; to the contrary, the evidence indicates that the fees were diverted from CHIO.

[2052] Therefore, Plaintiff concludes that the consolidated audited financial statements of Castor for 1988, 1989 and 1990 are materially misstated.

Defendants

[2053] Defendants allege that the issue of the "diversion" of the DT Smith fees raises at least four questions:

- First, was there a fraudulent diversion of fees or were the amounts that were transferred to Stolzenberg, David Smith and to different entities, which may or may not have been related to Gambazzi and Bänziger, a fee sharing arrangement?
- Second, was the audit of these fees a completeness of revenue test as suggested by Plaintiffs or a cut off test as suggested by Defendants?
- Third, should the "diversion" of these fees have been detected by ordinary GAAS?
- Fourth, were the financial statements misstated by the non-inclusion of these fees in income?

[2054] To the first question, Defendants answer that the evidence is not clear but if the Court comes to the conclusion that cash payments were made to Stolzenberg, David Smith and the various entities, and that these payments were kicked back from the DT Smith fees, then this was a fraud on C&L.

[2055] To the second question, Defendants answer that the audit of these fees was a cut off test, not a completeness of revenue test.

[2056] To the third question, Defendants answer no, since none of the tracings that were required for Plaintiffs' experts to identify the fee diversion is ordinary GAAS.

[2057] To the fourth question, Defendants answer that there is no evidence in the record that the financial statements were misstated. To support their answer, they rely on the following extract of the testimony of Selman:

> A- So the whole thing is just this huge amount of transactions whi.ch are not very clearly identified and out of which Mr. Vance has picked out the CHIO fees and said those went to Stolzenberg and Smith. And I just don't think that the evidence is that clear. So there are many conflicting possibilities and it's difficult to support Mr. Vance's conclusion that they all started with monies that CHIO transferred to CH Cyprus.
>
> Q- Okay. Mr. Selman, assuming the Court concludes that Mr. Vance's explanations are more likely explanations, how would that have changed the accounting treatment for the payments to Mr. Stolzenberg?
>
> A- Well, I describe Mr. Vance's view in 6.13.12 of my report. From a perspective of the accounting, as I said I don't think it could be said with assurance that the fees were intended to belong to CHIO and therefore it may not have been correct to characterize the onward transfers as Mr. Vance says as CHIO expenses. But even if the transfers were accounted for that way, this would not change the net financial result from that which was reported. There would be simply more revenue and a fully offsetting expense.

The materiality of them wouldn't be very consequential in their net result because there would be essentially a wash.

I do agree that if the transactions were advances that were intended to be repayable and therefore would have been appropriately recorded as an asset in the first instance, there would be a need to determine whether they could have been collected. In other words, if the monies belonged to CHIO, CHIO should have shown more revenue, but it would have had to then report either an expense representing the transfers to Mr. Stolzenberg and Mr. Smith which would wash out that portion of the revenue that wasn't being retained by it or it would have had to say in its accounts: "These monies were taken by Mr. Stolzenberg and Mr. Smith. They belong to us to go on our balance sheet as an asset".

Now, are they collectible from Stolzenberg and Smith?

Now, no question that in recording them as an advance in that manner, they're recording them as something which they didn't agree to presumably on Mr. Vance's construction of the situation. But nonetheless, from an accounting standpoint, they would amounts owing to CHIO and they would have to be set up in the accounts in that manner.

And then the question would have to be dealt with.

Now, obviously, this bypasses the entire question of what would have occurred if it would come to the attention of the auditors that there were these amounts and the amounts belong to OHIO and were being in effect. . . there was in effect a defalcation or a theft of them.

So, in summary, I'm saying that I've looked at in all and I cannot give you a firm conclusion that the CHIO fees were in fact a theft by Mr. Stolzenberg and Mr. Smith from CHIO or that you can in fact trace, through the "Various" account, the monies coming from CHIO into the "Various" account as going out to Mr. Stolzenberg and Mr. Smith because the evidence that you have just doesn't permit that kind of conclusion.

> And Mr. Vance - and we'll see the reaction of the other experts - but Mr. Vance has agreed that he cannot exclude the possibility that this was essentially a fraud in the United States Treasury and that this was an artificial way of Stolzenberg and Smith taking money out of the D.T. Smith Group of companies.[2272]

Evidence

[2058] The loan documentation evidencing the agreements entered into between CHIO and the DT Smith entities refer to very substantial placement and renewal fees payable by the DT Smith companies to CHIO.[2273]

[2059] All placement and renewal fee revenue was to be paid to CHIO [2274]– there is no reference that such revenue was to be shared with any other entity or individual.

[2060] CHIO was funding 100% of all costs, fees and expenses relating to the DT Smith projects. Thus, CHIO was also funding the placement and renewal fees that it was charging to the DT Smith companies.

[2061] Each time CHIO would advance funds to the DT Smith companies, a portion of the advance would include the placement fee.[2275]

[2062] For 1988, 1989 and 1990, a total of US$27.9 million was collected by CHIO as fees generated from its loans to the DT Smith companies. Of that amount, only US$12.9 million was recognized as revenue by CHIO: the balance, namely US$15.1 million, was not recognized as income by any Castor company[2276] and was ultimately transferred to CHIF's "Various US" current account.[2277]

[2272] Selman, May 22, 2009, pp.47-49

[2273] PW-1114 to PW-1123; See, for example, re- Dove Canyon II : PW-1114-1; PW-1114-2B; PW-1114-3B; PW-1114-12B.

[2274] Gourdeau, January 29, 2008, pp.77 and following; PW-1114 to PW-1123

[2275] See, for example, PW-1114-4, with respect to Dove II, where CHIO's advance of $7,860,825.54 on June 2, 1988 included an amount of $2 million as "placement fees to be sent back to C.H. Overseas". Gourdeau, January 29, 2008, pp.79 and following.

[2276] PW-2893-132; D-1347, p.120. These amounts match, exactly, the amounts set out in PW-2893-132, within PW-2908, Vol. 1, pp. 6-47, 6-56, 6-57, 6-59. See also Gourdeau, January 29, 2008, pp. 77 and following; Gourdeau, February 25, 2008, pp.162-163

[2277] PW-2893-132.

[2063] Those amounts are more fully described in the following three exhibits of Vance's report [2278] entitled "*Analysis of fee revenue from D.T. Smith Projects*" :

Year end December 31, 1988

Exhibit 1

ANALYSIS OF FEE REVENUE FROM D. T. SMITH PROJECTS
YEAR ENDED DECEMBER 31, 1988

Name of Project	Total Fees Collected and as set out in Loan Agreements	Recognized as Fee Revenue	Transferred to Other Parties
Dove Canyon I**	U.S. $ 2,000.000	U.S. $1,000.000	U.S. $1.000.000
Dove Canyon II**	2,000.000	1,000.000	1,000.000
Tennis Court Villas**	2,000,000	1,000,000	1,000,000
Wood Ranch II**	2,000,000	1,000,000	1,000,000
Gordon Ranch (Chino Hills)**	2,000.000	1,000,000	1,000,000
Laguna I	* 300,000	100,000	200,000
Dove Canyon I**	* 250,000	83,333	166,667
Dove Canyon II**	* 250,000	83,333	166,667
	U.S. $10,800,000	U.S. $ 5,266,666	U.S. $ 5,533,334

* Original deposit recorded as revenue in total and journal entry subsequently recorded to remove a portion of fee revenue and credit this amount to intercompany account.

** New loan in 1988 as per **B3** and **B4** (PW-1053-84-10).

[2278] PW-2908, vol. 1, pages 6-57, 6-58 and 6-59

Year end December 31, 1989

Exhibit 2

ANALYSIS OF FEE REVENUE FROM D. T. SMITH PROJECTS
YEAR ENDED DECEMBER 31, 1989

Name of Project	Total Fees Collected and as set out in Loan Agreements	Recognized as Fee Revenue	Transferred to Other Parties
Rancho California**	U.S. $ 3,600,000	U.S. $1,200.000	U.S. $2,400,000
Gordon Ranch (Chino Hills)	* 500.000	166,667	333,333
Walker Basin**	2,000,000	1,000,000	1,000,000
Rancho California**	* 400,000	133,333	266,667
Laguna I	* 350,000	116,667	233,333
Circle "R" Ranch	1,000,000	500,000	500,000
Rancho Parcel 2*	1,000,000	500,000	500,000
Rancho Parcel 5*	1,000,000	500,000	500,000
	U.S. $ 9,850,000	U.S. $ 4,116,667	U.S. $ 5,733,333

* Original deposit recorded as revenue in total and journal entry subsequently recorded to remove a portion of fee revenue and credit this amount to intercompany account.

** New loan in 1989 as per B5 and B6 (PW-1053-83-6).

Year end December 31, 1990

Exhibit 3

ANALYSIS OF FEE REVENUE FROM D. T. SMITH PROJECTS
YEAR ENDED DECEMBER 31, 1990

Name of Project	Total Fees Collected and as set out in Loan Agreements	Recognized as Fee Revenue	Transferred to Other Parties
San Marcos	U.S. $ 800,000	U.S. $ 400,000	U.S. $ 400,000
Laguna II	1,500,000	600,000	900,000
Ritz Point	3,000,000	1,500,000	1,500,000
Walker Basin	2,000,000	1,000,000	1,000,000
	U.S. $ 7,300,000	U.S. $ 3,500,000	U.S. $ 3,800,000

[2064] Entries in Castor's books and records clearly show that the amounts transferred from CHIO by inter-company transactions to CHIF's "Various US" current account represent a portion of the placement fees from CHIO's loans to the DT Smith companies.[2279]

[2065] From CHIF's "Various US" current account, a number of cash payments were made to Stolzenberg personally (totalling US$4,741,168), David Smith personally (totalling US$1,141,502). There were as well as transfers or credits to the account of Interglob (totalling US$6,629,787), and to Fianico/ c/o Marco Gambazzi (totalling US$2,832,906).[2280]

[2066] Additional supporting documents, such as bank statements, telexes and payment vouchers, are proof of the diversion of a significant portion of the fee income of the DT Smith companies.[2281]

[2067] The entries recording the transfers from CHIO to CH Cyprus, and thence to CHIF's "Various US" current account, make it clear that the amounts being transferred

[2279] See PW-2893-132.
[2280] PW-2908, Vol. 1, pp. 6-60, 6-61, 6-62 and 6-63.
[2281] PW-1776; PW-1777; PW-1780 (OSR #248 dismissed); PW-1781; PW-1782.

were placement fees relating to the DT Smith projects.[2282] Indeed, the entries relating to these transfers specifically refer to the transfer of placement fees, and name the specific DT Smith project.[2283]

[2068] C&L Cyprus were preparing statutory financial statements for the Cyprus entities of Castor, namely CHIO.

[2069] Each year, C&L Cyprus wrote to C&L asking them to perform various procedures or to confirm the results thereof.

- In relation to C&L's 1988 audit, C&L Cyprus wrote on January 16, 1989 and C&L answered on March 1, 1989. In her answer, Ford mentioned the following at item # 5 "*Reviewed loan (receivable/payable) documentation on a test basis. Sample included all new loans receivable entered into in the year*".[2284]

- In relation to C&L 1989 audit, C&L Cyprus wrote on January 29, 1990[2285]. C&L Cyprus namely asked as their demand # 4 "*for commissions (received/payable) agree details and amounts to relevant documentation*" and as their demand # 6 "*for all loans (given/obtained) agree terms to the relevant documentation*". On February 12, 1990, C&L answered[2286]. In her answer, Ford mentioned the following in relation to item # 4 "*On a test basis, agreed details of commissions (received/payable) to supporting documentation*" and the following in relation to item # 6 "*Reviewed loan (receivable/payable) documentation on a test basis. Sample included all new loans receivable entered into in the year*"[2287].

- In relation to the C&L 1990 audit, C&L Cyprus wrote on August 2, 1991, making the same demands as the one made the previous year[2288]. The audit working papers include information that C&L would have sent them on February 5, 1991, i.e. in relation to item # 4 "*On a test basis, agreed details of commissions (received/payable) to supporting documentation*" and the following in relation to item # 6 "*Reviewed loan (receivable/payable) documentation on a test basis. Sample included all new loans receivable entered into in the year.*"[2289]

[2282] PW-2908, Vol. 1, pp. 6-45, 6-46.
[2283] See, for example, PW-145A, Vol. 2, bates #055884, entries recorded on August 31, 1989 relating to Circle R. Ranch, Rancho Parcel 2 and Rancho Parcel 5, and PW-145A, Vol. 2, bates #055883, entries recorded on May 31, 1989, relating to Walker Basin.
[2284] PW-1053-84, sequential pages 11-12
[2285] PW-1053-83, sequential pages 62-65
[2286] PW-1053-83, sequential pages 53-54
[2287] PW-1053-83, sequential pages 53-54
[2288] PW-1053-81, sequential pages 33-36
[2289] PW-1053-81, sequential pages 51-52

[2070] On September 5, 1996, at discovery, concerning the work she would have done at the request of C&L Cyprus in relation to commissions and fees payable to CHIO, Ford testified as follows:

> On a test basis agreed details of commissions, in brackets "receivable/payable" to supporting documentation".[2290] it would have been something that I did.[2291] That is the work that I performed while I was on site.[2292]
>
> Q- And you say that you agreed the commissions?
>
> A On a test basis, yes.[2293]
>
> My recollection of what I did in 1989, was that when I was reviewing the loan files the information would have been available to me at the time to ensure if it there was a commission due or payable or receivable, and I would have, on a test basis, looked at those.[2294]
>
> Q-Apart from the fact that you represent in the letter that, you did, is there any evidence of what work you did?
>
> A- No, Sir.[2295]
>
> I verified to documents but not to cash receipts.[2296] I do not recall doing it for those – for commissions, Sir. I know I recall doing it for interest. Though I may have.[2297]

[2071] On December 8, 2009, thirteen years later, Ford testified at trial that she only did a cut-off test, not a completeness test. She alleged not to have been required to perform a completeness test.[2298]

[2072] In December 1989, February 1990 and June 1990, during their preparation of their stand-alone 1988 financial statements, C&L Cyprus sent telexes to Bänziger requiring an explanation as to why the commission income (placement fees) earned were different from the amounts recorded in the records of CHIO[2299].

[2290] Ford, September 5, 1996, p.94
[2291] Ford, September 5, 1996, pp.94-95
[2292] Ford, September 5, 1996, p. 95
[2293] Ford, September 5, 1996, pp. 95-96
[2294] Ford, September 5, 1996, p.96
[2295] Ford, September 5, 1996, p.96
[2296] Ford, September 5, 1996, p.102
[2297] Ford, September 5, 1996, p.102
[2298] Ford, December 8, 2009, pp.30-52
[2299] PW-1530-1A; PW-1530-1B

[2073] On June 22, 1990, Bänziger sent the following answer to C&L Cyprus:

> Commissions
>
> We cannot comment as to the discrepancies between information you had from loan documents to amounts received. It happened from time to time that commission agreements are changed subsequent to the first negotiation, depending upon the specific situation."[2300]

[2074] David Smith admitted having received part of the fees that his companies had to pay to CHIO according to the loan agreements, as follows:

> "Q. I certainly will ask you, Mr. Smith, it's marked in favour of D. Smith. The D. Smith there is who?
>
> A. Me.
>
> Q. And did you maintain a personal account in London at that account number?
>
> A. Yes.
>
> Q. What was the reason for the payment?
>
> A. According to an agreement I had with Mr. Stolzenberg, he agreed to return a portion of the placement and/or extension fees to me.
>
> Q. To you personally?
>
> A. Yes.
>
> Q. And this is how it was paid and when it was paid?
>
> A. Yes."[2301]

[2075] Gourdeau, Castor's Trustee in bankruptcy, thought at first that the inter-corporate transfers between CHIO and CHIFNV were done in order to save taxes,[2302] but he traced the flow of funds through the various Castor accounting records and uncovered the transfers to Stolzenberg and David Smith.

[2300] PW-1530
[2301] David Smith, March 14, 2000, p. 208
[2302] Gourdeau, January 29, 2008, pp. 147-148

Experts' evidence

Vance

[2076] Vance testified that some completeness test on the revenue was done by the Montreal audit team, for CHL, but that none was done by the overseas audit team for CHIO.[2303]

[2077] Vance mentioned that the largest source of placement fees for Castor was the DT Smith Group, and that CHIO was its receiver according to the loan documentation.

[2078] Vance opined that it would have been easy to do a completeness test on the fees owed to CHIO, and that it was required to audit in accordance with GAAS[2304]. Vance added that the diversion of fees would have been obvious, if it had been done.[2305]

[2079] Vance described the test that should have been performed as follows: "*the test is to look at what the revenue should be from the documents, the loan documents, particularly for placement fees, and then to track that revenue and see that it is actually collected*".[2306]

[2080] Vance opined that the completeness test was "*not forensic accounting by any way, shape or form, it's just standard auditing and following the audit trail*".[2307]

[2081] Vance noted that "*The diversion of fees started in nineteen eighty-eight (1988), eighty-nine ('89) and ninety ('90), and the money was paid out to diverted in effect, and the balance at the end of ninety ('90) arrived at exactly the same amount to the penny that it was in nineteen eighty-seven (1987)*".[2308]

[2082] Vance confirmed that he had effectively verified all the entries in Castor's books and records pertaining to the diversion of fees.[2309]

[2083] Vance opined that "*The proper accounting treatment to disclose what had taken place would have been to either record the full amount of the fee revenue and then record, as a properly described expense, the payments to the other parties while also disclosing as related party transactions the payments to Wolfgang Stolzenberg*". He however proposed that an alternative treatment could have been "*to record the full fee revenue and then record the payments and transfers of credits as receivable from the*

[2303] Vance, April 7, 2008, pp.94-99
[2304] Vance, April 7, 2008, pp.93 and following
[2305] Vance, March 13, 2008, pp.204-207; Vance, April 7, 2008, pp.99 and following; Vance, May 12, 2008, pp.60 -62; Vance, June 12, 2008, pp.86-121
[2306] Vance, March 13, 2008, p.204
[2307] Vance, March 13, 2008, p.206; Vance, April 16, 2008, pp.91-93; Vance, June 12, 2008, pp.95-96
[2308] Vance, March 13, 2008, p. 205
[2309] Vance, April 7, 2008, p.101

recipients. The likelihood of ever collecting these amounts would then have to be taken into consideration. If collection was doubtful, a provision for loss would have to be recorded, in which case, the net result would be the same as if the payments and transfers of credits were directly recorded as expenses. The receivables from Mr. Stolzenberg (...) would be shown as receivables from related parties". [2310]

[2084] Vance retained that the amount of the misstatements represented by the understatements of revenue for 1988, 1989 and 1990 far exceeded the preliminary materiality assessments established by C&L and using C&L preliminary assessments of materiality, he concluded that the financial statements were materially misstated.[2311]

[2085] Vance concluded that "*Had C&L performed the appropriate audit procedures, they would have been obliged to raise questions regarding the possibility of collusion between management and a significant borrower, the failure to disclose related party transactions, and Castor being deprived of a material amount of revenue. These issues would also have served as "red flags" to the auditors to conduct additional audit procedures to determine whether there were similar issues in other areas of their audit and to question the integrity of management.*".[2312]

[2086] During his cross-examination, Vance explained that the auditors were not defrauded, even if the diversion of fees was or could be a misappropriation of the company's funds[2313] since nothing was concealed from them[2314].

[2087] During his cross-examination, Vance acknowledged that the diversion of fees would have no impact on the income statement of the financial statements, as follows: "*the net effect on the income statement is zero because if you have... the accounting treatment when you come across misappropriation is you could either record it and set up the revenue, set up a receivable from the recipient, and then you would have to write off that receivable as being unlikely of being collected, so the impact on the income statement is nil in the balance sheet.*"[2315]

Froese

[2088] Froese asserted that Ford was requested by C&L Cyprus, who were performing a stand-alone audit of CHIO, to perform a test which, if done correctly, should or would have allowed her to detect the diversion of fees.[2316]

[2310] PW-2908, volume 1, p. 6-49
[2311] PW-2908, volume 1, p. 6-50
[2312] PW-2908, volume 1, p. 6-56
[2313] Vance, June 12, 2008, pp.87-94
[2314] Vance, May 12, 2008, pp.32-36
[2315] Vance, June 12, 2008, p.97
[2316] PW-2941, vol.5, pp. 190 and following; Froese, December 2, 2008, pp.123-127; Froese, December 8, 2008, pp. 184 and following;

[2089] During his cross-examination, Froese acknowledged that it was possible to read the procedure to be performed by Ford as a cut-off test,[2317] but he nevertheless maintained that Ford had to look at the loan agreements.[2318]

[2090] During same cross-examination, after having reviewed Ford's testimony on discovery and acknowledged that it was confusing to some extent, Froese reiterated that Ford " *did some on a test basis, in which case she either got it wrong, she got it wrong each time, or she didn't do the work at all, in which case it should have been done*" [2319].

[2091] Froese admitted that, to comply with GAAS, C&L needed not "*to trace the commission income through all the books and records of Castor unless there was something that would raise their suspicion*". [2320]

Selman

[2092] Selman agreed that the «*recognition of fee income on the David T. Smith Group loans*» is set out in the 1st and 2nd mortgages, entered into between CHIO and the DT Smith entity, and he cited, as an example, the 1st and 2nd mortgage loan agreements relating to the Dove I project.[2321]

[2093] Selman explained that a balance sheet approach audit would not require tests like those suggested by Plaintiff's experts on the completeness of revenue or the sub-ledgers. Selman added that to detect the fee diversion, an auditor would have to design an audit with a forensic component.[2322]

[2094] Selman agreed that Castor's books traced the transfers of this fee income and stated that there was no attempt to conceal this process.[2323]

[2095] Selman acknowledged that "*if the payments had come to the auditors' attention, they needed explanations, there's absolutely no question about that.*"[2324]

[2317] Froese, December 10, 2008, pp.119-120 and pp. 126-132
[2318] Froese, December 10, 2008, p.121
[2319] Froese, December 10, 2008, pp.126-131
[2320] Froese, December 10, 2008, pp.113-114
[2321] D-1295, p. 345, paragraphs 6.13.04 & 6.13.05.
[2322] Selman, May 22, 2009, pp. 54-60
[2323] D-1295, pp. 345, 351, paragraphs. 6.13.02. and 6.13.14.
[2324] Selman, May 22, 2009, p. 55

[2096] Selman emphasized that the payments to David Smith were not concealed, which suggested to him that there was a viable explanation.

> I want to emphasize the fact that the payments were not concealed, .they're not clearly linked to the placement fees when you look at the "Various" account, that they were not concealed. I can pick up the "Various" account, go down the "Various" account and see the payments to D.T. Smith... to David Smith in the "Various" account, okay.
>
> So that suggests to me that there was a viable explanation. Otherwise, if there wasn't a viable explanation, these were not unsophisticated people; that we can see is obvious.
>
> If there wasn't a viable explanation for this, it has to evident that they would have concealed the payments to David Smith by not writing a cheque to him from CHIFNV, but by sending the money to some other shell company somewhere through Dr. Marco Gambazzi's companies somewhere or something to that order and then disbursing it back to him out of there. There was no attempt to conceal the payments to David Smith... there was no attempt to conceal the payments to Wolfgang Stolzenberg rather.
>
> So you have to ask yourself why would they... these organizations who we've seen were so clever at concealing things, have simply left those payments there opened in the books.[2325]

[2097] Selman added that if CHIO was merely a conduit and if no money was, in fact, owed to CHIO that "*an explanation would have been desirable since CHIO was being used then in an unusual and very unconventional manner and in a substantial way*".[2326]

[2098] Selman opined that he was not expecting C&L to devote a lot of time looking at the various accounts.[2327] He mentioned that "*the balances at the end of the year were not very large although, in some years, they were above the technical materiality limit.*"[2328]

Levi

[2099] Levi explained that the purpose of the test that Ford would have performed was a cut-off test of the receivables and payables.[2329]

[2100] Levi considered and opined that such transfers were concealed.[2330]

[2325] Selman, May 22, 2009, p.56
[2326] Selman, May 22, 2009, p.57
[2327] Selman, May 22, 2009, p. 58
[2328] Selman, May 22, 2009, p.60
[2329] Levi, January 12, 2010, pp. 236-237

Conclusions

[2101] A test of completeness on CHIO's placement fee income was required.

[2102] Had C&L performed this test, they would have determined that a significant portion of the fee revenue had been diverted to other parties. Such tests of completeness were performed at the Castor Montreal and CHIF level, but not for CHIO.[2331]

[2103] Selman's position is that C&L performed a "*balance sheet audit*". According to Selman, C&L was not testing the completeness of Castor's revenue. He concedes that there was no testing of CHIO's revenue, be it for "cut-off", or for any other purpose.[2332] Vance disagrees that C&L were performing a "balance sheet audit", which he states: *«...disappeared in Canada in 1951...-»*[2333] and he refers to an extract from Meigs.[2334]

[2104] For 1988, the total fees charged by CHIO on the DT Smith loans amounted to US$10.8 million, representing more than 50% of Castor's consolidated net earnings,[2335] and 70% of CHIO's net earnings.[2336]

[2105] For 1989, the fees charged to the DT Smith companies totalled US$9.8 million, representing approximately 40% of Castor's consolidated net earnings[2337] and approximately 50% of CHIO's net earnings.[2338]

[2106] For 1990, the fees charged to the DT Smith companies totalled US$7.3 million, representing approximately 25% of Castor's consolidated net earnings,[2339] and 35% of CHIO's net earnings.[2340]

[2107] For all three years, C&L had no written audit program setting out the procedures for testing CHIO's "commissions earned" account.[2341] The only reference to a test of CHIO's commission income is Ford's correspondence with C&L Cyprus.

[2330] D-1347, p. 236.
[2331] PW-2908, Vol. 1, pp. 6-50 to 6-53.
[2332] D-1295, p. 355, paragraphs. 6.13.21 and 6.13.22.
[2333] Vance, April 15, 2010, p. 100.
[2334] PW-3053-3.
[2335] PW-5, Tab 10.
[2336] PW-1053-84, seq. p. 4.
[2337] PW-5, Tab 11.
[2338] PW-1053-83, seq. p. 16.
[2339] PW-5, Tab 12.
[2340] PW-1053-81, seq. p. 5.
[2341] Martin, August 28, 1996, pp. 136-140.

[2108] For the 1989 audit, C&L Cyprus, which was responsible for the Cyprus statutory audit of Castor's Cyprus subsidiaries, wrote to her concerning the «*audit work required for year ended December 31, 1989*».[2342] Item #4 reads: «*For commissions (receivable/payable) agree details and amounts to relevant documentation.*» Ford replied to C&L Cyprus, confirming that she had performed the work requested, on a test basis, adding, at the point #6: *«The sample of loans reviewed included all new loans receivable entered into in the year».* [2343]

[2109] In fact, for year-end 1989, there is no reference to her tracing the commission earned on such new loans to loan agreements.[2344] Thus, five out of the seven loans, for which the fees were diverted, were new loans in 1989, and were part of Ford's sample for review. Froese opined that had Ford performed the required procedures, such diversion would have been discovered, and the Court agrees.[2345]

[2110] C&L Cyprus did test the "commission earned" account for 1988, and noted that there was a discrepancy between the amount of commissions earned according to the loan documents, and the commissions earned as per the financial statements. They wrote to E. Bänziger for an explanation, referencing to the following four projects: Dove Canyon I, Dove Canyon II, Tennis Court Villas and Laguna I.[2346]

- The Dove I and Dove II and Tennis Court I projects were part of the sample that Ford purportedly reviewed in 1988.[2347] If, in fact, she did review these three loans, she did not notice any discrepancy between commissions earned, as per the loan agreements, and commissions earned, as per the financial statements.

- There is absolutely no evidence, written or testimonial, and certainly nothing in C&L's audit working papers, to support Bänziger's reply to C&L Cyprus to the effect that «*from time to time, commission agreements are changed, subsequent to the first negotiation ...*».

- C&L Cyprus never advised C&L Montreal of the discrepancies that they noted.

[2342] PW-1053-83, seq. pp. 62-64.
[2343] PW-1053-83, seq. pp. 41-42
[2344] PW-1053-83, seq. pp. 103, 112, 113, 116, 119, 121, 123.
[2345] PW-2941, Vol. 5, p. 184, para. 11.3.
[2346] PW-1530B.
[2347] PW-1053-84, seq. pp. 89, 92.

[2111] Selman was specifically asked by the Court if Ford would have seen the two pages of the Konto Kurrents ("**KK**") showing the payments coming out of the various account to both Stolzenberg and DT Smith, assuming she had performed procedure #3 set out on the working paper PW-1053-87 at sequential page 107. Selman replied: «*If she checked all the KKs in CHIF NV, yes*». [2348]

[2112] The payments to Stolzenberg were related party transactions. As payments out of CHIO's assets, they should have been disclosed as RPTs: Vance and Selman agree.[2349]

[2113] The Court agrees with the following propositions:

- A proposition of Selman: the transfer of the placement fees from CHIO to CHIF's various account was clear.[2350]
- A proposition of Froese: had «*C&L appropriately audited CHIO's fee revenue, they would have had the opportunity to detect the diverted fees.*»[2351]
- A proposition of Vance: this diversion of placement fees constituted a fraud against the company, but not against C&L, as the audit trail was not concealed.[2352]

[2348] Selman, June 8, 2009, p. 156.
[2349] PW-2908, Vol. 1, p. 6-54; D-1295, p. 350, para. 6.13.13.
[2350] D-1295, p. 345, para. 6.13.02
[2351] PW-2941, Vol. 1, p. 32.
[2352] PW-2908, Vol. 1, p. 2-12.

Information conveyed by Castor's audited consolidated financial statements of 1988, 1989 and 1990

[2114] Paul Lowenstein ("**Lowenstein**"), a Plaintiff's expert witness who testified on the issue of due diligence and reliance, pointed out that audited financial statements give a reader an accurate portrait of the financial status of a company as at the date of the statements and as at the same date the previous year, when the statements are comparative (such as those of Castor)[2353].

[2115] In a private company, Lowenstein explained that independent audit verification and comparative audited financial statements enable a reader to compare the trend of the company, the company's operating results and financial position over a period of time, and to understand the accounting policies that were used in preparing those financial statements.

[2116] Through the notes attached to the financial statements, Lowenstein added that the reader gets to know whether there are any outstanding and important qualifications or items that would be of importance beyond what normally appears in financial statements[2354].

Highlights (1988)

[2117] Lowenstein described the highlights the 1988 audited consolidated financial statements of Castor as follows:

- The auditor's report is an unqualified report.
- The 1988 results are most impressive: in every important category for a company of Castor's nature there had been a significant growth, both on the revenue line, the net earnings line, growth in assets, and accompanying growth in their ability to finance those assets.
- Pre-tax net income had increased from $20,574,000 to $29,113,000, a 40% increase very impressive.
- There had been an increase of over 30% in their activity from $773,452 to $1,005,992,000 financed from a variety of sources: Castor had raised approximately $12,000,000 more of equity capital (From $48,140,000 to $58,933,000); the retained earnings of the company had increased from $28,466,000 to $39,783,000; the subordinated debentures had increased from

[2353] Lowenstein, March 21, 2005, p.59
[2354] Lowenstein, March 21, 2005, pp.59-61

$41,770,000 to $52,717,000; Loans and advances from shareholders had increased from $21,300,000 to $43,042,000, such an increase constituting a vote of confidence from the shareholders; Bank loans had increased from $289,131,000 to $376,531,000, which demonstrated that the banks were prepared to assist in the growth of the company; notes payable had increased from $327,640,000 to $441,236,000, which was a substantial increase, again indicating that the company was able to find sources to finance its growth.

- The company had liquid assets of $122,544,000, which had increased from $89,421,000.

- The category "Accrued interest and other receivables" had only increased from $17,610,000 to $18,009,000, which indicated that despite the approximate 30% increase in the investment portfolio, seemingly the company was even more promptly collecting interest on its mortgages, which attests to the credit quality of the mortgage portfolio.

- Castor was matching its liabilities against its assets.

- There was no separate line for a provision for loan losses or loan loss write-offs. In a company of Castor's nature, that is very significant: the very fact that there was no separate line for a provision for loan losses, coupled with the fact that there was no mention of any specific unusual accounting policies with respect to loan losses, led a reader to conclude that there were no material loan losses. Castor's portfolio was operating extremely well.[2355]

Highlights (1989)

[2118] Lowenstein described the highlights the 1989 audited consolidated financial statements of Castor as follows:

- Outstanding, excellent progress.

- The investment portfolio has grown by approximately 40%.

- The cash position has gone down by approximately $30,000,000, which suggests that Castor had used some of its cash to invest in its main activities, investment in a mortgage portfolio, but there still is a significant cash cushion of $92,000,000.

[2355] Lowenstein, March 21, 2005, pp.61-85

- Castor's offsetting liabilities, particularly notes payable, the way they've financed the business, has kept pace with the growth of the company.
- Gross revenue has increased by almost 50%, from $132,000,000 to $197,711,000.
- Pre-tax net income of $29,113,000 in 1998 going up to $37,843,000, a 28% increase which is good solid growth, good performance.
- There is no separate provision for loan losses in either the body of the financial statements or any reference to any change in accounting policies under the note number 1, or any other note with respect to loan losses.
- The company continues to be well matched (assets versus liabilities).
- The auditors have again issued an unqualified report[2356].

Highlights (1990)

[2119] Lowenstein described the highlights the 1990 audited consolidated financial statements of Castor as follows:

- Growth in the investment portfolio from $1,424,000 to $1,689,973,000.
- Cash is back up by approximately close to a third.
- The growth of the business continues to be financed by an increase in financing obtained from note holders and bankers.
- Castor has experienced approximately a 25% increase in its gross revenues, from $197,711,000 to $259,246,000.
- Net income before income taxes has only slightly increased, which suggests a maintenance of the company's significant profitability but not growth in the profitability, which in turn suggests that either the company's general and administrative expenses have grown faster than the revenue line has, or there has been compression of the interest rate spread.
- The company's matching continues to be in line, satisfactory. The company continues to be well matched.

[2356] Lowenstein, March 21, 2005, pp.167-171

- There is no separate disclosure of a provision for loan losses and no change in -- no highlighting of any change in the accounting policy approach used for loan losses.

- The auditors have issued an unqualified report[2357].

Results over a five year period

[2120] Commenting Castor's statements and comparative results over a five year period, all from the consolidated audited financial statements and reproduced on C&L's letterhead with C&L's Legal for Life Certificate[2358], Lowenstein concluded:

- Solid growth, most impressive growth over a five-year period.

- Impressive growth in the financial service sector: the asset growth, the ability for the company to finance that growth, the increase in revenue and the increase in net earnings.

[2357] Lowenstein, March 21, 2005, pp. 171-175
[2358] Lowenstein, March 21, 2005, p.85

The 1988, 1989 and 1990 audited financial statements of Castor were materially misstated and misleading

Professional standards

[2121] The objective of an audit of financial statements of a company is to express an opinion whether the financial statements present fairly, in all material respects, the financial position, results of operations and changes in the financial position in accordance with GAAP[2359].

[2122] An assumption underlying the preparation of financial statements in accordance with GAAP, commonly referred to as the "going concern" assumption, is that the enterprise will be able to realize assets and discharge liabilities in the normal course of business for the foreseeable future[2360].

[2123] In performing his or her examination, the auditor seeks reasonable assurance that the financial statements taken as a whole are free of material misstatement[2361].

[2124] The concept of materiality recognizes that some matters, either individual or in the aggregate, are important if financial statements are to be presented fairly in accordance with GAAP[2362].

[2125] A misstatement or the aggregate of all misstatements in financial statements is considered to be material if, in the light of surrounding circumstances, it is probable that the decision of a person who is relying on the financial statements, and who has a reasonable knowledge of business and economic activities would be changed or influenced by such a misstatement or the aggregate of all misstatements[2363].

[2126] Misstatements in financial statements arise from departures from GAAP and include departures from fact, inappropriate determination of accounting estimates, and omissions of necessary information[2364].

[2127] Absolute assurance in auditing is not attainable due to such factors as the need for judgment, the use of testing, the inherent limitations of internal control, and the fact that much of the evidence available to the auditor is persuasive rather than conclusive in nature[2365]. In other words, every audit presents the risk that the auditor will fail to

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[2359] PW-1419-1A, PW-1419-2A and PW-1419-3A, section 5000.01
[2360] PW-1419-1A, PW-1419-2A and PW-1419-3A, section 5510.51
[2361] PW-1419-1A, PW-1419-2A and PW-1419-3A, section 5000.04
[2362] PW-1419-1A, PW-1419-2A and PW-1419-3A, section 5130.04
[2363] PW-1419-1A, PW-1419-2A and PW-1419-3A, section 5130.05
[2364] PW-1419-1A, PW-1419-2A and PW-1419-3A, section 5130.05
[2365] PW-1419-1A, PW-1419-2A and PW-1419-3A, section 5000.04

express a reservation in his or her opinion on financial statements that are materially misstated.

[2128] In all cases, as mentioned in the italicized recommendation 5130.24 "*The nature, extent and timing of the auditor's procedures should be designed so that, in the auditor's professional judgment, the risk of not detecting a material misstatement in the financial statements is reduced to an appropriately low level*"[2366].

[2129] To establish "*the nature, the extent and the timing of his or her procedures*", the auditor needs first to plan the audit and to establish levels of risk.

[2130] To plan properly, a prerequisite to any serious audit, the auditor needs to know his client's business.[2367] He can gain or update such knowledge through various methods and sources:

- Reviewing working papers of previous years' engagements.
- Reading financial information such as interim financial reports, budgets and forecasts.
- Consulting sources of information such as accounting and auditing pronouncements, industry publications, research studies, textbooks, periodicals, financial newspapers, and financial statements of other enterprises in the industry.
- Considering applicable statutory and contractual requirements.
- Visiting the client's business place(s).
- Consulting knowledgeable individuals (authors) within or outside the enterprise.

[2131] Since the auditor has to understand the events, transactions and practices that may have a significant effect on his or her examination (and on the nature, extent and timing of his audit procedures) or on the financial statements, he or she has to gain sufficient knowledge of the client's business to discharge adequately this professional duty.

[2132] There are 3 components to audit risk:

> Inherent risk – the risk of a material misstatement occurring in the first place;
>
> Control risk – the risk that the client's internal controls will not prevent or detect a material misstatement;

[2366] PW-1419-1A, PW-1419-2A and PW-1419-3A

[2367] PW-1419-1A, section 5140 (1988); PW-1419-2A, section 5140 (1989); PW-1419-3A, section 5140 (1990)

> Detection risk – the risk that any material misstatement that has not been corrected by the client's internal control will not be detected by the auditor[2368].

[2133] Before they started their audits of the 1988, 1989 and 1990 financial statements of Castor, C&L had to assess the inherent risk. As section 5130.16 of the Handbook stipulates, "*The purpose of assessing inherent risk is to assist the auditor in determining the nature, extent and timing of his or her auditing procedures by identifying balances or transactions that are susceptible to misstatement.*[2369]"

[2134] As per section 5130.22 of the Handbook, C&L's objective had to be the reduction of the risk of not detecting a material misstatement to an appropriately low level, the determination of that level calling for the exercise of professional judgment on their part[2370].

[2135] A direct relationship exists between materiality and audit risk.[2371]

[2136] Throughout an audit, decisions concerning materiality and audit risk are among the most significant because they form the basis for determining the extent of the auditing procedures to be undertaken. Therefore, these decisions should be addressed and documented at the planning stage of the engagement and revised, if need be, during the engagement[2372].

[2137] Finally, and in all cases, as the italicized recommendation 5130.40 stipulates "*If, based on the audit evidence obtained, the auditor concludes that the financial statements are materially misstated, he or she should request that management address the material misstatement. If management does not appropriately address the misstatement, the auditor should express a reservation in his or her report.*"[2373]

Evidence

[2138] The CHL Audit Planning Memorandum for 1988 included an "*Assessment of Risk and Materiality*".[2374] On a consolidated basis, the materiality levels were set at $400 000 for income items, and at $900 000 for net assets or other items affecting the balance sheet:

> the calculation is done showing both for the unconsolidated financial statements of Castor Holdings Ltd. and the consolidated financial statements, the

[2368] PW-1419-1A, PW-1419-2A and PW-1419-3A, section 5130.10
[2369] PW-1419-1A, PW-1419-2A and PW-1419-3A
[2370] PW-1419-1A, PW-1419-2A and PW-1419-3A
[2371] PW-1419-1A, PW-1419-2A and PW-1419-3A, section 5130.23
[2372] PW-1419-1A, PW-1419-2A and PW-1419-3A, sections 5130.25, 5130.29 and 5130.30
[2373] PW-1419-1A, PW-1419-2A and PW-1419-3A
[2374] PW-1053-24, seq. pp. 347-358.

> considerations for materiality and it's broken down between items that would affect the income statement and items that would affect net assets or the balance sheet, and the materiality level for income items on a consolidated basis, which are the financial statements at PW-5, is four hundred thousand dollars ($400,000), and for the net assets or affecting the balance sheet, is nine hundred thousand dollars ($900,000)..[2375]

[2139] The CHL Audit Planning Memorandum for 1989 included an "*Assessment of Risk and Materiality*".[2376] On a consolidated basis, the materiality levels were set at $556,000 for income items, and at $1,100 000 for net assets or other items affecting the balance sheet:

> And for nineteen eighty-nine (1989), the planning memorandum is PW-1053-20-1. Sequential page 257, at the foot of the page again is the materiality calculation, and again it's done on a consolidated basis and unconsolidated, and of interest in this case is the consolidated financial statements where the calculations for consolidation and net income items, and the amount is five hundred and fifty-six thousand dollars ($556,000), and for net assets, it's one million one hundred thousand dollars ($1,100,000).[2377]

[2140] The CHL Audit Planning Memorandum for 1990 included an "*Assessment of Risk and Materiality*".[2378] In 1990, C&L used a different method and came up with only one materiality level of $2,135,000, on a consolidated basis.[2379]

> And for nineteen ninety (1990), the planning memorandum is PW-1053-16-1. And this, in this year, the approach is slightly different, it's now using three (3) components and taking an average, and that is set out on page, sequential page 264, and this calculation, insofar as the consolidated financial statements are concerned, is at the foot of the schedule or last tabulation, where one percent (1%) of revenue is used, five percent (5%) of profit before taxes and one percent (1%) of net assets. Their total is then divided by three (3) to get a one materiality number that is used, rather than two (2) in the past two (2) years, but the materiality level for the nineteen ninety (1990) consolidated financial statements is two million one hundred thirty-five thousand dollars ($2,135,000).[2380]

[2141] Asked in his cross-examination what level of materiality he would suggest the Court use to assess the evidence, Selman answered "*The audit working papers contain a materiality level and since that was the judgment of the auditors to use that materiality level, initially that would be the level that I would apply*"[2381].

[2375] PW-1053-24, sequential page 349; Vance, March 6, 2008, p. 23
[2376] PW-1053-20, sequential page 257
[2377] Vance, March 6, 2008, pp.23-24
[2378] PW-1053-16
[2379] PW-1053-16, sequential page 264
[2380] Vance, March 6, 2008, p.24
[2381] Selman, June 4, 2009, p.123

[2142] Disclosure issues have to be looked at differently, acknowledged Selman: they shall be looked at on a qualitative basis rather than on a quantitative basis.[2382] For example, a related party transaction will generally be disclosed even though it is well under the materiality level otherwise calculated because the relationship is important to the reader.

[2143] Selman was asked specifically if the Court should apply the materiality level chosen by C&L in the CHL's Audit Planning Memorandums, i.e. $400,000 for income and $900,000 for assets[2383] in 1988. Selman answered:

> It's a difficult question. Let me address it this way. We're dealing firstly with the financial statements and not disclosure, just to make that clear. The materiality levels that you have reflected there (...) to my mind, are on the low side. I would personally not go as low as that in terms of the materiality in an audit of the size of Castor with the figures that we had in the financial statements.
>
> However, those are the materiality levels that the auditors chose and in making a judgment that those were the appropriate materiality levels to use, it seems to me that that judgment has to have some bearing on the assessment of the audits. If they consciously chose those materiality levels, I'm not sure whether the fact that I think they're a little low really should carry a great deal of weight or not. I just don't know.
>
> So, all I'm saying here is I would make a professional judgment more in the line of the two and a half (2½) million in nineteen ninety (1990) against income, and relate that to the level of income in eighty-nine ('89) and eighty-eight ('88), sort of that percentage, in general, you can go... I've seen as high as ten percent (10%) on income levels, but most people seem to come down and around the five percent (5%) range.
>
> On assets of something like a billion dollars, almost two (2) billion dollars in nineteen ninety (1990), a bit, a million nine hundred thousand (1,900,000), on assets, against a balance sheet which is getting very close to two (2) billion dollars, it seems like a fairly low number and if they had chosen three (3) million or four (4) million as the materiality level, I wouldn't have raised my eyebrows about that at all. So, it's a choice, they were very conservative in their choice of materiality levels, in my opinion.[2384]

[2144] After lunch, the same day, before his cross-examination resumed, Selman clarified his position as follows:

> I wanted to go back to the last question and just to clarify, when we were talking about materiality, there is not a direct relationship between the materiality level that the auditor chooses in order to make an assessment of individual items that

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[2382] Selman, June 9, 2009, pp.246-257
[2383] PW-1053-24, 10 sequential page 349
[2384] Selman, June 4, 2009, pp.124-126

> may be in his view errors or misstatements from what he thinks they should be, or the aggregation of them, there's not a direct relationship between that and between the concept of material misstatement of the financial statements as a whole. The test remains a subjective test and it is found in section 5130.05, .06, .07 and .08 of the handbook, and so it would be obvious, I think, that an auditor chose a materiality level of five hundred thousand dollars ($500,000) or something in that order for the assets on a financial statement that held something in the order of a billion dollars in assets, a misstatement of five hundred thousand dollars ($500,000) would not affect the decisions of a reasonable reader a s user of the financial statements as set out in the handbook.
>
> Five hundred thousand dollars ($500,000), a billion dollars, is nothing. On the other hand, if it was fifty (50) million dollars or... Fifty (50) million dollars or five percent (5%) of the billion dollars, it would have potentially a different assessment. So, the subjectivity of what is a material misstatement of the financial statements as a whole is not directly related to the decision that the auditor makes as to what he will bring forward or where he will cease to continue his testing in terms of the materiality level. He may decide that if he finds something under five hundred thousand dollars ($500,000), he won't look at it, it won't be of concern to it.[2385]

[2145] The term "materiality" is defined in the Handbook from the perspective of the user of the financial statements.

[2146] Meigs writes: «*In the opinion of the authors, the essence of the CICA position is to equate the quality of presenting fairly with that of not being misleading or not being materially misstated. Financial statements must not be so presented as to lead users to forecasts or conclusions that a company and its independent auditors know are unsound or unlikely*».[2386] The same idea is also found in Anderson's text book[2387], in the MacDonald Commission report[2388], and in Gibbins & Mason's text book.[2389]

[2147] Vance, Froese and Rosen have opined that the 1988, 1989 and 1990 consolidated audited financial statements of Castor were materially misstated and misleading. In their testimonies and in their written reports they have given numerous examples illustrating such conclusions.

[2148] Defendants' expert Selman agreed that Castor 1988, 1989 and 1990 audited consolidated financial statements would be materially misstated and misleading if the Court was to conclude that LLPs, as suggested by Plaintiff's experts, were required.

[2385] Selman, June 4, 2009, pp.129-130
[2386] PW-3053-1, p. 29
[2387] PW-1421-22, pp. 552-554
[2388] PW-1432A, p. 50, paragraph 3.45
[2389] PW-2917, pp. 126-127

Conclusions

[2149] The *objectives* of financial statements, the *materiality* and *relevance* of information communicated in financial statements are all assessed from the perspective of the utility of the information for readers.[2390]

[2150] Readers want to have information communicated to them to evaluate the liquidity and solvency of an enterprise and to assess the ability to generate cash from internal sources, to repay debt obligations, to reinvest and to make distributions to owners[2391].

[2151] By definition, materiality is information that, if omitted or misstated, would influence or change a decision.[2392]

[2152] The omitted information and the misstated information described in the previous sections of this judgment are clearly material.

[2153] The audited consolidated financial statements of 1988, 1989 and 1990 are materially misstated and misleading.

[2154] The failure to disclose the practice and quantum of capitalized interest materially misled the readers of Castor's audited financial statements.

[2155] Appropriate disclosure of the capitalized interest would have alerted the reader, namely Widdrington and his advisors, to the fact that the majority of Castor's loans were non-performing in that the borrowers were unable to pay interest on their loans. This would have raised concerns about the collectability of the loans, and questions as to whether the loans were on normal commercial terms (i.e., at arm's length).

[2156] Appropriate disclosure would have had a significant negative impact on the income, revenue and profit recorded by Castor. Capitalized interest increased profitability but did not improve cash liquidity. «*In effect, the earnings statement of Castor was showing success when the opposite was the case.*»[2393]

[2157] Appropriate disclosure would have alerted the reader, namely Widdrington and his advisors, to the fact that Castor was not generating cash from operations, which would have been surprising since Castor was presenting itself as a spread lender and not as a real estate developer, and would have raised concerns about Castor's liquidity and solvency.

[2158] Widdrington and his advisers, readers of the financial statements, were entitled to assume that most of the loans were producing cash income. They were also entitled

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[2390] PW-1419-1, sections 1000.12, 1000.14 and 1000.17
[2391] PW-1419-1, section 1540.01
[2392] PW-1419-2, section 1000.14
[2393] Rosen, PW-3033, vol.1, p. 64

to assume that the loans were collectable.[2394] As readers of the audited financial statements of Castor, they could not have known that Castor was tolerating the systematic failure of its borrowers to pay interest and fees in cash or about the degree to which capitalized interest and fees contributed to the falsely impressive growth in the loan portfolio, as represented in the audited financial statements. This information was not disclosed.

[2159] There were two Castors, Castor as depicted in its audited consolidated financial statements and the real Castor, as Rosen summed it up:

> (...) when someone looks at the financial statements of Castor, they will see an organization that has all of the markings of a short-term lender, combined with the information circular, combined with note 2 that talks about maturities, and note 3 showing when coming due, it all adds up to short-term investing and as Castor moved through the eighties, into eighty-eight ('88), eighty-nine ('89) and ninety ('90), it was anything of the sort. It was a long-term locked in situation desperately in need of cash[2395].

[2160] From the face of the 1988, 1989 and 1990 consolidated audited financial statements, it was evident that there was no Statement of Change in Financial Position ("**SCFP**"). In the scope paragraph of the audit opinion, there is no reference whatsoever to a presentation of changes in the financial position, whereas there are clear references to changes in net invested assets.

[2161] The audit opinion explicitly stated: "*We have examined the consolidated balance sheet of Castor Holdings Ltd. as at December 31, 1988 and the consolidated statements of earnings, retained earnings and changes in net invested assets for the year then ended.(...)...In our opinion, these consolidated financial statements present fairly the financial position of the company as at December 31, 1988 and the results of its operations and the changes in its net invested assets for the year then ended in accordance with GAAP (...)*" (our emphasis)

[2162] Even if the user had read only the audit opinion, he would not have been misled as to the content of the financial statements on which C&L gave an opinion: there was no SCFP and C&L was not opining on such a statement.

[2163] However, there should have been a SCFP. In the absence of such a statement, and given the fact that information about activities and their effects on cash resources was neither readily apparent from other financial statements, nor adequately disclosed in the notes, the financial statements were not in accordance with GAAP. C&L should have qualified their audit opinion, which they did not.

[2394] Morrison, October 10, 2006, pp. 131-132, pp. 140-143; Morrison, October 12, 2006, pp. 70-71.
[2395] Rosen, February 3, 2009, pp.47-48

[2164] The above mentioned information, which was withheld, was certainly material information from the point of view of an investor or a lender.

[2165] Rather than being an appropriate alternative, the presence of the Statement of Changes in Net Investment Assets ("**SCNIA**"), and its format in the 1988, 1989 and 1990 consolidated audited financial statements, participated in the misleading effect.

[2166] The most compelling proof that the SCNIA was materially misleading to a reader is the testimony of Cunningham and Hayes[2396], the second partners in charge of the Castor audit, as well as that of Higgins[2397], the peer review partner.

[2167] Cunningham and Hayes, the second partners in charge of the Castor audit, both testified as to their understanding of the SCNIA: this statement disclosed cash generated from Castor's operations[2398]. In fact, the SCNIA disclosed no such information.

[2168] Higgins, the peer review partner, acknowledged that the SCNIA did not disclose cash generated from operations and that the Handbook recommended that this be done[2399].

[2169] The failure to use a properly prepared SCFP had an effect which was to misrepresent to a user of Castor's financial statements the carrying value of its assets, its profitability, its liquidity and the maturities of its assets. Each of these items was very material to a user. In acceding to the request of its client, C&L permitted Castor to avoid the disclosure of information that was material to a user of the financial statements.

[2170] A reader of the 1988, 1989 or 1990 consolidated audited financial statements would not conclude that Castor needed necessarily the money of others to go on, while in fact, it did. The reader was provided with the illusion that all was well: the loan portfolio was growing with good assets, most of which were maturing within the following year, with no or very little loan loss provision. Had a proper SCFP been provided, things would have looked otherwise[2400].

[2171] In 1989, the net earnings of Castor were $28.4 million according to the consolidated statement of retained earnings.[2401] The same figure appeared in the SCNIA as "*net assets available for investments provided from operations*". None of these figures represented cash or cash equivalents. However, and as previously mentioned, Hayes and Cunningham, both partners of C&L, were misled and believed otherwise.

[2396] Hayes, October 31, 1995, pp. 85-87; Cunningham, December 13, 1996, p. 85-88.
[2397] Higgins, December 18, 1996, pp. 110-114.
[2398] Hayes, October 31, 1995, pp. 85-87; Cunningham, December 13, 1996, p. 85-88.
[2399] Higgins, December 18, 1996, pp. 110-114.
[2400] Vance, March 4, 2008, PM transcription, pp.60-61; Vance March 10, 2008, pp.44 and following
[2401] PW-5, tab 11

[2172] Had a proper SCFP been provided in 1989, it would have shown a negative figure of "cash from operations" given that there was capitalized interest for at least $53 million as identified by Belliveau during the audit.[2402]

[2173] A negative figure of "cash from operations" would have told any reader of the financial statements, namely Widdrington and his advisors, that Castor, in trying to generate cash from its operations, was doing very poorly, and that it would have had either to sell investments or to entice new investments through debt or equity in order to do better.

[2174] Castor intended Notes 2, 3 and 4 of the audited consolidated financial statements to provide information concerning the matching of current assets and current liabilities, which is critical to an understanding of the company's liquidity and solvency. The assessment of liquidity focuses on the short-term, i.e., the year following the financial statements, and evaluates the ability of the company to meet its obligations as they become due and in the normal course of business. Since Castor prepared a non-classified balance sheet, a reader had to refer to those notes in order to evaluate the company's short-term obligations as well as the company's ability to meet these obligations.[2403]

[2175] The contradiction between what notes 2, 3 and 4 conveyed to readers, such as Widdrington and his advisers, and the reality of the situation was described by Defendants' expert Morrison, in the following words: «*There was a strong indication that the mortgages were being renewed, rolled over, and if you had the details of the mortgage portfolio over time, I think that would have,* ***with hindsight****, been very evident.... it was indicated that there was a screaming contradiction here about the fundamental nature of Castor's business. It was effectively making much longer-term loans, whatever the contract period.* » (our emphasis)[2404]

[2176] During their audit work, having access to accounting books and records and to loan files, the auditors should have seen such "screaming contradiction". They should have foreseen the misleading nature of the information conveyed by notes 2, 3 and 4.[2405] Defendants' expert Morrison acknowledged that there was no way for a reader of the financial statements to infer from the notes 2, 3 and 4 that the loans were not collectible as at their maturity dates.[2406]

[2177] Notes 2, 3 and 4 disclosed a false picture of liquidity matching and solvency: they were misleading.

[2402] PW-1053
[2403] PW-2908, Vol. 1, p. 4-F-1.
[2404] Morrison, October 4, 2006, p. 129.
[2405] Rosen, February 5, 2009, pp. 83-85.
[2406] Morrison, October 12, 2006, pp. 70-71.

[2178] Castor's 1988, 1989 and 1990 audited consolidated financial statements were misleading as a result of the $100 million debenture transaction entered into by Castor in 1987 and noted to the financial statements.

[2179] The $100 million transaction was a cash circle, and Selman admitted that the 1988, 1989 and 1990 consolidated audited financial statements were materially misstated and misleading, if it was such[2407].

[2180] The 1988, 1989 and 1990 consolidated audited financial statements were misleading because of the non-disclosure of numerous related party transactions.

[2181] The 1988, 1989 and 1990 consolidated audited financial statements were also misleading because of the non-disclosure of restricted cash.[2408]

[2182] Moreover, and as pointed out by Selman, a significant increase in accrued interest and other receivables would have indicated the deterioration in Castor's position.[2409]

[2183] The misleading nature of the reallocation of accrued interests was compounded by the fact that the investments were described as being carried at cost and there was no disclosure to a reader that the investments in mortgages, secured debentures and advances were being carried at cost plus accrued interest, as shown in the financial statements of trust companies. As a consequence, this vital information was concealed from a user of Castor's financial statements.

[2184] Huge loan loss provisions should have been taken. As Selman pointed out, if the Court was to conclude that such loan loss provisions were required, nothing else in the case was really relevant anymore since a clean audit opinion, based on Castor being a going concern, could not have been possible.[2410]

[2185] The Court shares Vance's conclusion that: «*considering the extent of the misstatements in the consolidated financial statements of Castor for the year ended December 1988* (also applicable to 1989 and 1990), *C&L should not have issued unqualified opinions on these financial statements, but should have either denied an opinion or issued an adverse opinion indicating the extent to which the financial statements were materially misleading and stating that these financial statements did not present fairly the financial position, results of operations and changes in financial position of Castor.*»[2411]

[2407] Selman, May 25, 2009, pp. 28-29
[2408] Vance, March 13, 2008, pp.28-29; PW-2908A.
[2409] D-1295, pp. 171-173, paras. 5.03, 5.05, 5.06.
[2410] Selman, May 8, 2009, pages 182-183
[2411] PW-2908, Vol. 1, S-25; See also PW-3033, pp. 1-3; PW-3034, pp. 9-11, at p. 11.

Did C&L commit a fault in the professional work that they performed in connection with the audits of Castor for 1988, 1989 and 1990?

Conclusion

[2186] Because C&L did not conduct their audits in accordance with GAAS and because C&L cannot successfully plead fraud to excuse themselves, the Court concludes that C&L committed a fault in their professional work in connection with the audits of Castor for 1988, 1989 and 1990.

C&L did not conduct their audit of 1988, 1989 and 1990 in accordance with generally accepted auditing standards ("GAAS")

[2187] As Levi said "*An audit is not a science, it's an art. There aren't specific compartments that you can put it into and make it black or white, and this is why you have the issue of professional judgment in there, there is no strict standard procedures that will apply to every situation* "[2412].

[2188] The objective of an audit of financial statements, as set out in section 5000.01 of the CICA handbook, is "to express an opinion on the fairness with which they (the financial statements that are audited) present the financial position, results of operations and changes in financial position in accordance with generally accepted accounting principles"[2413].

[2189] In addressing the financial statements and assertions embodied therein, the auditor is required to perform the audit in accordance with GAAS. These standards are set out in Section 5100.02 of the CICA Handbook[2414] and read as follows:

> **General Standard**
>
> The examination should be performed and the report prepared by a person or persons having adequate technical training and proficiency in auditing, with due care and with an objective state of mind.
>
> **Examination Standards**

[2412] Levi, January 11, 2010, p.164
[2413] PW-1419-1A (1988), PW-1419-2A (1989) et PW-1419-3A (1990)
[2414] PW-1419-1A (1988), PW-1419-2A (1989) et PW-1419-3A (1990)

(i) The work should be adequately planned and properly executed. If assistants are employed, they should be properly supervised.

(ii) There should be an appropriately organized study and evaluation of those internal controls on which the auditor subsequently relies in determining the nature, extent and timing of auditing procedures.

(iii) Sufficient appropriate audit evidence should be obtained, by such means as inspection, observation, enquiry, confirmation, computation and analysis, to afford a reasonable basis to support the content of the report.

Reporting Standards

(i) The scope of the auditor's examination should be referred to in the report.

(ii) The report should contain either an expression of opinion on the financial statements or an assertion that an opinion cannot be expressed. In the latter case, the reasons therefore should be stated.

(iii) Where an opinion is expressed, it should indicate whether the financial statements present fairly the financial position, results of operations and changes in financial position in accordance with an appropriate disclosed basis of accounting, which except in special circumstances should be generally accepted accounting principles. The report should provide adequate explanation with respect to any reservation contained in such opinion.

(iv) Where an opinion is expressed, the report should also indicate whether the application of the disclosed basis of accounting is consistent with that of the preceding period. Where the basis or its application is not consistent, the report should provide adequate explanation of the nature and effect of the inconsistency.

[2190] GAAS deal with the planning of the audit, the execution of the audit, and the reporting of the results of the audit.

[2191] C&L provided their own guidance to staff regarding their approach to audits and policies. For the relevant years, C&L issued three types of such material:

- Technical Policy Statements ("TPS");
- Memoranda by the C&L's National Office referred to as "AM"
- "Tips and Tidbits", a newsletter issued by the National Research Department.

[2192] For their audits of 1988, 1989 and 1990, C&L did not comply with GAAS, namely in that:

- The engagement partner of these audits, Wightman, lacked independence and did not have an objective state of mind.
- The planning of the audits was inappropriate.
- The audit examination was performed without due care and by persons that did not have adequate technical training or proficiency in auditing.
- The assistants were not properly supervised.
- The auditors failed to gather sufficient appropriate audit evidence: the auditor failed to use adequate and sufficient means to afford a reasonable basis to support the content of their report.
- The auditors rendered an unqualified opinion without obtaining sufficient appropriate audit evidence to provide a basis to support the content of their report.

Lack of independence and of an objective state of mind

Positions

Plaintiff's position

[2193] Plaintiff argues that:

- It is a fundamental tenet of GAAS that an auditor must approach an audit with an objective state of mind. Because an auditor's unqualified audit opinion gives credibility to management's presentation of the company's financial position in its financial statements, the auditor has to speak freely and without influence. When the auditor is not independent of his audit client, every exercise of his professional judgment is called into question.
- Wightman was not independent of Castor, or its principal, Stolzenberg, and this detrimentally affected the conduct of the audits of Castor, including those conducted for the years ending 1988, 1989 and 1990.
- Wightman's objectivity was compromised by his intimate involvement as an advisor, a friend, a supporter and promoter of Castor, and by the numerous business relationships that he had with both Castor and Stolzenberg, outside of Castor, which he did not disclose to his partners in his annual declarations.

Defendants' position

[2194] Defendants argue that:

- Plaintiff has alleged that Wightman lacked independence and objectivity during 1988-1990 arising from certain investments made with Stolzenberg, and from the fact that he introduced Stolzenberg and Castor to several business opportunities, but no other C&L auditor is accused of a lack of objectivity, and Plaintiff does not link the perceived lack of objectivity to any GAAS or GAAP failure.

- The allegations relating to Wightman's independence are made to colour the file and to influence the Court's appreciation of Wightman's personal character.

- Since the Court is not seized with a complaint about a breach of the Quebec Code of Ethics, or with the removal of C&L under the NBBCA, she should reject the allegations as being irrelevant to a professional liability case.

- The only matter relevant is whether Wightman had an "objective state of mind", as required by the Handbook, and there is no evidence that he did not.

Court's conclusion on relevance of allegations relating to independence

[2195] Independence, and evidence in relation to independence, is relevant.

[2196] No auditor can comply with GAAS if he does not perform an audit with an objective state of mind.

[2197] Whether or not C&L's audits of 1988, 1989 and 1990 were performed in compliance with GAAS is at the heart of the debate.

[2198] Wightman was the engagement partner on the 1988, 1989 and 1990 audits and the only person at C&L who had complete knowledge of the client's business. Wightman was the person handling the wrap-up meetings with Stolzenberg and the person who had the final say as to the issuance and content of the audit reports.

[2199] Evidence purporting to shed light on Wightman's various business interactions with Castor and Stolzenberg is relevant to what his state of mind was or might have been at any given time.

[2200] Moreover, credibility and reliability of witnesses' sayings are crucial.

[2201] Wightman's actions or omissions, namely in the context of his obligations towards his partners, and Wightman's views on such constitute tools to assess credibility and reliability. They are therefore also relevant to said purpose.

Professional standards and other tools

[2202] The following sources of professional standards governing auditors' conduct and independence are relevant.

[2203] The Handbook[2415] provides that the audit shall be performed "*with due care and with an objective state of mind*".

[2204] The Code of Ethics of Chartered Accountants Regulation[2416] provides that accountants who are called upon to express opinions on financial statements must be free of influence that may impair, or be perceived as impairing, their professional judgment or objectivity and that an accountant cannot represent more than one party in the same transaction[2417].

[2205] The New Brunswick Corporations Act[2418] stipulates that a person is disqualified from acting as an auditor of a corporation if he or she is not independent of the corporation being audited, its affiliates or the directors or officers of such corporation or any of its affiliates.

[2206] Although it is not a professional standard but primarily a matter of partnership governance (it regulates conduct and disclosure as between partners), the C&L Policy of Professional Independence (TPS-A-104)[2419] is also relevant. Besides, such policy is very specific in stating its intent:

> "This policy statement sets forth the Firm's policy of professional independence. It neither describes nor supersedes standards of independence required by various statutes or the rules of conduct of the provincial institutes or Ordre. Partners and professional employees should be familiar with and adhere to such standards."

[2207] C&L Policy of Professional Independence defines C&L's expectations, on which C&L partners and employees interact with each other, namely as members of an audit team.

Evidence

[2208] Wightman was implicated in Castor's affairs, far beyond his role as Castor's auditor.

[2415] PW-1419-1A, Section 5100.02 and 5100.04 (1988); PW-1419-2A, Section 5100.02 and 5100.04 (1989); PW-1419-3A, Section 5100.02 and 5100.04 (1990)
[2416] PW-2311 Para 3.02. 3.02.05 and 3.02.06
[2417] PW-2311, Para. 3.02.05.
[2418] PW-2312-1. Sections 104(1) and 104(2)
[2419] PW-1420-1A.

[2209] Wightman was the architect of Castor's corporate structure since its inception in 1978 until its demise in 1992.

[2210] Wightman played an important role as a promoter of Castor.

[2211] Wightman introduced Castor to various investment and business opportunities: Cafa Financial Corporation, Ouimet Hubbs, Orion Maritime Inc., Brandywine & Iotech Corporation and potential Coat-Hangers (Laurentian Group, JT/Guardian and Sensormatic)

[2212] Wightman introduced Stolzenberg and Castor to many opportunities in which he was involved, including Chur, Petra and Sloppin, Baxter Street, CMF and Expo Overseas[2420].

[2213] Wightman invested Sloppin's money in various companies, some of which he was the auditor of, which he introduced to Stolzenberg who, himself, acquired a financial interest in the company's affairs: Pigments & Chemical, Compagnie de Recyclage de Montréal, Perkins Paper and Ideal Metals.

Implication in Castor's affairs

[2214] Wightman was involved in the development of Castor's corporate structure prior to its inception. He was part of the decision to liquidate Castor Holdings Inc., and to incorporate CHL in New Brunswick.[2421]

[2215] When Castor was incorporated at the end of 1977, C&L became its auditors, and remained so until its eventual demise in 1992.

[2216] Much like he had done with its predecessor, Castor Holdings Inc., Wightman was deeply implicated in Castor's affairs, and his implication went far beyond his role as an auditor[2422].

[2217] During the relevant years, Castor accounted for 7 to 10% of Wightman's personal billings in Montreal, and this, exclusive of work which was done for other clients or himself, in which he involved Castor or Stolzenberg, and for which Castor was not charged[2423].

[2218] The revenue for the provision of special services by C&L to Castor accounted for almost three times the auditing revenue[2424].

[2420] PW-3095
[2421] Wightman, September 5, 1995, p. 156.
[2422] PW-3101: Review of services.
[2423] Wightman, September 7, 1995, pp. 98-101.
[2424] PW-1053-2A-4, PW-1053-2A, seq. pp. 29, 103, 110

[2219] As it appears from C&L's invoices for professional services rendered, Wightman and C&L were involved in all facets of Castor's business[2425], including:

- Consideration of various business ventures, such as the acquisition of oil and gas drilling projects, the purchase of scientific research credits, consideration of the acquisition of a hotel, consideration of various loans, advice with respect to investment in other financial services companies, including Pollux Capital and Cafa Financial Corporation, and advice regarding the acquisition of an aircraft, to name a few.

- Preparation of Legal for Life Certificates which enabled Castor to attract investments from institutional investors, such as pension funds, and to which Wightman referred to present Castor[2426].

- Establishment of the fair market value of Castor shares, which were being used to set the price for the purchase of shares by new and existing shareholders, and the sale of shares by existing shareholders.

- Advice and consultation regarding changes to Castor's share capital and the issuance of subordinated debentures.

- Various tax advice, with respect to matters such as the tax treatment of the subsidiaries, tax advice with respect to various transactions, the calculation of dividends and withholding taxes and, most notably, continuous correspondence with income tax authorities in Quebec and Canada in the context of audits to, among other things, justify the allocation of revenue and expenses between Castor and its subsidiaries.

[2220] Wightman frequently attended the Castor directors' meetings in Montreal and in Toronto, as well as in Europe. He made presentations to the Board and he sometimes stayed for the whole meeting[2427].

[2221] Wightman was responsible for the development of Castor's corporate structure internationally - he was the architect of Castor's expansion to international jurisdictions, such as Switzerland, the Netherlands, the Netherlands Antilles, the United States, Cyprus and Ireland[2428]. In addition to conceiving and structuring these subsidiaries, Wightman was also involved in implementing his recommendations. He helped Castor

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[2425] PW-3104, PW-3105, PW-3106, PW-3107, PW-2372-25

[2426] PW-1053-6, seq. p. 103.

[2427] PW-3104, PW-3105, PW-3106; PW-2400-23, PW-2400-29; PW-2400-34, PW-2400-38, PW-2400-61, PW-2400-70; PW-2400-75, PW-2400-98, PW-2400-101.

[2428] PW-2400-20. PW-2400-34, PW-2400-75, PW-2400-83, PW-2400-87, PW-2400-98, PW-2400-101, PW-2400-102

to find office space, to hire personnel and to assign people to act as directors, often employing local C&L employees in the process[2429].

[2222] The role played by Wightman with respect to CH (Ireland) is a prime example of his integral role in setting up Castor's subsidiaries.

[2223] Wightman began proposing Ireland as a potential low-tax jurisdiction in which to establish a subsidiary as early as 1984[2430].

[2224] Wightman conceived the concept for this entity and spearheaded the process to obtain the required approvals to bring the project to fruition[2431].

[2225] Throughout the process, Wightman:

- negotiated with Irish authorities to obtain the required operating license[2432], and
- was involved in :
  - incorporating the entity[2433],
  - hiring personnel[2434],
  - introducing Castor to prospective financers[2435],
  - reviewing proposed transactions for the company[2436], and
  - finding clients to make use of the operations that he designed[2437].

Role as Castor's promoter

[2226] Wightman was considered by his client to be an important promoter of Castor among the lending community, and "*having him as a friend was very key to the promotion and goodwill of Castor*"[2438].

[2227] C&L assisted Castor in developing and maintaining financing from lenders[2439] and depositors.

[2429] PW-2711, Wightman, August 15, 1996, pp. 104-108.
[2430] PW-2400-75
[2431] Simon, May 1, 2009, pp. 126-127
[2432] PW-2372-27
[2433] PW-2443
[2434] PW-2711
[2435] PW-2452; PW-2452-1; Simon, June 17, 2009, p. 64
[2436] PW-2455
[2437] PW-2718
[2438] R. Smith, May 14, 2008, pp. 110-111.

[2228] Wightman promoted Castor to many of his friends and business associates, and many of them became depositors to Castor upon his initiative, advice or instruction, namely:

- Rudolph Steinmetz, Vittorio Sanguineti and Bowne of Montreal.
    - Wightman requested that the financial statements and information memorandum be sent to Steinmetz and Sanguineti, who were his audit clients, for the purpose of them making an investment in Castor.[2440]
    - Both men, as well as the company in which they were principals, Bowne of Montreal Ltd. (which was also an audit client of Wightman[2441]) subsequently made substantial deposits with Castor.[2442]
- Ryan Plastics.[2443]
- Lawrence Rodney.
    - Upon distribution of the payout of the Baxter Street investment, money was placed for Rodney on a short-term deposit with CHIF, at Wightman's request.[2444]
    - in 1990, Wightman was still acting as an agent for Rodney in connection with funds he had on deposit with Castor.[2445]
- Jochem Reiss.
    - Upon distribution of the payout from the Baxter Street investment, Wightman instructed that funds be placed on deposit for Reiss.[2446]
- Sloppin Investments.[2447]
- CAFA Financial.
    - Castor became a significant shareholder in this financial services company that Wightman introduced to Castor, and that was also one of his audit clients.[2448]

[2439] Wightman, March 11, 2010, pp. 72-75; PW-2372-28; PW-2372-29
[2440] Simon, May 1, 2009, pp. 153-154
[2441] Wightman June 20, 1996, pp. 57-60
[2442] Wightman, June 20, 1996, pp. 57-58, PW-1053-25, seq. pp. 53,54, 100-103
[2443] PW-1053-49 seq. p. 101
[2444] PW-643
[2445] PW-1134, bates p. 2450
[2446] PW-643
[2447] See paragraphs of the present judgment

- Wightman is indirectly responsible for the deposit relationship that developed between these companies.[2449]

- Gardex Inc.
  - Gardex Inc. deposited funds with Castor.[2450]
  - The principal of this company was introduced to Castor by Wightman.[2451]

- Colin Cope.
  - Cope was a client of Wightman.[2452]
  - The deposit relationship between Cope and Castor was on Wightman's introduction.[2453]

Introducing Castor to various business deals or opportunities

[2229] Wightman introduced Castor to significant business deals or opportunities: Cafa Financial Corporation, Ouimet Hubbs, Orion Maritime Inc., Brandywine & Iotech Corporation, potential Coat-Hangers (Laurentian Group, JT/Guardian and Sensormatic), Chur, Petra and Sloppin, Baxter Street, CMF and Expo Overseas.

Cafa Financial Corporation

[2230] Wightman was involved in finding investors to participate in Cafa Financial, which became a C&L audit client.[2454]

[2231] Upon Wightman's introduction and advice[2455], Castor invested in this company, along with other Wightman clients such as the Allsops, Steinmetz and Sanguineti[2456]. On November 1, 1986, Castor subscribed for just over 20% of its common shares and just over 40% of its preferred shares[2457].

[2448] Wightman, June 20, 1996, p. 55-57
[2449] PW-1053-28 seq. pp. 45, 57
[2450] PW-1053-25 seq. pp. 53-54, 112
[2451] Simon, May 1, 2009, pp, 146-147
[2452] Wightman, August 15, 1996, p. 68
[2453] Wightman, March 10, 2010, p. 74, PW-1053-18 seq. pp. 205, 219, PW-1053-25 seq. pp. 53-54, 120, PW-1053-28 seq. pp. 45, 71
[2454] PW-1053-23, seq. pp. 106-115, Wightman, February 9, 2010, p. 53
[2455] PW-2400-87
[2456] Wightman, June 20, 1996, p. 57
[2457] PW-1053-23, seq. p. 83

[2232] Wightman advised Castor with respect to this investment and billed Castor for advice and consideration in connection with Cafa Financial[2458].

Ouimet Hubbs

[2233] Wightman introduced Stolzenberg to an investment in a brokerage firm called Ouimet Hubbs[2459]. This investment was presented to Stolzenberg, who determined that the investment should be taken up by Castor, rather than by him personally[2460].

[2234] Castor acquired a 20% interest in the common shares and a 40% interest in the preferred shares of Ouimet Hubbs parent company, 1561159, for a total investment of $760,000[2461]. Both the parent and subsidiary were auditing clients of Wightman[2462].

[2235] Castor ended up having to take significant write-downs on this investment[2463].

Orion Maritime Inc.

[2236] Wightman introduced Stolzenberg to Orion Maritime, a venture in which Castor invested $500,000 in 1987.

[2237] Wightman was involved in this project because he had agreed to take care of the financing arrangements for its principal, Baillargeon[2464].

[2238] While Orion was not an audit client of Wightman, it would likely have become one had the deal gone through[2465].

[2239] The project was not successful, and Castor wrote-off $653,400 in principal and $34,963 in interest as a bad debt at year end in 1988[2466].

[2240] In the end, Stolzenberg viewed the loss that had to be taken on this project as "*the cost of doing business*" with Wightman[2467].

Brandywine & Iotech Corporation

[2241] Wightman introduced Castor to two transactions (identical in structure) that he designed to enable his clients, Mr. and Mrs. Reiss, to reduce the income tax payable from their ventures at the Vancouver exposition[2468].

[2458] PW-2372-25
[2459] Wightman, September 5, 1995, p. 57
[2460] Wightman, June 25, 1996, pp. 149-150
[2461] PW-2400-92, PW-1053-23, seq. p. 89
[2462] Wightman, February 9, 2010, p. 57, PW-1053-23, seq. pp. 93-103
[2463] PW-1053-15, seq. pp. 345-346
[2464] Wightman, February 9, 2010, p. 71
[2465] Wightman, February 9, 2010, p. 78
[2466] PW-1053-23, seq. p. 130
[2467] Ron Smith, May 14, 2008, p. 113

[2242] The first was effected by Castor loaning $35 million to a numbered corporation (141999), which in turn acquired shares in Brandywine, which in turn deposited back the $35 million with Castor.

[2243] The second was effected by Castor loaning $60 million to Munich Fest House and Beergarten Reiss, which in turn acquired shares of Iotech (which was also Wightman's auditing client)[2469], which in turn deposited the same amount with Castor for the term of the loan[2470].

[2244] While Castor earned a $10,000 fee on the closing of each of these transactions, as well as ½% of interest due to the spread[2471] on the "loan"[2472], these transactions served no commercial purpose, and were designed solely so that the Reiss family could save money.

[2245] At trial, Wightman tried to distance himself from Brandywine[2473]. However, he designed the transaction, and introduced all of the parties involved to Castor.

Potential Coat-Hangers (Laurentian Group, JT/Guardian and Sensormatic)

[2246] Wightman initiated several companies to potentially use Castor's facilities in Ireland to establish "coat-hanger" companies for tax saving purposes[2474].

Chur, Petra and Sloppin

[2247] Wightman approached Stolzenberg and Castor[2475] with the opportunity to invest with a number of his friends, acquaintances and C&L partners,[2476] in an offshore investment fund company.[2477]

[2248] Sloppin was an offshore corporation incorporated in the Bahamas. Chur and Petra were the shareholders of Sloppin. Sloppin was owned by its investors through

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[2468] Wightman, February 9, 2010, p. 82
[2469] Wightman, February 9, 2010, pp. 83-84
[2470] PW-2460, Simon, May 1, 2009, pp. 177-179
[2471] Simon, May 1, 2009, p. 180
[2472] PW-2460
[2473] Wightman, February 9, 2010, pp. 82-83
[2474] PW-2470 and PW-2470-1, PW-2469-1
[2475] PW-2462: Memo dated February 11, 1983 from Simon to Stolzenberg. «*E. Wightman advises that they too are proceeding, albeit slowly on the offshore fund. He was pleased to hear that you are interested to pursue the idea as outlined in his memo to you.*»; PW-2400-61: «*Mr. Wightman summarized a proposal in virtue of which the Company could join with others in establishing an offshore company, probably in Bermuda, which could be of significant advantage to senior officers and employees of the Company; it was agreed in principle that management should proceed with such a proposal.*»
[2476] Wightman, February 8, 2010, pp. 191-193.
[2477] PW-347; PW-362; Wightman, February 8, 2010, pp. 186-187

their ownership of shares in Petra and Chur, whose sole assets were their shares in Sloppin[2478].

[2249] The corporations provided tax benefits to Canadian investors under Bahamian and Canadian fiscal laws.

[2250] Castor invested in $200,000 of Petra's preferred shares, half of which was held by CHIF, and the other half, by Stolzenberg personally[2479]. The common shares were distributed equally among Castor's senior management[2480] and Stolzenberg[2481].

[2251] Wightman's wife', Ruth Wightman, invested CDN $125 000 – she owned around 10% of the shares of Chur[2482]. In 1985, when Chur was wounded-up, Mrs. Wightman became a shareholder in Petra[2483].

[2252] Wightman wanted to set up Sloppin in such a fashion that it would not be taxable in Canada. It was necessary for Sloppin to have its headquarters and management outside of Canada. It was also necessary that the actual decision making of the company be done outside of Canada. [2484]

[2253] Wightman called in Bahamian partners, from C&L Bahamas. One of them was Johnson, the company's director in the Bahamas. Johnson relied exclusively on Wightman's advice and due diligence when approving the company's investments, and he could not recall a single instance where he rejected a proposal by Wightman[2485].

[2254] In spite of appearances, Wightman was, in every way, the directing mind of Sloppin.

- He conceived of the operation.[2486]
- He instructed C&L Bahamas to incorporate the companies.[2487]
- He introduced all shareholders.[2488]

[2478] Wightman, June 25, 1996, p. 80: "(...) and between CHUR and PETRA they at that time owned a hundred percent (100%) of SLOPPIN".
[2479] PW-345, PW-350H, PW-350N.
[2480] Wightman, February 8, 2010, pp. 191-192, PW-345, PW-350H.
[2481] PW-350O (shows shares registered to "bearer", Stolzenberg's name appears to have been removed), PW-353O, PW-354O, PW-355O, PW-345 (financial statements confirming that Stolzenberg has 100 common shares and 100,000 preferred shares).
[2482] Wightman, February 8, 2010, p. 191-192.
[2483] Wightman, February 8, 2010, pp. 193-194.
[2484] Wightman, February 8, 2010, pp.185-192
[2485] Johnson, October 27, 1998, p. 146.
[2486] Johnson, October 27, 1998, pp. 63-64.
[2487] Wightman, September 5, 1995, p. 192.
[2488] Johnson, October 28, 1998, pp. 207-208.

- He located all investment opportunities.[2489]
- He negotiated the investments.[2490]
- He did the accounting work for the company.[2491]
- He prepared and sent financial statements to the shareholders.[2492]

[2255] Wightman was in total control of every single investment decision made by Sloppin, and he used this authority to make investments, which were beneficial to Castor or Stolzenberg, and at times, upon their instructions or request.

[2256] When CHIF subscribed for its $200,000 of shares in Petra, Sloppin placed roughly $700,000 on deposit with CHIF. This short-term deposit, made on Wightman's suggestion, included a surplus of funds from the initial share subscription, and remained on deposit with CHIF until another suitable investment was brought forward[2493].

[2257] The money was withdrawn on September 20, 1985, with interest, in the amount of $737,890.70[2494].

[2258] Wightman admitted that one of the reasons he suggested the deposit remain with CHIF was because "*Stolzenberg requested it*[2495].

[2259] Wightman did not disclose to Johnson that CHIF was an audit client when he directed Johnson to make the investment[2496].

121 Baxter Street

[2260] Wightman put together a group of investors to acquire a 50% interest in this condominium project in New York City organized by his friend, Sant Singh Chatwal[2497].

[2489] Johnson, October 27, 1998, p. 68; Wightman June 20, 1996, p. 127.
[2490] Ex: Re Perkins Paper loan: Wightman, September 6, 1995, p. 17.
[2491] Johnson, October 27, 1998, p. 67.
[2492] Wightman, February 25, 2010, p. 23; PW-353-1; PW-354; PW-354I (PW-354 A through to Y are the letters sent to all shareholders for that year); PW-355; PW-355I (PW-355 A through to Z are letters sent to all shareholders for that year); PW-356: PW-351J (PW-351 A through to Z are the letters sent to all shareholders for that year); PW-356-1 (Petra); PW-368-1 (Sloppin): Draft 1990 financial statements with Wightman's notes on them
[2493] Johnson, October 27, 1998, p. 76.
[2494] PW-2535.
[2495] Wightman, June 20, 1996, pp. 139-143.
[2496] Johnson, October 27, 1998, pp. 76-77. and Wightman, June 20, 1996, pp.141-142 testimony that he did not know whether or not he disclosed that information to Johnson and that in his views this was not important
[2497] Wightman, February 9, 2010, pp. 16-17.

[2261] Stolzenberg acquired a 40% interest in the venture[2498] (using funds advanced from CHIF[2499]). The other investors were Wightman's clients, Reiss[2500] and Rodney[2501], and the following Petra's shareholders: Robertson, the Allsop, Pechet and his wife, and Ruth Wightman[2502]. Part of Ruth Wightman's contribution was drawn from the Wightman's joint account by way of a cheque signed by Wightman[2503]. Each acquired a 10% interest in the project[2504].

[2262] Sloppin loaned $280,000 with respect to this project[2505], which Johnson (partner of C&L Bahamas and director of Sloppin) understood to be a loan to the project,[2506] but which in fact was a loan to certain members of Wightman's investment group, namely Stolzenberg, Mrs. Wightman, Robertson and the Allsop[2507].

[2263] This investment was held by Bänziger through a nominee company, Ceru-Wecua[2508], whose directors were Stolzenberg, Gambazzi and Bänziger[2509].

[2264] Wightman was involved in the project as a quasi-manager of the group, and a liaison between this group and the project's principal[2510]. He kept all of them up to date on the progress of the project, and prepared and sent them financial projections with respect to the project.

[2265] When the investment was repaid, Wightman also worked out the distribution of proceeds,[2511] which were deposited in CHIF until all of the instalments were received by Ceru-Wecua[2512]. As appears from the scheme of distribution, CHIF obtained three new depositors from this transaction on Wightman's instructions[2513].

CMF

[2266] Ruth Wightman, Wightman's wife, was a shareholder of 160883, which owned 7,500 shares of CMF on behalf of the Canadian investors in the venture[2514].

[2498] Wightman, February 9, 2010, p. 19
[2499] PW-2523.
[2500] Wightman, February 9, 2010, pp. 20-25.
[2501] PW-1134 bates 2450.
[2502] PW-345 (shows they are shareholders).
[2503] PW-2520; PW-2521.
[2504] PW-2521 (shows they are investors in the project).
[2505] PW-358: Note: on PW-622 series, the loan from Sloppin is shown as only $200,000.
[2506] Johnson, October 28, 1998, pp.232 and following
[2507] PW-644.
[2508] PW-643
[2509] PW-2525.
[2510] Wightman, September 5, 1995, p. 145: «Q: *And you were the one through whom all the communications were taking place?* A: *That's correct.*»
[2511] PW-2524; PW-2543; PW-622-1; PW-622-2; PW-622-3; PW-622-4; PW-622-5; PW-622-6; PW-644.
[2512] Wightman, December 11, 1996, pp. 147-148.
[2513] PW-2521 (Bänziger confirmation); PW-644 (Wightman instructions).
[2514] PW-940 and PW-970.

[2267] Wightman asked Stolzenberg to participate in this investment[2515], which he did, by purchasing 750 shares in the company and by becoming one of its directors[2516].

[2268] Other interested persons in this company included Petra shareholders like Robertson (through his company, Robertson Financial Services) and Cope (through his company Nicophil Investments) and Sloppin's' borrower, Ryan Plastics[2517].

[2269] Wightman was in complete control of CMF:

- He instructed C&L Cyprus to incorporate the company for him in Cyprus.[2518]
- He gave the Cypriot directors all of their instructions.[2519]
- He approved the Cypriot directors' invoices for professional services.[2520]
- He was a signing officer with the authority to manage the company's Canadian bank accounts.[2521]
- He produced the draft financial statements.[2522]
- At his initiative, C&L Cyprus were appointed auditors of the company.[2523]
- Share in the distribution was paid back by CMF to CHIF by way of a cheque signed by Wightman.[2524]

Expo Overseas

[2270] Expo Overseas Management is another business relationship that Wightman entered into with Castor.

[2271] Wightman organized this back-to-back transaction[2525] whereby Castor Finanz and CHIF were used to assist Reiss, a Wightman client, to 'avoid' taxes while financing various restaurants at Expo 88 in Australia[2526]. The operation was funded primarily by

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[2515] Wightman, September 6, 1995, p. 25.
[2516] PW-940
[2517] PW-970
[2518] Wightman, September 6, 1995, p. 26.
[2519] See PW-952, PW-964 as examples of such instructions
[2520] PW-980: Example of an invoice from C&L Cyprus sent to Wightman for approval.
[2521] PW-982.
[2522] PW-985
[2523] PW-940
[2524] PW-2536 PW-2249
[2525] PW-388.
[2526] PW-1012

Reiss. However, Sloppin[2527] and Wightman[2528], alleging that he advanced money for a friend[2529], also contributed.

[2272] The transaction was structured so that the investors could deposit funds with CHIF, and in turn, equivalent funds were disbursed from Castor Finanz to the operations in Australia[2530].

[2273] Wightman proposed using Castor's facilities for these transactions[2531], and communicated with Bänziger with respect to the operation of the account for Reiss[2532].

[2274] At the end of the project, and in consultation with Wightman[2533], the Expo Overseas account at CHIF was converted into a personal in trust account for Reiss, the statements of which were sent to Wightman[2534].

Investments of Sloppin's money: Pigments & Chemical, Compagnie de Recyclage de Montréal, Perkins Paper and Ideal Metals

[2275] The internal staff at Castor, be it O'Connor or Monica Bertele, the secretary of Stolzenberg, referred to Pigments & Chemical, Compagnie de Recyclage de Montréal, Perkins Paper and Ideal Metals as the "*Elliot Wightman Companies*"[2535].

[2276] Stolzenberg's acquisition of his interests in these companies was financed for the most part by Castor[2536].

Pigment & Chemical

[2277] Pigments & Chemical was Wightman's audit client[2537].

[2278] In 1989, Sloppin loaned $750,000 to Pigments & Chemical[2538]. The loan was approved and disbursed on April 10, 1989, even though Johnson only obtained the

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[2527] Johnson, October 28, 1998, p. 259-260.
[2528] PW-2518; Wightman September 5, 1995, pp. 112-115.
[2529] Wightman, February 9, 2010, pp. 48-49.
[2530] PW-2629, PW-2639, PW-2631.
[2531] Wightman, February 9, 2010, pp. 49-50.
[2532] PW-2635, PW-2637, PW-2638.
[2533] PW-2639
[2534] PW-2652.
[2535] O'Connor, January 15, 2009 (p.m.), p. 35.
[2536] Pigment & Chemicals: O'Connor, January 14, 2009, pp. 205-212; PW-668-3A; PW-668-3B, Compagnie de Recyclage: O'Connor, January 14, 2009, pp. 164-171; PW-668-7A, PW-668-7B. PW-668-7B1, Perkins Paper: O'Connor, January 14, 2009, pp. 187-190; PW-668-2A, PW-668-2B, PW-668-2C, Ideal Metals: O'Connor, January 14, 2009, pp 224-237; PW-668-11A, PW-668-11C, PW-668-11E (WOST Holdings) and PW-668-13A, PW-668-13B, PW-668-13E (WOST Development).
[2537] PW-662-4, PW-662-1
[2538] PW-358

documentation on April 24, 1989 and signed the relevant paper work on May 5, 1989[2539].

[2279] Stolzenberg was involved in Pigment & Chemicals as a director[2540] and shareholder, and invested $855,999.60 in shares of 156370[2541], which owned 100% of the shares of Pigments & Chemical.

[2280] Cafa was also a shareholder[2542].

Compagnie de Recyclage de Montréal

[2281] Sloppin loaned $500,000 to La Compagnie de Recyclage de Montréal[2543] as part of the initial financing to enable a group of investors put together by Wightman and Berkowitz, also of C&L[2544] , to purchase the company in January 1989[2545].

[2282] Stolzenberg was one of these initial investors, who invested $400,000[2546] and obtained a 25% interest in the company[2547]. In July 1989, Stolzenberg further injected $122,500 into the operation by way of a loan and a subscription of preferred shares[2548], but he did not reinvest when asked in 1990[2549].

[2283] Sloppin was never repaid.[2550]

[2284] In a memo to Stolzenberg, Bertele, Castor's bookkeeper, wrote: «*He is very well aware of the fact that you invested monies in his company just because of Mr. Elliot Wightman, however, as the deal is now closed and you have invested money in his company he wanted to thank you for your confidence.*»[2551]

Perkins Paper

[2285] Perkins Paper was an audit client of Wightman[2552].

[2286] Sloppin loaned $500,000 to Perkins Paper in 1983, for a period of 10 years. The loan was repaid with a penalty in 1984[2553].

[2539] PW-377A
[2540] PW-662-3
[2541] PW-663-1
[2542] PW-662 (series)
[2543] PW-358
[2544] PW-664-3
[2545] PW-664-3
[2546] PW-668-7A
[2547] PW-664-7
[2548] PW-664-12
[2549] PW-664-15
[2550] PW-353
[2551] PW-664-5
[2552] Wightman, September 5, 1995, p. 68

[2287] The Allsop and Robertson, who were shareholders of Perkins Paper, were also shareholders of Petra[2554].

[2288] Wightman introduced Stolzenberg to this company, and was instrumental in designing the transaction so that Stolzenberg would become a significant shareholder by investing $17,382,750 in 1989[2555]. Half of this acquisition was financed by a loan originally from CHIF, which indirectly became a loan to Stolzenberg's numbered company from Global Management, who in turn became the borrower from CHIF[2556] .

Ideal Metals

[2289] Ideal Metals was an audit client of Wightman[2557].

[2290] Sloppin invested in Ideal Metals by acquiring 2000 shares of the company on September 16, 1986. The other shareholders in this venture were fellow Petra investors and Wightman friends such as Cope (through Marcol Holdings) and Robertson (through Robertson Financial Services)[2558].

[2291] Stolzenberg acquired an interest in this company by purchasing 49% of 147097, which owned shares in 146670[2559], which owned 64% of the shares of Ideal Metals[2560]. Stolzenberg was a director of both of these numbered companies, which were also Wightman's audit clients[2561].

[2292] Wightman assisted Stolzenberg in acquiring shares of Ideal Metals on the market by arranging that purchases be made in trust by an employee of C&L named Duranleau[2562]. Wightman set up this arrangement and gave Duranleau the initial instructions to purchase shares for Stolzenberg at the initial purchase price of $2.00-$2.50. Through this arrangement, Stolzenberg acquired an additional 324,400 common shares of Ideal Metals for $1,033,931.76[2563].

[2553] PW-358
[2554] PW-567-26
[2555] PW-567-20
[2556] O'Connor, January 14, 2009, pp. 187-190; PW-668-2A, PW-668-2B, PW-668-2C
[2557] PW-570-19
[2558] PW-570-6
[2559] PW-570-28
[2560] PW-570-17
[2561] PW-570-6, PW-570-28
[2562] PW-2512, PW-2513
[2563] PW-668-13E

Credibility and reliability

[2293] At trial, Wightman tried to "improve" this portion of his testimony.

- **Example # 1 (disclosure of investments to C&L partners)**
    - At discovery, in 1995 and 1996, he could not remember whether or not he disclosed certain investments, like CMF[2564]. He was not even aware that he was required to disclose his investments in private companies in his annual declaration[2565]
    - At trial, in 2010, he claimed he did consider the C&L Policy carefully, specifically provision 16 (a), and concluded that due to the size of the investments or the control or influence exerted over the projects, disclosure of these investments was not required[2566].
- **Example # 2 (Sloppin's deposit of 700 000$ with CHIF)**
    - At discovery, on September 5, 1995, Wightman could not recall any circumstances for the deposit[2567].
    - At discovery, nine months later, on June 20, 1996, Wightman remembered having advised Johnson to deposit a surplus of funds with Castor because Stolzenberg had requested it[2568].
    - At trial, fourteen years later, on February 9, 2010, Wightman claimed that Simon had requested that the surplus of funds be loaned to Castor and that he had communicated the terms of the deposit to Johnson on Simon's behalf,[2569] whereas Simon testified that, other than physically repaying the deposit, he had no knowledge and remembered no discussions about the transaction[2570] - the Court believes Simon's version of the facts.
- **Example # 3 – (Castor's investment in Orion Maritime)**
    - At discovery, on June 25, 1996, Wightman was certain that the deal was presented to Stolzenberg in a non-specific way, and that Stolzenberg, not him, had decided to give this venture to Castor.[2571]
    - At trial, in 2010, Wightman recounted in great detail that he introduced this deal to Castor, and cited many reasons, including Castor's knowledge of

[2564] Wightman, August 15, 1996, pp. 77-78
[2565] Wightman, September 5, 1995, 160-162
[2566] Wightman, February 9, 2010, pp. 41-43
[2567] Wightman, September 5, 1995, pp. 210-211
[2568] Wightman, June 20, 1996, pp. 139-143
[2569] Wightman, February 9, 2010, pp. 10-12
[2570] Simon, May 1, 2009, pp. 231-234, June 17, 2009, pp. 131-133
[2571] Wightman, June 25, 1996, pp.151-152

the hotel industry and Luerrsen's knowledge of the shipping industry as to why he thought that Castor might be interested in participating.[2572]

[2294] Wightman minimized his role or refused to admit certain facts until he was confronted with evidence that he could not discard.

- **Example # 1 : preparation and sending of financial statements for Petra**
    - At trial, in examination in chief, on February 9, 2010, Wightman minimized his role with Chur, Petra and Sloppin:
        - ***The only thing that I did*** *was I,* ***from time to time****, introduced new shareholders or advised them that some shareholders wished to withdraw. I, from time to time,* ***suggested that they consider*** *some investment deals, and I also did* ***some accounting*** *work for Sloppin, which annually I would* ***send to Mr. Johnson for him to*** *incorporate and to produce the final financial statements.*[2573] (emphasis added)
    - At trial, in cross-examination, on February 25, 2010, confronted with the content of various exhibits[2574], Wightman had no choice but to admit that his involvement went beyond that which he had previously testified to – that he had sent financial statements[2575].

[2572] Wightman, February 9, 2010, pp. 71-77
[2573] Wightman, February 9, 2010, p. 8.and Wightman, February 25, 2010, p. 23
[2574] PW-353-1: Letter from Wightman to Johnson stating that they the 1987 financial statements are being sent to shareholders "over" Johnson's name; PW-353I: Letter enclosing the1987 Financial Statements of Petra sent to Simon c/o Stolzenberg (PW-353 A through to Y are letters sent to all shareholders for that year); PW-354: Letter from Wightman to Johnson stating that they the 1988 financial statements are being sent to shareholders "over" Johnson's name; PW-354I: Letter enclosing the1988 Financial Statements of Petra sent to Simon c/o Stolzenberg (PW-354 A through to Y are the letters sent to all shareholders for that year); PW-355: Letter from Wightman to Johnson stating that they the 1989 financial statements are being sent to shareholders "over" Johnson's name; PW-355I: Letter enclosing the1989 Financial Statements of Petra sent to Simon c/o Stolzenberg (PW-355 A through to Z are letters sent to all shareholders for that year); PW-356: Letter from Wightman to Johnson stating that they the 1990 financial statements are being sent to shareholders "over" Johnson's name; PW-351J: Letter enclosing the1990 Financial Statements of Petra sent to Simon c/o Stolzenberg (PW-351 A through to Z are the letters sent to all shareholders for that year); PW-356-1 (Petra); PW-368-1 (Sloppin): Draft 1990 financial statements with Wightman's notes on them
[2575] Wightman, February 25, 2010, p. 23

- **Example # 2 – Baxter Street –preparation of financial projection**
    - At trial, in examination in chief, on February 9, 2010, Wightman claimed that:
        - he was not involved at all with Stolzenberg's decision to invest, apart from introducing the project; and
        - all information had been provided by his friend Chatwal[2576]
    - At trial, in cross-examination, on February 11, 2010, Wightman was confronted with a document that he had himself prepared and had remitted to his group of investors including, namely, Stolzenberg and had sent to Bänziger[2577].

[2295] Wightman denied being aware of certain things or being involved in certain arrangements. The Court does not believe him.

- **Example # 1 – knowledge of Stolzenberg being a director of CMF**
    - Wightman claimed he did not know that Stolzenberg was a director of CFM and that he learned about that through discovery (it came as a complete surprise to him).[2578]
    - Notes of a meeting attended by Wightman concerning CMF indicate that Stolzenberg was one of the directors for the company. [2579]
- **Example # 2 – Stolzenberg's investment in Perkins Paper -source of financing**
    - Wightman claimed that he did not put his mind to the issue of the source of the financing[2580];
    - Wightman was deeply involved in the details of this transaction,[2581] and he raised the question of financing[2582].

[2576] Wightman, February 9, 2010, pp. 17-19
[2577] Wightman, February 11, 2010, pp. 87-92; PW-2524 and PW-3097
[2578] Wightman, February 9, 2010, p. 38
[2579] PW-951
[2580] Wightman, June 25, 1996, pp. 139-141
[2581] PW-567-20, PW-567-25
[2582] PW-567-24

- **Example # 3 – arrangement to help Stolzenberg buy shares of Ideal Metals**
    - Wightman claimed that he only introduced Stolzenberg to Mrs. Duranleau of C&L, and he denied having anything to do with instructions.[2583]
    - Exhibits PW-2512 and PW-2513 show otherwise.

Conclusions

[2296] As C&L knew, a purpose of its engagement to audit Castor was to add credibility to the financial statements of Castor[2584]. Clients and people associated with them rely on auditors because they believe in the auditors' professional integrity, independence, and objectivity.

[2297] Objectivity is a fundamental tenet of auditing.

[2298] At all relevant time, Wightman had to have an objective state of mind:[2585] he did not.

[2299] Objectivity imposes the obligation to be impartial, intellectually honest, and free of conflicts of interests. Independence enhances the auditor's ability to act with integrity and objectivity. Independence is a question of fact.

[2300] Wightman had a double responsibility :

- to avoid actual impairment of objectivity – to avoid actual impairment of willingness to recognize and confront the facts regardless of consequence; and
- to avoid perceived impairment of objectivity - to avoid perceived impairment of willingness to recognize and confront the facts regardless of consequence [2586]

[2583] February 9, 2010, Page 64

[2584] PW-1420, tab 2 – C&L Technical Policy Statement ("TPS") - Accounting & Auditing (TPS-A-104), entitled "Professional Independence" on October 15, 1977 and a revised version on October 5, 1988 – Introduction – section 2

[2585] PW-1419-1A, Section 5000.02 (1988); PW-1419-2A, Section 5000.02 (1989); PW-1491-3A, Section 5000.02 (1990)

[2586] PW-1421-2: *R. J. Anderson*, F.C.A., "The External Audit", second edition, published in 1984, pages 53 to 58 section entitled "Objectivity"

[2301] Any of the following interactions an auditor has with an audit client or with persons associated with an audit client in decision-making capacities (chief executive and financial officers, directors, substantial shareholders and other senior persons in a position to influence the client or the way the client manages his affairs) can impair the auditor's objectivity or the auditor's willingness to recognize and confront the facts regardless of consequence:

- Borrowing money from;
- Lending money to; or
- Engaging in any other business relationships (participation in joint business ventures and limited partnerships, lease arrangements, sales of items and other business transactions related to the supplying of professional services).

[2302] It is of no surprise that all of the above is prohibited by C&L in its technical policy entitled "Professional Independence"[2587].

[2303] Wightman, in respect of his engagement to express an opinion on Castor's financial statements in 1988, 1989 and 1990, had to hold himself free of any influence, interest or relationship that could impair or would impair or would be perceived as capable of impairing his professional judgment or objectivity[2588].

[2304] While it was not unusual for professional accountants to introduce investments opportunities to and between clients and to refer business to clients, as Froese[2589] and Levi[2590] acknowledged, it remains that such activities could only be legally done if they had no impact on the objectivity of the auditor.

[2305] As the summary of evidence in previous paragraphs of the present judgment indicates, Wightman interacted with Castor and Stolzenberg in the various ways described above and on numerous occasions.

[2306] Wightman's professional judgment was impaired and caused him to approach the audits without exercising objectivity or independence. Conclusive proof of such impairment includes his casual attitude towards the work performed by his audit teams, which demonstrates carelessness, his absence of skepticism in his dealings with Stolzenberg, his superficial wrap-up meetings which, in fact, never probed any transaction to the bottom, and his blindness to numerous "red flags" or suspicious circumstances.[2591]

[2587] PW-1420, tab 2 – C&L Technical Policy Statement ("TPS") - Accounting & Auditing (TPS-A-104), entitled "Professional Independence" on October 15, 1977 and a revised version on October 5, 1988

[2588] Sections 3.02.01, 3.02.05 and 3.02.06 of the Quebec Code of Ethics of Chartered Accountants

[2589] Froese, December 8, 2008, pages 156 to 158

[2590] Levi, February 2, 2010, pages 52-53

[2591] For a list of some of those red flags, see Froese, January 27, 2009, pp. 58-64

[2307] The fact that he hid these numerous relationships from his partners in his annual declarations[2592], and to his partner Johnson in the context of their relationship for Sloppin, suggests that he knew or felt that he had something to hide. Moreover, his changing or "improved" testimonies on these issues point in the same direction.

Inappropriate planning

[2308] The Handbook defines "planning" as follows:

> Audit planning consists of developing a general strategy and a detailed approach for the expected nature, extent and timing of the examination. Analytical procedures would assist the auditor in developing a general strategy and a detailed approach (see AUDIT EVIDENCE, paragraph 5300.31). Plans may need to be changed as the audit progresses.
>
> Matters which the auditor needs to consider when planning his examination include:
>
> (a) the terms of the engagement and the expected date of his report;
>
> (b) the nature of the client's business including applicable statutory and contractual requirements;
>
> (c) the experience gained during the previous audit engagements;
>
> (d) the accounting policies and the degree of complexity of the accounting systems;
>
> (e) materiality and the components of audit risk;
>
> (f) any involvement of other auditors;
>
> (g) any involvement of internal auditors and persons having special expertise;
>
> (h) the intended reliance on internal controls;
>
> (i) the level of experience and number of any assistants to be assigned to the engagement, and, and
>
> (j) the date the procedures are to be performed taking into account the availability of audit evidence to be obtained and the effectiveness of performing such procedures at that date.[2593]

[2592] PW-2527.

[2593] PW-1419-1A, sections 5150.05 and 5150.06 (1988); PW-1419-2A, sections 5150.05 and 5150.06 (1989); PW-1419-3A, sections 5150.05 and 5150.06 (1990)

[2309] C&L technical material also includes information and instructions relating to planning:

> 16. Auditors must plan their examination in the knowledge that the financial statements could be materially misstated because of fraud and the nature, extent and timing of audit procedures should be designed to detect material misstatements from this cause.[2594]

[2310] In order to determine its audit plan and audit procedures, an auditor has to understand the nature of his client's business. If the nature of that business evolves, the auditor has to determine if the audit plan and resultant audit procedures need to be modified.[2595]

[2311] For the 1988, 1989 and 1990 audits, it was imperative that C&L understand the true nature of Castor's business to select appropriately the audit strategy[2596].

[2312] Castor held itself out to be a short-term lender. In its marketing materials, Castor described its business as focused «*on short and medium term loans in the North American mortgage market*».[2597] In fact, as the nature of Castor's business progressed during the 80s, Castor slipped farther and farther away from being a short-term lender.

[2313] From a short-term lender, Castor became a long-term lender, accepting primarily unsecured high risk. This was not hidden from the auditors, but C&L ignored that change in the nature of their client's business and failed to implement an audit plan that was appropriate in the circumstances.

[2314] C&L failed to alter their auditing approach of project loans secured by real estate and to adjust it to corporate borrowings, which is wholly dependent on the capacity of the borrower to pay. C&L audited unsecured relationship loans (corporate borrowings) the same way they audited mortgage loans secured by real estate[2598].

[2315] The planning failed to differentiate among the different types of loans and to specify audit procedures for each different type. For example, the planning for auditing the carrying value of a mortgage loan ought to have been very different from the planning for an unsecured loan which would differ from a loan secured by a pledge of shares, which would differ from a loan supported by a personal or corporate guarantee.

[2316] Furthermore, for each type of loan, the planning ought to have focused on the loan which had the greatest risk to Castor. For example, it is inexplicable that the

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[2594] PW-1420, TPS-A-101 "Professional Responsibilities and Conduct" - revised August 31, 1988.
[2595] PW-3034, p. 9
[2596] PW-3034, pp. 11-20
[2597] PW-1057-1, (June 1988); PW-1057-2 (April 1989); PW-1057-3 (April 1990)
[2598] PW-2908, Vol. 2, F-12; PW-2941, Vol. 3, pp. 12-14

auditors would have reviewed the carrying value of a first ranking mortgage loan on the CSH and not considered the lower ranking mortgage or equity loans related to the same project.

[2317] The planning was performed in an automatic, thoughtless manner without professional judgment or serious consideration of anything other than going through the motions of mindlessly filling out forms.

[2318] The planning did not include instructing the staff on how to perform audit procedures. For example, in addressing the procedure as to whether interest had been paid or capitalized, there was no explanation as to how interest charged to account 046 was to be treated.

[2319] In determining whether repayment terms were being met, the almost universal failure of Castor's borrowers to comply with contractual obligations was not addressed. Although C&L requested that Castor prepare year-end working papers[2599] each year, a review of the information that C&L requested discloses that no attempt was made to have Castor provide them with financial information on borrowers, loan to value and other applicable financial ratios, credit approval and monitoring assessments, compliance by borrowers with covenants, details of revenue received in cash, and all of the other types of typical information that one would expect a diligent lender to retain in its loan files.

[2320] The audit was not planned to give the auditors enough time to complete the audit. This was particularly problematic given the lack of experience of the audit staff assigned to the more complicated aspects of the portfolio and the absence of staff continuity. The work should have begun prior to the year end and should have been completed following the year end in order to allow sufficient time for the complex work to be completed. The need for additional time was recognized during the 1990 wrap-up meeting when Wightman arranged with Stolzenberg for pre-audit work to be performed on the loan portfolio in future audits so that the staff could have sufficient time to complete their work. This procedure should have been put into effect earlier, for the 1988, 1989 and 1990 audits.

[2321] In 1990, Hunt was recruited at the last minute[2600] to act as the supervisor of the CHL audit. He had never worked on Castor's audit. He had never worked on any similar client's audit. He had no experience with the real estate business or with the lending business.[2601] He did not know Wightman and had never met him. He did not know Quintal either. He had no knowledge of Castor's affairs.[2602] He came from Nova Scotia and acted as the supervisor of the audit without even meeting with or speaking to the

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[2599] For example, D-29-1; Tooke, February 27, 2008, pp. 91-97.
[2600] Hunt, March 28, 1996, p. 20
[2601] Hunt, March 28, 1996, pp.5 and following
[2602] Hunt, March 28, 1996, pp. 10-11

engagement partner, Wightman.[2603] He did not know the staff members whom he was asked to supervise. Nevertheless, he planned[2604] and supervised the audit!

[2322] No planning occurred with respect to obtaining audited (or even unaudited) financial statements of borrowers, guarantors and the entities whose shares had been pledged or whose accounts had been assigned as collateral. This omission was particularly troubling in the case of unsecured loans, loans secured by pledges of shares and loans secured by assignments of accounts receivable. During the 1988 to 1990 period, the audit staff charged with reviewing the investment section in both Montreal and Europe did not receive one single audited financial statement of a borrower or of an entity relied upon to give value to security.

[2323] No planning occurred for the use of appraisals. The staff members were not instructed in the required steps for analyzing the assumptions used in an appraisal report and comparing such assumptions to actual performance.

[2324] The planning did not provide any instructions or procedures to assess whether loan covenants had been breached by borrowers. No procedures were planned to question management on their credit approval and monitoring processes. The audit plan failed to include any provision for having staff experienced in the audit of loans generally, and real estate loans in particular, assigned to this crucial function.

[2325] In 1988 and 1990, the planning did not require calculation of the quantum of capitalized interest in Montreal. This aspect was not considered at all in the overseas audits during any of the three years, even though such a calculation was effected in 1986. In the overseas audit, there was no planning memorandum and no evidence in the AWPs of audit planning in any of the three years.

[2326] The complexity of the structure of the loans and the detailed audit work required to properly perform the required audit procedures could only be done by an experienced and well trained auditor with specific knowledge of the audit of real estate and construction loans. The failure to plan for appropriately trained and experienced staff was exacerbated by the superficiality of the supervision and review. Countless errors contained in the AWPs are eloquent evidence of the failure to plan for supervision and review.

[2327] C&L was opining on consolidated audited financial statements. Planning was even more crucial that C&L had accepted to use two separate and different audit teams, one for CHL and one for the overseas subsidiaries, while CHL and the overseas subsidiaries were lending to the same borrowers[2605].

[2603] Hunt, March 28, 1996, p. 20
[2604] Hunt, March, 28, 1996, pp. 29 and following
[2605] For example see : YH Group, MLV, MEC and the Toronto Skyline

[2328] For example, C&L failed to take into account how the client's business had evolved, namely how much more loans and allegedly generated revenue were with the overseas subsidiaries, and to allocate the proper human resources accordingly.

> the **portfolio overseas** was growing and it **now surpassed the portfolio in Montreal** and a consolidated audit plan was properly used sending **two peoples overseas** to do the audits of a number of companies, two sets of consolidations, put them together, plus audit a loan portfolio that's larger than the loan portfolio in **Montreal**, where you're sending **five people in for three weeks**, and you're sending **two people for ten days**, roughly, **overseas**, that's just **a recipe for disaster**.[2606] (our emphasis)

[2329] The following illustrates the effect, a negative consequence, of the failure to plan the audit in conjunction with the C&L Europe team.

- Ford did not select the $20 million of CFAG loans made to YH (YHDL and KVWIL) for audit review even though these loans represented the vast majority of the loan portfolio of CFAG and even though the audit plan in Montreal called for C&L to select approximately 85% of the loans by dollar value for detailed audit work.

[2330] Knowledge gained in prior audits should have served as planning tools.[2607] The following examples will serve as illustrations of knowledge that could have, and should have served, but did not:

- The situation of the loans to Lambert (never followed up) and the relationship between the Lambert loans and the Toronto Skyline property.
    - C&L knew, prior to 1988, about the relationship between Lambert and Topven and the information should have been brought forward each year.
    - Ron Smith confirmed the relationship when he explained the major refinancing to the junior auditor for the 1988 audit.[2608]
    - For the 1986 audit, JG Martin brought forward the fact that he had been unable to obtain financial information about Lambert from Stolzenberg and that the consolidated financial statements should not be released in final form without that information.[2609] Wightman erroneously assumed that the balance sheet of Lambert was provided to his staff although there is no evidence in the AWPs to that effect.[2610] The 1986 audited financial statements were issued and there was no follow-up thereafter.

[2606] Vance, March 13, 2008, p. 183
[2607] Vance, March 11, 2008, p.41; PW-1419-1A, section 5140.06 (1988); PW-1419-2A, section 5140.06 (1989); PW-1419-3A, section 5140.06; Wightman, February, 11, 2010, pp.143 and following
[2608] R. Smith, September 5, 2008, pp. 34-35.
[2609] PW-1053-31, seq. p. 278.
[2610] Wightman, February 11, 2010, p. 171.

- Pursuant to discussions that would have taken place at the 1986 wrap-up meeting, something was supposed to happen to the Lambert loans within a short period. Nothing happened, except the continued capitalization of interest. There was no follow-up.

- Reluctance of Stolzenberg to communicate information.[2611]

- The capitalization of interest on the CHL loans to debenture holders of MLV to a CHIF loan[2612] (in relation to compliance with loan covenants).

- Representations made regarding the payment of loans related to the MLV project in 1986 and 1987 (not followed up).

- Representations relating to refinancing of certain projects[2613] (planned refinancing[2614]), and the need for projects to be sold to "clear out" the loans.[2615]. (For example, with respect to Mellon Bank and the MLV project).

- Concentrations of loans – more than 50% of Castor's loans were connected to the YH group (a fact that appeared from the AWPs).

- The very small amount of cash payments during eleven months (January to November), the significant amount received in December and the use of Account 046 (YH account), especially at year-end.

- The nature of the security for the loans in the portfolio – by 1988, less than half of the loan portfolio was secured by collateral in the form of real estate.

- The roll over, year after year, of loans.

- Gambazzi acting for Stolzenberg on an "in trust" basis, from time to time (in connection to related party transactions).

[2331] C&L should have followed-up on the client's representations made at the year-end meetings, they should have used them as a planning tool, but they did not. Had they done that, they might have elucidated some management misrepresentations. The following examples will serve as illustration:

[2611] PW-1053-3, pp. 473-477; Wightman, February 11, 2010, pp.159 and following

[2612] PW-1053-3, pp.473-477

[2613] PW-1053-23, seq. p. 168 re: Skyline Hotels; R. Smith, September 5, 2008, p. 40.

[2614] PW-1053-23, seq. p. 117 re : $50M from the Mellon Bank so that Castor's loans will be reduced in the next 3-4 months by $15-18M.

[2615] PW-1053-23, seq. p. 117 re : Meadowlark, which C&L knew was an Edmonton Shopping Centre ranking behind a loan to BMO.

- Representations at the 1986 audit year end meeting that some of the loans relating to the MLV project (loans to debenture holders) should be repaid by 1987.[2616] None of these loans were repaid.

- Representations at the 1988 audit year-end meeting about a complete refinancing of MLV by Mellon bank, about a reduction of Castor's exposure on MLV and about the sale of the project for $90 to $100 million (sale in 1990) or sale of the mortgage.[2617] The Mellon Bank withdrew its offer to finance, Castor's exposure increased and nothing was sold.

    - Wightman said that Stolzenberg had advised him that the Mellon Bank financing had not gone through but there is no documentary evidence that Wightman or anyone at C&L inquired about why these plans did not materialize. There is no evidence either that anyone considered the implications of the abortion of the Mellon Bank financing with respect to the collectability of the related loans[2618]or how this information impacted on the future operations note[2619] in the draft 1987 MLVII financial statements contained in the AWPs.

[2332] The audits were not planned to address the dangerous concentration of loans to the YH group and the risks associated with such concentration.

[2333] Although C&L understood that Castor's practice of capitalization of interest was a "hot topic" because of the possibility that borrowers could not meet their obligations, they did not adjust their audit of the loans to obtain information as to why the borrowers were failing to meet their loan covenants (as had been recommended by Higgins in the peer review). This was a blatant audit failure. C&L also failed to determine why the YH borrowers were not respecting their loan covenants regarding the monthly payment of interest and, in the case of loan 1081, the quarterly payments of principal and interest[2620].

[2334] The audits were not planned to allow sufficient resources and sufficient time to carry out the needed work, and it jeopardized the confirmation process of the overseas subsidiaries of Castor.

[2335] For the overseas subsidiaries, C&L used a confirmation process they should never have contemplated, and which defeated the purposes of this essential audit procedure. They completely gave up control over the preparation and the mailing of the confirmations, leaving it into the hands of Bänziger. They also gave up having an audit staff member, who knew about Castor's business and affairs, and who could review the

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[2616] PW-1053-3, sequential page 474; Wightman, February 11, 2010, pp.176 and following
[2617] PW-1053-23, sequential page 117; Wightman, February 11, 2010, pp. 189 and following
[2618] Wightman, February 25, 2010, pp. 86–91; PW-1053-19, seq. p. 102.
[2619] R. Smith, May 16, 2008, pp. 89-92; PW-1053-23, seq. p. 166.
[2620] PW-1054-3

signed confirmations: the confirmations were sent to C&L's Geneva office, and they were handled by a C&L Geneva partner who did not have that knowledge.

[2336] When correctly performed, the confirmation procedure provides one of the best forms of substantive audit evidence, especially when dealing with third parties.[2621] The existence assertion is confirmed: it is one of the most used audit tests, a universal test.[2622] But for it to achieve its goals, there are fundamental prerequisites.

[2337] In his book "*The External Audit*", R.J. Anderson, an authority recognized by all experts who appeared before this Court, identifies the six prerequisites for reliable confirmation (to allow the confirmation process to satisfy its purposes):

> Six prerequisites for reliable confirmation are: **respondent independence**, client consent, **careful checking**, **auditor control**, provision of return address, and respondent comprehension. (...)
>
> 1. **Independent respondents** can be expected, in their own self-interest, to provide accurate replies to confirmation requests. Most non-independent respondents may be equally accurate in their responses, but there is always the danger (a) that they themselves rely wholly on the records of the company under audit or (b) that they may be instructed by an officer of that company to provide a specified response without further checking. In either case, the confirmation provides no evidence in addition to that available from internal documentary evidence, and **in the latter case it may well be concealing fraud or deliberate misrepresentation. Control over the risks of reliance on non-independent respondents depends on** the thoroughness of the auditor's procedures for identifying related parties and auditing related party transactions (see Chapter 21).
>
> (...)
>
> 3. All pertinent **information in the confirmation request should be carefully checked by the auditor prior to mailing.** Descriptive information, dollar amounts, date of the confirmation, and name and address of the prospective respondent **should be compared to the client's accounting records.** If the address is a post office box number or if it appears unusual, it may be desirable to compare it with the telephone book or trade directory. If control is inadequate to prevent an employee from misappropriating cash receipts, that employee could use a post office box or other address to which he or she controlled access, under a fictitious name or the name of an actual customer, to intercept correspondence such as a confirmation request and fabricate a fraudulent reply.
>
> 4. It is important **the auditor control** the selection, preparation, checking, and mailing of the confirmation requests. There is always the danger that they may

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[2621] PW-1419-1A, section 5300.20 (1988); PW-1419-2A, section 5300.20 (1989) ; PW-1419-3A, section 5300.20 (1990); Vance, April 7, 2008, pp.47 and following

[2622] Vance, April 7, 2008, p.48

> be inadvertently lost or, worse, deliberately suppressed or altered by an employee wishing to conceal discrepancies. Thus, while the assistance of the client's clerical staff should be sought to minimize the costs of preparing, typing, and addressing confirmation requests, **these procedures and the final mailing of the requests should be under the auditor's control.** (...) [2623] (our emphasis)

[2338] C&L knew control was an essential ingredient of the integrity of the confirmation process: in their internal material, they described the procedures as follows:

> 5 The procedures listed below should be among those followed when the confirmation technique is employed:
>
> (a) The request should be mailed by the auditor.
>
> (b) An envelope bearing the auditor's return address should be included in the mailing to ensure that the response is received directly.
>
> (c) Names and addresses should be checked to appropriate client records.
>
> (d) Any requests that cannot be delivered by the post office should be investigated either by the auditor or by the client under the auditor's control.
>
> (e) Account balances and other financial information included in the confirmation request should be checked to the accounting records. When such checking is done to detailed accounting records that support a control account, the total of the details should be agreed to the control account. After such checking has been completed, the auditor should maintain control over the confirmation requests until he has mailed them.
>
> (f) All responses should be reviewed, and any exceptions noted should be investigated either by the auditor or by the client under the auditor's control.
>
> (g) Confirmation requests should be clear and concise and should be prepared in a form that makes replying easy (e.g., by providing a copy of the request for return to the auditor and space for the addressee to sign indicating that the information is correct).[2624]

[2339] Moreover, C&L was aware that a review of the signed confirmation responses was a procedure which could assist the auditor in identifying undisclosed related party transactions. In connection with the 1982 audit, one of C&L's supervisors indicated in the following queries in respect of returned confirmations:[2625]

[2623] PW-1421-1
[2624] PW-1420, tab 13, TPS-A-313, Appendix A, page 2
[2625] PW-1053-49, audit working papers BB-7 to BB-72

> Have you examined signatures - it appears that Stromeyer & Raulino are same.- Pls verify that all related parties are adequately disclosed. The confirmations may tell you something[2626]

[2340] The alleged reasons[2627] that would explain and justify C&L's decision to accept the total delegation of the confirmation process to Bänziger are unacceptable. Even though it was legitimate to wish to satisfy the client's deadline and to try to maximize the responses' rate, C&L should have known better.

[2341] C&L was not facing a situation described in sections 6020.12 and 6020.19 of the Handbook:[2628] communication with Castor's debtors was not impracticable or deemed to be harmful[2629]. In any case, assuming C&L could or would have seen it otherwise, abdicating the control of the confirmation process in favor of Bänziger was not a suitable alternative.

[2342] Lack of planning had a serious and negative impact on the quality of the audit work, and it prevented the exercise of sound professional judgment, whereas it is a cornerstone to comply with GAAS.

Examination performed without due care and by persons that did not have adequate technical training or proficiency in auditing

[2343] For the 1988, 1989 and 1990 audits, C&L never asked to see any credit analysis performed by Castor in connection with the making or the renewal of the loans that they reviewed with Ron Smith[2630].

[2344] They did not question Ron Smith as to the performance of the projects, the debt service requirements associated therewith or the financial capacity of the borrowers or guarantors to satisfy their obligations.[2631]

[2345] This is particularly noteworthy because in November 1988 (prior to the 1988 audit), a peer review of the Castor Montreal audit specifically noted that the loan questionnaires «*do not address the question of whether the client is up to date with their review of the debtors financial position or has complied with all loan covenants.*

[2626] PW-1053-47- 3 seq. p. 333
[2627] Jean Guy Martin, January 5, 2010, pp.117-118
[2628] PW-1419-1A (1988); PW-1419-2A (1989); PW-1419-3A (1990); see also PW-1419-4A (same section – no significant changes- from 1973 to 1987)
[2629] For example: see exhibits and situations described by Counsel for the Plaintiff in Jean Guy Martin cross-examination, January 6, 2010, pp.222 – 237 and January 7, 2010, pp.31-53
[2630] Ron Smith, May 14, 2008, p. 92
[2631] Ron Smith, May 14, 2008

Consideration should be given to revising the loan review sheets used in conjunction with those currently in use on bank audits»[2632]

[2346] Despite this criticism of the audit work, C&L did not modify the questionnaires or attempt to assess the way Castor approved or monitored loans.

[2347] The audit work was superficial, limited to a mechanical review of commitment letters and promissory notes and the filling out of forms, without thought or analysis.

[2348] Smith described the exercise as follows:

> They never asked me to review any financial statements or the results of the hotel. That was not part of their focus. Their focus was basically a superficial type of analysis. And it was the same for all loans, it was a review of the loan documentation to make sure that it was in order, and it was a limited review, limited primarily to promissory notes, mortgage documents and the appraisal, and that was it. There was no other review of any other documents, and I was never asked for it. [2633]

[2349] Smith's description of the exercise is corroborated by the testimonies of audit team members who worked on the CHL investment section of the audits.[2634]

[2350] C&L did not request to see audited or unaudited financial statements of YHDL, YHDHL, KVWIL or other YH entities, nor net worth statements of Wersebe. In fact, C&L did not consider that financial statements were a necessary tool to perform their audit work, and they did not consider the borrowers' capacity to pay[2635].

[2351] The most junior members of the Montreal audit team were assigned to audit the loans. Information that appeared in AWPs of prior years was mechanically (and usually erroneously) brought forward to later audit years without any analysis or critical review.

[2352] C&L had the obligation to assess the credit monitoring process and to verify that Castor's borrowers were complying with their loan covenants. They failed to perform such elementary auditing procedures.[2636]

[2353] Junior staff believed that promissory notes were security and merely compared the loan balance to the face amount of the promissory note to determine if there was a deficiency.

[2632] PW-1426, para. 5(h)
[2633] R. Smith, September 5, 2008, p. 47
[2634] 1988: Séguin, December 12, 1995, pp. 283-295, October 25, 1996, pp. 60-68, pp. 152-153, pp. 193-195, and p. 237.; 1989: Belliveau, April 1, 1996, pp. 69-96, 109; 1990: Quesnel, November 23, 1995, pp. 176-188, November 24, 1995, pp. 102-108
[2635] Quintal, February 19, 1997, pp. 39-44; December 1, 1995, pp. 85-95; Belliveau, April 1, 1996, pp. 98-103; Quesnel, November 24, 1995, pp. 147-155; Wightman, September 27, 1995, pp. 36-38
[2636] PW-2908, Vol. 1, p. 4-B-13; Vance, March 13, 2008, pp. 179–186; Vance, March 6, 2008, pp. 79-84

[2354] C&L failed to consider the purpose of the loans and to verify whether funds were being advanced to borrowers to create value.

[2355] Numerous red flags[2637] were readily apparent regarding the portfolio at large and the YH corporate loans, in particular. Information was available to C&L audit staff members, but they did not look at it or they did not ask for it.[2638]

[2356] When negative information was provided to C&L, their audit approach did not change, and no further questions were put to Castor management. The auditor did not request or obtain additional audit evidence.[2639]

Lack of supervision and review

[2357] The Handbook defines "supervision" as follows:

> Supervision consists of:
>
> (a) instructing assistants as to:
>
> > (i) the procedures they are to perform and the objectives of such procedures, and,
> >
> > (ii) matters such as those outlined in paragraph 5150.06 which in the auditor's judgment are relevant to the portion of the examination they are to perform;
>
> (b) determining by such means as observation, discussion and review whether the work carried out by assistants is properly executed, and,
>
> (c) keeping informed of auditing problems encountered by the assistants during the examination so that their significance may be evaluated.[2640]

[2358] C&L's own material includes the following information and instructions relating to supervision and review:

> 1. When a partner delegates work to other personnel, he continues to be responsible for forming and expressing the opinion of the financial statements.

[2637] Vance, March 13, 2008, pp.181-182; Froese, November 28, 2008, pp.187 and following; Froese, December 2, 2008, pp. 124-127; Froese, January 12, 2009, pp.101-102; Froese, January 27, 2009, pp. 58-64 ; Rosen, February 17, 2009, pp. 220- 223; Rosen, February 20, 2009, pp. 178-179; Rosen, February 27, 2009, p. 17, 91, 97, 168, and 209 and following ; Rosen, March 24, 2009, pp.28 and following; Selman, May 6, 2009, pp.93-94; Levi, January 29, 2010, pp.169-170.

[2638] R. Smith, September 17, 2008, p. 162

[2639] R. Smith, September 16, 2008, pp. 213-218.

[2640] PW-1419-1A, section 5150.07 (1988); PW-1419-2A, section 5150.07 (1989); PW-1419-3A, section 5150.07 (1990);

For this reason, adequate control procedures involving supervision and review are an essential part of engagement management.

2. Supervision includes monitoring the work done to ensure it is in accordance with the audit strategy and plan. Detailed monitoring would usually be performed by the staff member in charge or the manager.

3. Supervision also involves:

> (a) Monitoring the progress of work to determine that personnel at all to have the necessary skills for their assigned tasks, to understand their instructions and to be performing their work in accordance with the audit program and other planning documents;

(...)

4. Thus, work done by each auditor should be supervised, reviewed and approved by a more senior person. The staff member in charge will normally review the work of staff under his control, the manager will review the audit as performed by the field staff, and the engagement partner will review the overall quality and conduct of the audit.

(...)

6. The manner in which supervisory and review procedures are carried out will depend on various factors, including the level of experience (both general and as applied to the particular engagement), training and competence of the various personnel involved. Accordingly, this policy statement does not set out in detail how the procedures should be performed.

7. Some general guidelines for the review of audit files and working papers are listed below:

(...)

> (e) The reviewer should ensure that all significant exceptions identified by the staff member who has performed the work are disposed of satisfactorily or, in the case of significant exceptions, recorded on the interim or final MAP form.

8. It is the Firm's policy that there should be proper evidence on the audit file for all significant audit work performed, including its review and approval (see TPS-A-202, Audit Files and Working Papers). The Firm's documentation generally provides for the evidencing of review and approval procedures.[2641]

[2641] PW-1420, Tab 8 : TPS-A-216 "Engagement Control", December 22, 1986

[2359] The working papers of C&L contain countless errors[2642] that eloquently evidenced the failure to plan for supervision and review, and the failure to supervise and review.

[2360] The audit suffered from a virtual absence of supervision and review, as the content of C&L's audit working papers eloquently illustrate. For example, and to cite just a few:

- For each of the 1988, 1989 and 1990 years, the same loan information questionnaires and loan evaluation questionnaires used for the 1987 (and previous audits) continued to be used, despite the comments in response to the Quality Control review of the 1987 audit[2643] that consideration would be given to amending the forms or using the loan review sheets that were designed for bank audits.

- The loan information questionnaires and loan evaluation questionnaires on file were not fully completed and contained many errors, including the following:

    - The complete address of the borrower was not shown.

    - Despite that interest was not being paid in accordance with the loan covenants, and was being systematically capitalized, the question "*Are interest and repayment terms being met?*" was continually incorrectly answered "*Yes*".

    - The section of the loan evaluation questionnaire dealing with audited financial statements of borrowers was not completed. This failure was crucial in that C&L did not audit the ability of the borrowers to repay their loans and to satisfy their debt service obligations.

    - In many cases, the value of real estate security is shown as "*per Ron Smith*" and there is no further audit evidence to support these representations, while there should be to comply with the need to obtain SAAE.

    - The question "*Existing Liens on property*" was left blank in cases where there was significant prior ranking debt on the property.

- The "*Auditor's Overall Appraisal of Loan*" was generally left blank in 1988 and 1989. In 1990, while this was generally completed, in a number of instances, C&L staff expressed concerns over the underlying security, or lack thereof, and those concerns were never dealt with and resolved by more senior personnel.

[2642] PW-1053
[2643] PW- 1426

[2361] The design of the Castor audits was such that only one member of C&L had a global perspective of the company, a sound knowledge of the loan portfolio as a whole (Montreal and overseas)[2644]. Except for Wightman, the engagement partner, no one else at C&L really knew Castor's business.[2645]

[2362] C&L's internal materials on engagement control[2646] and on MAPs[2647], provide guidance as to the expectations for the work of the engagement partner who is responsible to «*review the overall quality and conduct of the audit*».

[2363] Nevertheless, Wightman did not:

- Know what level of experience the audit staff members had.[2648]
- Discuss with the managers and supervisors the level of experience required to work on the various audit sections.[2649]
- Review the audit working papers.[2650]
- Assess the quality of the work that had been done[2651].

[2364] Lack of review and lack of supervision had serious and negative impact on the quality of the audit work and it prevented the exercise of sound professional judgment whereas it is a cornerstone to comply with GAAS.

Unqualified opinion without sufficient appropriate audit evidence

[2365] General Standard 5100.02[2652] requires that the examination be performed by persons with adequate technical training and proficiency in auditing, and with due care.

[2366] Nevertheless, the audit staff assigned to work on the crucial and high risk elements of the 1988, 1989 and 1990 audits in Montreal lacked the experience, expertise and guidance to enable them to perform their tasks adequately. Junior members were assigned to work on the investment section of the audits, while it is one of the most difficult, if not the most crucial section of the audit work to be done.[2653]

[2644] Wightman, March 9, 2010, pp. 73–74.
[2645] Martin, December 18, 1995, p. 154.
[2646] PW-1420, Tab 8.
[2647] PW-1420, Tab 5.
[2648] Wightman, March 9, 2010, pp. 59-60, 79
[2649] Wightman, March 9, 2010, pp.60 and following
[2650] Wightman, March 9, 2010, pp.59, 79 and following
[2651] Wightman, March 9, 2010, pages 58 to 63, 79 and following
[2652] PW-1419-1A (1988); PW-1419-2A (1989); PW-1419-3A (1990)
[2653] Hunt, March 28, 1996, pp.35-36

Q.-Now, do you agree that the highest risk of material misstatement in the Castor audits was with respect to the carrying value of certain loans and investments?

A- Yes.

Q- And would you also agree that, for that reason, it would be necessary to design audit procedures to be satisfied that the carrying value of Castor's loans and investments was appropriate?

A- It would be necessary to select appropriate procedures, whether they were in the plan or not in the plan, before they went into do the field work. They certainly had to select appropriate procedures when they started to do the field work, when they... in the carrying of the field work, they had to carry out appropriate procedures.[2654]

[2367] Provided they were properly supervised, Selman sustained that juniors could work on the investment section of the Castor audit. Lack of supervision or inadequate supervision would constitute however a clear breach of GAAS, said Selman.

Q.-So you're saying that a green auditor should have had no difficulty in getting the audit of Maple Leaf Village correct, is that what you're suggesting?

A- I'm saying that a green auditor **properly supervised** ought to be able to have accomplished that, yes, it's how you learn, by making mistakes and having people correct them.

Q- **And what if the corrections are not made, is that a serious breach of GAAS?**

A- **It depends upon the consequences, but it's a breach of GAAS, yes.**

Q- Now, the person assigned to do the work, would it not have been required that that person have experience and knowledge in auditing real estate loans and more complex loans?

A- It's just impossible. You come back to what I said before, you have a pool of people. It would be nice to take a real estate expert, but there are very few real estate experts to our... you know, late students, or early CA's, it just doesn't work that way.

Q- So is it your testimony that it's acceptable under GAAS to take a student and put that student in charge of doing the audit of the investment section?

A- **If he's properly supervised**.

Q- So your answer is yes, it's acceptable to take a student?

[2654] Selman, June 1, 2009, p. 102

> A- **If he's properly supervised.**[2655]
>
> (our emphasis)

[2368] Supervision was inadequate, if there was supervision. Audit working papers were deficient and would not allow an external review. No supervisor intervened to correct the situation.

> Q.-Would you agree with me that there were a surprisingly large amount of audit working papers dealing with the audit of the investment section that were deficient?
>
> A- Well, there certainly were a number of working papers as I recall that were deficient (...)[2656]
>
> Q.-On your review of the working papers of the investment section in Montreal, did you note an inordinate amount of errors, big and small?
>
> A- No, I noted... what I did notice, as best as I can recall, was a number of gaps, sections not filled in, what I have seen many times, which is sort of insufficient documentation of working... on the working papers, insufficient information on the working papers to permit a external review at a distance in time.[2657]

[2369] By 1988, C&L was or should have been aware than at least a half of Castor's investment portfolio was secured by collateral other than real estate. The shift in the composition of the security for Castor's loans was critically important. Nevertheless, C&L conducted the Castor audits on the premise that the loans were secured by real estate.

[2370] The failure of C&L to understand the shift in the nature of Castor's lending operations led to a failure to recognize the increasing and alarming risks in the nature of its business and to egregious failures in both audit planning and execution.

[2371] In its audits of 1988, 1989 and 1990, C&L failed to obtain sufficient appropriate audit evidence ("**SAAE**") in respect of the collectability of the loans and the ability of Castor's borrowers and guarantors to satisfy their obligations. Moreover, in most cases where the securities of the loans were not mortgages on real estate, C&L obtained no SAAE.

[2372] C&L failed to seek or obtain reliable financial information regarding the various YH borrowers. C&L should have sought and obtained audited financial statements of YHDL and, at the least, insisted on obtaining unaudited statements of the other YH

[2655] Selman, June 1, 2009, pp. 137-138
[2656] Selman, June 1, 2009, p. 77
[2657] Selman, June 1, 2009, p. 140

borrowers, credit analyses prepared by Castor and other SAAE that would have enabled them to reach conclusions as to the borrowers' capacity to pay and as to the carrying value of the loans.

[2373] Although YHDL's audited financial statements were included in the 1987 AWPs, no concern was raised when no such financial statements were made available for review by C&L in 1988, 1989 and 1990.[2658]

[2374] Representations by Castor management that loans would have been "good" made no difference: still, C&L had to obtain SAAE, an obligation that Selman acknowledged as follows:

> Did you make or do you make any distinction between a circumstance where the auditor is told that a loan is good or okay and a situation where no such statement is made?
>
> I don't see a difference. The first one is simply a representation that needs to be corroborated by sufficient appropriate audit evidence. In the second situation, you have an assertion in the financial statements, the financial statements themselves, that the books and records are an assertion as to the carrying value and so consequently, that also has to be subjected to the acquisition of sufficient appropriate audit evidence to support the assertion. They're both assertions, one just happens to be verbal.
>
> Q- So, it's essentially the same situation.
>
> A- Essentially[2659].

[2375] C&L not only failed to obtain sufficient appropriate audit evidence; they also failed to document properly the work allegedly done.

Working papers

[2376] An auditor should document matters which, in his professional opinion, are important in providing evidence to support the content of his report[2660].

[2377] While it is neither necessary nor practical for the auditor to document in his working papers every observation, consideration or conclusion, the auditor needs to document matters which, in his professional opinion, are important in providing

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[2658] Quintal, December 1, 1995, p. 92.
[2659] Selman, May 26, 2009, p. 104
[2660] CICA handbook - section 5145.06 (italicised recommendation) - PW-1419-1A (1988), PW-1419-2A (1989) and PW-1419-3A (1990)

evidence to support the content of his report, including his representation as to compliance with generally accepted auditing standards[2661].

[2378] The preparation of good audit working papers is an essential part of audit work.

[2379] Good working papers provide a record of matters like the client's operational history, and the auditing problems encountered.

[2380] Working papers contribute to the quality of the examination by providing a good starting point for planning the audit of the subsequent period.

[2381] Since there is not necessarily staffing continuity on a particular audit engagement, working papers are an important means for new staff to gain an overall understanding of the client's organization and operations, and to anticipate problems encountered in previous years.

[2382] If work is done and not properly documented on the working papers, how can a reviewer carry out a proper review and assess the judgments made by the preparer?

[2383] Working papers reflect the quality of the audit work done.

[2384] Even though every accounting firm has a slightly different approach to file organization, approaches are not so unique that another auditor cannot readily understand them.

[2385] As Selman writes on page 265 of his report:

> There are many common ways in which things are done such that files are generally easily understood by auditors from other firms, and, once someone looks at a file, it isn't difficult to describe how that file is organized.[2662]

[2386] Other auditors, who may act for third parties, should be able to contend, from looking at the working papers, that a proper audit was carried out. Working papers must be prepared with this in mind.

[2387] Adequate documentation of planning, knowledge of the client's business, accounting procedures, the internal control systems, test procedures, results of test work, important discussions with client officials, decisions and conclusions reached, will enable the auditors to perform their audit adequately and appropriately.

[2388] In February 1980, the CICA issued an audit technique study titled "Good Working Papers", a revised edition of a study first published in 1970[2663]. What working papers

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[2661] CICA handbook - section 5145.01 - PW-1419-1A (1988), PW-1419-2A (1989) and PW-1419-3A (1990)
[2662] D-1295
[2663] PW-2910

should demonstrate in a year-end file is found in Chapter 3 on organization and content, at paragraph 41. Its item 4 reads as follows:

> The auditors' compliance with generally accepted auditing standards.
>
> The year-end working papers should record the nature, extent and timing of the auditing procedures carried out, and identify the audit evidence obtained to check the existence, occurrence, completeness, ownership, valuation, measurement and statement presentation of each material item. The working papers should include a conclusion as to whether each item has been fairly stated on a consistent basis. Evidence that there has been appropriate consideration of events occurring subsequent to the balance sheet, and conclusions on their disposition should also be included. The procedures used will usually conform with a standard approach predetermined by the auditors. One method of encouraging a uniform approach to audit engagements is to use preprinted audit programs adapted to meet the specific requirements of the audit of the client in question.[2664]

[2389] C&L and its staff knew or should have known all the above. C&L's internal material makes it obvious.

[2390] In TPS-A-202 titled "*Audit Files and Working Papers*", C&L writes:

> "AUDIT FILES AND WORKING PAPERS
>
> Introduction
>
> 1. This policy statement describes the audit files normally maintained on all audit engagements and the working papers completed in the course of the audit examination.
>
> 2. Audit files (with particular reference to items (a) and (b) in paragraph 12) and the working papers contained therein constitute a historical record and sole documentary evidence of the audit examination. They must be legible, neat and orderly. It is quite possible that today's audit files may be produced as evidence in a court of law in the future. Consequently, they should be prepared on the assumption that this may occur and that judgment of the Firm's performance will be influenced by them."[2665]

[2391] TPS-A-313 deals with substantive tests and appendix B, with substantive test working papers. C&L states in paragraph 5 of appendix B to TPS-A-313:

> 5. Working papers should be prepared in sufficient detail to allow the person reviewing them to:

[2664] PW-2910
[2665] PW-1420-1A

> (a) form an opinion whether the work was carried out so as to identify any exceptions in relation to the substantive test program step; and
>
> (b) assess judgments made by the auditor regarding matters such as valuations of assets and liabilities[2666].

[2392] In TPS-A-216, C&L sets out its review policy as follows, in paragraphs 4 and 5[2667]:

> "4. Thus, work done by each auditor should be supervised, reviewed and approved by a more senior person. The staff member in charge will normally review the work of staff under his control, the manager will review the audit as performed by the field staff, and the engagement partner will review the overall quality and conduct of the audit.
>
> A second partner will review specific aspects of the financial statements and audit (see TPS-A-209, Review of Audit Engagements by More than One Partner).
>
> 5. The review procedures can be divided into two separate functions, as follows:
>
> (a) at the time the work is performed, the reviewer (as defined in paragraph 4) should be available when needed to give advice, guidance or other help to the staff members. The reviewer's professional experience would often enable him to identify when such help is needed; and
>
> (b) after the work is completed, it should be reviewed for technical content. Taken as a whole, the review process should be such as to ensure that the work done accords with that required, that it is properly documented on working papers and signed for on audit programmes, that exceptions are dealt with appropriately, and that conclusions drawn from the work are valid."

[2393] Mari Beth Ford claims she was aware of the technical policy statements that existed for Coopers & Lybrand[2668].

Coopers working papers for Castor's audit (in general)

[2394] In his cross-examination, on June 11, 2009, Selman described the purpose of the working papers as follows:

> to provide information for two levels for the reviewer, the immediate reviewer, to understand what was done. That could have been done by a verbal discussion and not documented.

[2666] PW-1420, tab 13, paragraph 5
[2667] PW-1420, tab 8
[2668] Selman, December 10, 2009, pages 49 and 50

> The second purpose of the working papers is to identify the document on which reliance is placed with respect to a judgement called by the auditor on a matter, in this case the special agreement[2669].

[2395] Being asked if he would have expected Ford to document the evidence of a special agreement in the audit working papers, he said he would have[2670].

[2396] Being asked if he agreed that the failure to document the evidence of any special agreement, in the particular case that was discussed, was a serious breach of GAAS, he said:

> I don't consider it a serious breach of GAAS, but I do believe that it should have been documented[2671]

> So I would have expected it to be documented so that the special agreement could be identified at a later date, when ther e's a later review.
>
> Now, this special agreement has not turned up in the files, so not documenting it was a... was a breach of the expectations with respect to documentation, but as I told you when I was testifying in chief about the nature of working papers, a lack of perfection in the preparation of working papers is something that is quite common in the accounting profession, for better or worse, that's just the facts of the matter. So I wouldn't attach the word "serious" to it, it's just another case, in my view, of these working papers not containing all of the information that we would like them to have[2672].

[2397] Asked "*During the course of your review of the audit working papers of the overseas audit, did you note many instances where Ms. Ford failed to properly document her audit procedures in accordance with GAAS?*", Selman replied:

> I certainly noted a number of instances where there is less documentation than I would have expected. Ms. Ford was, got to say, brief in preparing her working papers, generally speaking, so her working papers are not very fulsome or informative[2673].

[2398] Selman qualified Mari Beth Ford's working paper as:

- Too brief. [2674]
- Certainly far from a perfect set of working papers.[2675]

[2669] Selman, June 11, 2009, pages 13-14
[2670] Selman, June 11, 2009, page 13 lines 15 to 17
[2671] Selman, June 11, 2009, page 13 lines 18 to 22
[2672] Selman, June 11, 2009, page 14 lines 7 to 20
[2673] Selman, June 11, 2009, page 14 lines 21 to 25 and page 15, lines 1 to 4
[2674] Selman, June 11, 2009, page 15 lines 5 to 7

- Without question, below the standard of working paper preparation that would be the norm.[2676]
- Without question, not very good working papers in total. [2677]
- Below the norm. [2678]
- Definitely not meeting the normal standard of working papers that he had seen in his experience.[2679]
- Deficient.[2680]

[2399] Levi commented on C&L's working papers:

> I was just going to say, after looking at nineteen eighty-eight (1988), eighty-nine ('89), it's about time they did a new sheet[2681].

[2400] Evidence revealed other situations where the file documentation was poor. [2682]

[2401] C&L had an internal inspection program, sometimes referred to as a peer review. This quality control procedure was used to assess the quality of the audit work carried out by the partners of the firm, and to assess compliance with GAAP and GAAS as well as compliance with firm policies and procedures[2683].

[2402] The specific objectives of the C&L's National Quality Control Program is set out in TPS-A-600 and includes not only compliance with the policies and practices of the firm, but also «*whether the report or communication issued in connection with the engagement is adequately supported in terms of the technical standards applied and the working papers.*»[2684]

[2403] Appendix B of TPS-A-600 sets out areas that the national review of audits should concentrate on[2685]. These relate directly to GAAS and GAAP and include planning, which is a GAAS standard[2686], comments on whether accounting practices are followed (including disclosure) and whether the estimates and other judgments made are

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[2675] Selman, June 11, 2009, page 15 lines 14 and 15
[2676] Selman, June 11, 2009, page 15 lines 20 and 21
[2677] Selman, June 11, 2009, page 15 line 25 and page 16, lines 1 and 2
[2678] Selman, June 11, 2009, page 16 line 4
[2679] Selman, June 11, 2009, page 16 lines 5 to 7
[2680] Selman, June 11, 2009, page 16 line 9
[2681] Levi, January 28, 2010, p. 205
[2682] Levi, February 2, 2010, pages 198 to 200
[2683] Vance, April 8, 2008, page 49 ; Froese, November 12, 2008, page 170
[2684] PW-1420, Tab 16, paragraph 2
[2685] PW-1420-1B, TPS-A-600, Appendix B, p. 3.
[2686] PW-1419-1A section 5100.02(i) (1988); PW-1419-2A section 5100.02(i) (1989); PW-1419-3A section 5100.02(i) (1990)

reasonable, otherwise known as the "stand-back" look, and adequacy of supervision and review, which is a GAAS standard[2687].

[2404] In a peer review report, issued in November 1988, prior to the 1988 audit, and concerning Castor's 1987 audit, the following was noted:

> No partner disposition was noted on any individual MAP.[2688]
>
> The MAPs appear rushed and unorganized generally especially in light of the analysis on file in the various sections. [2689]
>
> From the loan review sheets it is not clear that C&L has checked the information gathered to supporting documentation. The sheets also do not address the question of whether the client is up to date with their review of the debtors financial position or has complied with all loan covenants. Consideration should be given to revising the loan review sheets used in conjunction with those currently in use on bank audits[2690]

[2405] Despite this criticism of the audit work, and the content of the reply sent by Wightman concerning the loan review sheets[2691], C&L did not modify the loan evaluation and information questionnaires. As a matter of fact, they did not attempt to assess the way Castor approved or monitored loans either.

Year-end wrap-up meetings (in general)

[2406] As explained by Vance, «*...a year-end meeting is held with management to review those matters and in effect determine what other audit evidence is needed, what other work has to be done or get the audit evidence at that meeting.*"[2692]»

[2407] As Froese explained, an auditor needs to enter the year end meeting with an understanding of the work that was done[2693].

[2408] Vance explained that it is a normal practice for the engagement partner to bring a manager or the "in charge" into the meeting as well, so a meaningful discussion about the audit can ensue.

[2409] C&L's internal materials set out that «*when a partner delegates work to other personnel, he continues to be responsible for forming and expressing the opinion of the financial statements.* »

[2687] PW-1419-1A section 5100.02(i) and section 5150 (1988); PW-1419-2A section 5100.02(i) and section 5150 (1989); PW-1419-3A section 5100.02(i) and section 5150 (1990)
[2688] PW-1053-21, seq. p. 353 item 2b
[2689] PW-1053-21, seq. p. 353.item 2c
[2690] PW-1053-21, seq. p. 353 item 5h
[2691] PW-1053-21, seq. p.357 item 5h
[2692] Vance, April 9, 2008, p. 20.
[2693] Froese, November 25, 2008, p. 117.

[2410] The final resolution of audit issues at the level of the engagement partner is a significant audit procedure and represents the final exercise of professional judgment at the highest level.

[2411] Wightman did not take this audit step seriously, or seriously enough.

[2412] At trial, in 2010, Wightman tried to "improve" the testimony he gave on discovery, in 1995, with respect to the year-end meetings, suddenly being certain of things he was not sure of on discovery, and recalling new details that he did not previously recall despite extensive questioning on the very same issues much closer to the events in question. Here are few examples:

- At trial, he recalled the structure of the meetings, and the order in which things were discussed,[2694] whereas on discovery, he could not even remember how long the meetings generally were or when they took place[2695].

- At trial, he allegedly remembered going back to his office after the 1990 meeting to compose his notes[2696], while on discovery, he could not recall any details of what took place after the meeting[2697].

- At trial, he claimed to be certain that he had the MAPs with him at the meeting[2698]. Whereas, on discovery, he did not say he had them.[2699]

- At trial, Wightman testified that Smith was present during the entire wrap-up meeting of 1990,[2700] whereas 15 years earlier, during the examination on discovery, he was uncertain that Smith was present for the entire meeting[2701].

[2413] On cross-examination at trial, in 2010, he admitted that he did not have any notes that could have refreshed his memory with respect to any of the meetings, other than the 1990 meeting notes, which he had during discovery as well.

[2414] Viewed in light of these recollections and numerous inconsistencies between new and old memories, serious questions arise as to the credibility and reliability of Wightman's entire testimony.

[2694] Wightman, February 8, 2010, pp. 178-182.
[2695] Wightman, September 29, 1995, pp. 54-59, 66-67.
[2696] Wightman, February 10, 2010, pp. 89-90.
[2697] Wightman, October 10, 1995, p. 54
[2698] Wightman, February 10, 2010, p. 57-58.
[2699] Wightman, October 19, 1995, pp. 66-67.
[2700] Wightman, February 11, 2010, pp. 93–95
[2701] Wightman, September 29, 1995, p. 208.

Year-end wrap-up meetings for the 1988, 1989 and 1990 audits (in general)

[2415] Each year, at the end of the field work, prior to signing the Auditors' Report for the annual consolidated financial statements, Wightman met with Stolzenberg for a wrap-up meeting.

[2416] Wightman considered that the audit work was finalized prior to these meetings and never requested further audit work before releasing the audited financial statements because of issues that arose or information provided to him at wrap-up meeting[2702].

[2417] He testified that the team in Europe held its own wrap-up meeting with Stolzenberg and that, although he was not aware of the details of those discussions, he saw no need to discuss the overseas loans again at his own wrap-up meeting with Stolzenberg[2703].

[2418] Wightman had a cavalier approach with respect to this important audit step.

[2419] Wightman's shortcomings in this respect resulted in many avoidable audit errors.

[2420] He did not study the AWPs in detail[2704], or ensure that a manager or the "in charge", who possessed the required knowledge of the audit, was always with him at the meetings.

- He was only accompanied once by the Montreal audit manager for the three audits at issue[2705].
- Although he testified that the reason why the manager in 1990, Quintal, did not attend the wrap-up meeting was because he was unavailable, this testimony is not reliable- Quintal did not recall ever being asked to attend the meeting[2706]. In any event, in Quintal's absence, Wightman did not request Hunt, the "in charge", to attend in his place, even though he was available and, in fact, waiting on Castor's premises should he have been needed[2707]. Hunt acknowledged the rather startling fact that he never met once with Wightman throughout the whole audit and prior to being sent back to Halifax[2708].

[2702] Wightman, February 11, 2010, pp.181 and following; Wightman, February 25, 2010, pp.75 and following
[2703] Wightman, March 9, 2010, pp. 75–76.
[2704] Wightman, February, 25, 2010, pp. 39-40
[2705] Wightman, September 29, 1995, pp. 47-49.
[2706] Wightman, February 8, 2010, pp. 182-183; Quintal, November 29, 1995, p. 189.
[2707] Hunt, March 28, 1996, pp. 68-69.
[2708] Hunt, March 28, 1996, p. 20.

[2421] Wightman inappropriately and negligently abdicated his responsibilities with respect to the resolution of issues pertaining to Castor's overseas portfolio.

[2422] Wightman's decision to exclude a consideration of the overseas portfolio as part of the wrap-up meetings he had with Stolzenberg essentially doomed the audits to fail as there was no analysis by C&L of the audit issues on a consolidated basis.

[2423] Wightman assumed that material matters had been cleared without any personal verification of the status of the issues and without any documentary evidence in the AWPs to support that conclusion.

[2424] C&L made no attempt to identify Castor's overall exposure on the YH loans, although information recorded in C&L's AWPs indicated that at least a half of Castor's loan portfolio was connected to the YH group.

[2425] Wightman testified that he did not consider it appropriate to look at the entire YH connection and have a careful analysis performed of the collectability of those loans and the ability of those loans to service debt «because it was all gone through by the staff before»[2709].

[2426] As Wightman was the only member of the C&L audit team that had knowledge of the global portfolio, the fact that he failed to recognize his responsibility to address Castor's global exposure to the YH group at the year-end meetings with Stolzenberg, is inexcusable.

[2427] Wightman was made aware, at least as early the 1986 audit, that there were loan exposures that needed to be considered on a global basis: for example, with respect to the TSH. Despite the information brought forward to him in the Inter-Office MAPs, Wightman never integrated this information with his knowledge of the Montreal loan portfolio. The exposures on projects such as the TSH, the CSH and MLV were never really addressed on a global basis with Stolzenberg. This is namely evidenced by Wightman's attempt to aggregate related loans in the notes he allegedly made during or shortly after to the wrap-up meeting for the 1990 audit (wrap-up meeting held a week after the date of the Inter-Office MAPs for 1990).[2710]

[2428] The final resolution of audit issues at the level of the engagement partner is a very significant audit procedure[2711] and represents the final exercise of professional judgment, at the highest level. The only detailed summary notes of the wrap-up meetings for the relevant period (1988, 1989 and 1990) that can be found in the AWPs are notes relating to the 1990 audit. For 1988 and 1989 Wightman sustained he did not

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[2709] Wightman, March 10, 2010, pp. 30-31.
[2710] PW-1053-12, seq. pp. 76-93; PW-1053-71, seq. pp. 45-49
[2711] Selman, June 2, 2009, pp. 14-15.

consider the notes useful, and he discarded them. [2712] This explanation is surprising to say the least.

1990 wrap-up meeting

[2429] Smith testified that he attended a portion of the wrap-up meeting for the 1990 audit with Stolzenberg and Wightman. This was his only meeting with Wightman in the context of any audit. In fact, over a period of 11 years, Smith's meetings were always held with junior auditors. [2713]

[2430] When Smith walked into the meeting on February 15, 1991, Wightman was aware that «*there was a potential problem of approximately two hundred and seventy-five (275) million dollars relating to various loans in the portfolio, notably the Maple Leaf Village loans, the hotel loans for Topven on the Skyline Toronto and Calgary, and relating to the forty (40) million dollars of loans that were just booked*»[2714].

[2431] Prior to this wrap-up meeting with Stolzenberg, Wightman knew that the junior staff had identified $133 million of unsecured and doubtful loans in the Montreal portfolio alone, and that $40 million of that amount had been identified as representing the aggregate of nine loans made in the last few weeks of the year.[2715]

- At trial, Wightman denied having seen this schedule stating that he rather relied on the manager's summation of the information.[2716] However, on discovery, he acknowledged having seen the schedule by justifying why he did not view the accounts as doubtful despite this listing by the auditors.[2717] Contrary to his assertion at trial, he also admitted that he did not discuss with the audit manager why he wrote "MAP" on the working paper, E-65C that listed these $133 million in unsecured loans.[2718]

- The Court concludes that Wightman had seen the schedule and was fully aware of the situation.

[2432] A number of the projects were discussed, and then Smith was dismissed from the meeting prior to any discussion of the $40 million of new unsecured loans[2719]. At that point, Smith was certain that there was a major problem with the audit.

> Wightman indicated to me that he wanted to have further discussions with Mr. Stolzenberg alone and that I was no longer required, and as a result, I was

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[2712] Wightman, February 11, 2010, pp. 141–142.
[2713] R. Smith, May 14, 2008, pp. 83–84.
[2714] Ron Smith, May 14, 2008, pp. 103-105
[2715] PW-1053-15, seq. pp. 128–131.
[2716] Wightman, February 26, 2010, p. 68.
[2717] Wightman, September 29, 1995, pp. 77-78, 84-85.
[2718] Wightman, September 29, 1995, pp. 198-199.
[2719] Ron Smith, May 14, 2008, p.103-106

> dismissed from the meeting and that's the end of the meeting, I left the meeting and **I thought that we had a major problem with our portfolio** in leaving that meeting and I went down to meet with Dragonas and Goulakos in the Wost offices within our offices, and I informed them that **I thought that we weren't going to get our audit this year, that there were major problems indicated, and that I was prepared to work all week-end,** if there were more questions to be decided, or that the final restructuring was finally going to take place within York-Hannover and Castor. I had been pushing Mr. Stolzenberg for, you know, restructuring of York-Hannover a number of years, and while attempts had been made, it was moving very slowly at that point, and I thought that well, now, now **the auditors are going to push that on us** and it's going to be a major situation where we do restructure from this point onwards.[2720] (our emphasis)

[2433] Later that evening, at a dinner he attended with his wife and where Wightman and Stolzenberg were also present, Smith was surprised to learn that the issues had been settled and that the audit was complete[2721].

> After about fifteen (15) minutes of sitting down, I got up and walked to the washroom and in walks Mr. Wightman. And **Mr. Wightman indicated**... I asked Mr. Wightman what had transpired and he just indicated to me **that the audit process was finished, everything had been settled and the audit was over and completed.** That somewhat surprised me at that point in time, after having left the meeting, I certainly felt that we had major issues that were going to have to be discussed.[2722] (our emphasis)

> I went back to my table with my wife and within another fifteen (15) minutes, Mr. **Stolzenberg walked in**, and they were round tables, so his back was with me, (inaudible), and I turned around as soon as **he sat down and asked** "What's going on here, **did we go through the audit?",** and **he indicated "Yes, everything has been settled, the audit process is over,** it has been completed, **the statements will be published shortly, let's get over to party".**[2723] (our emphasis)

[2434] The Courts finds Ron Smith's testimony relating to the 1990 wrap-up meeting credible and reliable. Wightman's testimony about same is self-serving and not reliable.

Conclusion

[2435] At the stage of the audit where the most significant exercise of professional judgment was required, no such judgment was exercised.

[2720] Ron Smith, May 14, 2008, pp. 105-106
[2721] Ron Smith, May 14, 2008, pp. 105-108
[2722] Ron Smith, May 14, 2008, p. 107
[2723] Ron Smith, May 14, 2008, p. 107

Steps not taken by C&L during their audits

[2436] C&L failed to perform their professional services in accordance with the standards of the day, in accordance with GAAS. Such failures were blatant, pervasive and inexcusable.

[2437] C&L audit planning failed to address, among other matters, the concentration of borrowers and projects, and the interconnected loans made in Europe and in Canada.

[2438] C&L ignored the changing nature of their client's business and failed to implement an audit plan that was appropriate in the circumstances. In effect, C&L failed to perform an audit pertaining to a short-term or a long-term lender,[2724] and performed no meaningful audit in respect of Castor's ever increasing non-performing loan portfolio.

[2439] C&L had the obligation to assess the credit monitoring process and to verify that Castor's borrowers were complying with their loan covenants. During all the relevant years, 1988 to 1990, C&L failed to perform such elementary auditing procedures.[2725] Therefore, C&L completely failed to consider the implications for Castor's borrowers to be systematically in default.

[2440] During the three relevant years, C&L failed to obtain sufficient appropriate audit evidence in respect of the collectability of the loans and of the ability of Castor's borrowers and guarantors to satisfy their obligations to Castor. Furthermore, in most cases, C&L obtained no sufficient appropriate audit evidence at all in cases where loans were not secured by mortgages on real estate.

[2441] C&L failed to consider the purpose of the loans[2726] and whether funds were being advanced to borrowers to create value. Rosen described the following as the most basic audit question: «*What do you intend to do with the money should I loan it to you*?«[2727] C&L never asked themselves that question, nor did they ask Castor, for that matter, nor did they ask any other questions to find out why Castor was continuing to transact with its largest borrower when it could not pay interest or fees and did not have tangible security to offer to collateralize the corporate loans.

[2442] C&L failed to seek or obtain reliable financial information regarding his various borrowers that would have enabled them to reach a conclusion as to the borrowers' capacity to pay and as the carrying value of the loans.[2728]

[2724] PW-3034, pp. 9-20
[2725] PW-2908, Vol. 1, p. 4-B-13; Vance, March 13, 2008, pp. 179–186; Vance, March 6, 2008, pp. 79-84
[2726] PW-3033, Vol. 1, p. 44
[2727] Rosen, February 3, 2009, p. 49.
[2728] D-1295, p. 363; Selman, June 4, 2009, p. 230; June 10, 2009, pp. 65-72

[2443] Although C&L understood that Castor's practice of capitalization of interest was a "hot topic" because of the possibility that borrowers could not meet their obligations, they did not adjust their audit of the loans to obtain information as to why the borrowers were failing to meet their loan covenants (as had been recommended by Higgins in the peer review).

[2444] C&L assigned the most junior members of the audit team to audit the loans, and information that appeared in the AWPs of prior years were mechanically, and often erroneously, brought forward to later audit years without any analysis or critical review. In addition to the overwhelming GAAS errors on the valuation of the loans, the way the AWPs were documented was, in and of itself, a breach of GAAS, which should have been apparent to the reviewers.

[2445] The audits appear to have been limited to a mechanical review of commitment letters and promissory notes, and to the filling out of forms without thought or analysis. The superficial review conducted by C&L, as described by Smith,[2729] is corroborated by the testimony of the junior auditors who worked on the investment sections.[2730] C&L never questioned why one-year loans that were non-performing were routinely renewed, from year to year, and not repaid by the borrowers.

[2446] Superficiality[2731] and brevity characterized the audits.

[2447] The auditors failed to consider the numerous red flags that were readily apparent regarding the portfolio and failed to ask for information that was available to them. [2732]

[2448] C&L's audit approach never changed, even when negative information was provided. No further questions were put to Castor management.[2733]

[2449] The auditors placed inappropriate and undue reliance upon representations of management, notwithstanding guidance of section 5300 of the Handbook on "*audit evidence*", and namely guidance of sections 5300.08, 5300.19, 5300.20, which stipulate:

> **08.** Sufficient appropriate evidence should be obtained to enable the auditor to evaluate whether management's accounting estimates are reasonable within the context of the financial statements as a whole.
>
> When the auditor is unable to obtain sufficient appropriate evidence to provide reasonable assurance that management's accounting estimates are reasonable

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[2729] Ron Smith, September 5, 2008, p. 47
[2730] 1988: Séguin, December 12, 1995, pp. 283-295, October 25, 1996, pp. 60-68.; 1989: Belliveau, April 1, 1996, pp. 69-96, 109; 1990: Quesnel, November 23, 1995, pp. 176-188, November 24, 1995, pp. 102-108
[2731] Ron Smith, May 14, 2008, pp. 88-102, 230-231; September 5, 2008, p. 47
[2732] R. Smith, September 17, 2008, p. 162
[2733] R. Smith, September 16, 2008, pp. 213-218

> within the context of the financial statements as a whole or has obtained evidence that refutes management's estimates, the auditor would discuss the findings with management and consider the effect on his or her opinion.

> **20.** Generally, evidence developed by the auditor is more reliable than evidence obtained from the enterprise or third parties, documentary evidence is more reliable than oral evidence and external evidence is more reliable than internal evidence. The auditor may gain increased assurance when audit evidence obtained from different sources or of a different nature is consistent. In these circumstances, he may obtain a cumulative degree of assurance higher than that which he attaches to the individual items of evidence by themselves. Conversely, **when audit evidence obtained from one source is inconsistent with that obtained from another**, the reliability of **each remains in doubt until further procedures** have been performed to **resolve the inconsistency**.

> **26** Enquiry consists of seeking appropriate information of knowledgeable persons within or outside the enterprise. Enquiries may range from formal written enquiries addressed to third parties to informal oral enquiries to persons within the enterprise. (...) **A response from a person within the enterprise does not usually constitute sufficient appropriate audit evidence in itself** but requires corroboration. Such corroboration may include making further enquiries from other appropriate sources within the enterprise. Consistent responses from different sources provide an increased degree of assurance. (...)(our emphasis)

[2450] As Anderson writes:

> Enquiry of management and employees is applicable to almost every financial statement figure to be verified even though **oral representations from persons within the organization** being audited must be treated as **the least reliable form of audit evidence. All representations** of material consequence **must therefore be corroborated** by other evidence.[2734] (our emphasis)

[2451] Ford failed to document either the levels of materiality, or the risk factors used in determining the nature, extent and timing of the audit procedures.[2735]

[2452] C&L failed to bring forward information or representation made to them.

[2453] For each of the three relevant years, C&L failed to detect several material transactions that improved dramatically and artificially Castor's balance sheet and income statement.

[2734] PW-2908, vol. 1, chapter 6, page 6-34

[2735] Ford, December 8, 2009, p. 127. See also PW-1419-2A, Section 5145.05

[2454] At every phase of the audit work, C&L failed to exercise professional judgment or they exercise it improperly, without thought or critical analysis.

[2455] In general terms, in the 1988, 1989 and 1990 audits, breaches of GAAS originated from or resulted in:

- The failure to aggregate loans in Montreal and Europe and in relation to each project.
- The failure to assess the financial ability of borrowers (and guarantors) to repay their loans.
- The failure to obtain financial statements for each borrower and guarantor (or for entities whose assets served as loan collateral).
- The failure to review and assess the reasonableness of appraisal assumptions and to require up to date appraisal reports.
- The failure to select the highest risk loans related to a project to be audited.
- The failure to analyze properly what security was available to Castor for each loan and what liabilities of a project (or liabilities of a borrower) ranked in priority to Castor's security.
- The failure to obtain sufficient appropriate audit evidence for the carrying value of unsecured loans and loans secured by personal guarantees, corporate guarantees, pledges of shares, assignments of receivables and other non-real estate assets.
- The failure to review correspondence files in relation to loans and to assess Castor's credit granting and monitoring procedures.
- The failure to determine whether interest and fees were being paid in cash by each borrower or being capitalized in some manner.
- The failure to identify and probe unplanned capitalization of interest and breaches of covenants by borrowers.
- The failure to question large receipts of cash payments at year-end (as opposed to small sums received during the first eleven months) and the failure to generally perform window dressing procedures.
- The failure to carry forward important information gathered in prior years.
- The failure to consider the ever growing portion of loans not directly secured by real estate.

- The failure to properly complete loan questionnaires.
- The mechanical use of audit working papers carried forward from previous years without tracing information to supporting documentation, and other errors which evidence a lack of understanding, a lack of care and a robot-like propensity to copy information from the previous audit working papers, sometimes erroneous and out of date.
    - For example, an incorrect loan description, such as a loan being a 2nd mortgage, was repeated year after year even though such description was wrong and inconsistent with the audit confirmation letters received by C&L.
- The failure to take account of the publicized loan to value ratio of Castor, which was 75%-80%, especially after C&L noted its importance in the audit of the Les Terrasses loans for 1986.
- The acceptance of changes to notes 2, 3 and 4 without sufficient appropriate audit evidence after having carried out their own audit procedures.
- The use of a statement of changes in net invested assets in contrast to a statement of changes in financial position contrary to the specific requirements of GAAP.
- The failure to perform audit procedures in connection with undisclosed related party transactions.
- The failure to exercise professional judgment with an objective state of mind (in connection with the carrying value of loans, loan loss provisions, related party transactions, economic dependence, maturities of loans receivable and payable, disclosure of a proper statement of changes in financial position, disclosure of restricted cash).
- The failure to appropriately document work performed.
- The failure to control the confirmation process.
- The failure to confirm the $100 million debentures in Montreal.
- The failure to identify the concentration of risk and economic dependence.
- The failure to identify and disclose restricted cash.
- The failure to implement recommendations made by their own quality control department.

- The failure to comply with their own technical materials.
- The failure of the engagement partner, during the year end wrap-up meeting, to obtain adequate information, to analyze properly the one obtained, to ask additional questions and to test such information.
- The failure of the engagement partner, further to the year-end wrap-up meeting, to request that further audit work be performed.

[2456] C&L's audits of the carrying values of the loans appear to have been nothing more than summarily (but not in all cases) asking Smith if the loans were "good" or "ok". Smith testified that because Castor had not taken a loan loss provision on the loans, it was the company's position that the loans were good and he merely reflected such position. Selman acknowledged that asking management if a loan is "good" adds nothing to the audit process if no additional requests for information are made by the auditor.

[2457] In practical terms and in regard to specific loans or projects that were reviewed or should have been reviewed during the 1988, the 1989 or the 1990 audit, not complying with GAAS entailed the following effects or consequences.

1988

MLV

[2458] C&L failed to aggregate all CHL and CHIF loans secured by the assets of the MLV project. The inter-office memorandum from the overseas audit staff stated that this aggregation had to be performed in Montreal.[2736] Even though a tick mark suggests that this item was "cleared", the Court finds that it was not.

- The loan analysis performed[2737] does not aggregate all the loans.
- Examinations of audit staff members reveal that the work was not performed.[2738]

[2459] In connection with the Castor Montreal loans, C&L failed to include Loan 1105 to MLVII in the amount of $3.1 million, Loan 1048 to YHLP in the amount of $14 million and Loan 1125 to KVWIL in the amount of $7.2 million in their analysis.

[2460] The draft (7th draft) financial statements of MLVII, still not finalized 16 months after the balance sheet date, reflected serious financial difficulties in addition to a "future operations" note. These financial difficulties were a major and obvious "red flag" to any

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[2736] PW-1053-22, sequential page 184.
[2737] PW-1053-23 sequential page 153 (E72).
[2738] For example, Séguin, December 12, 1995, pp. 128-135.

competent auditor.[2739] The auditors ought to have assessed how a project in such a difficulty, and a borrower so reliant on financial support could possibly service its debt to Castor.

[2461] The audit working papers ("**AWPs**") themselves reveal errors, which illustrate the failure to trace information to supporting documentation or a lack of understanding. Some of those errors are convincing evidence of a lack of analysis and of a mechanical, robot-like, propensity to copy or bring forward information from previous years' AWPs without any thought.[2740]

[2462] The use of appraisals was superficial and inadequate. Aside from copying the date of the appraisal, the name of the appraiser and the amount, no audit work was performed in relation to the assumptions which supported the out-of-date appraisal used for the 1988 audit:[2741] This Mullins appraisal was issued in 1983 and the financial position of MLV had deteriorated substantially since that date. The audit staff did not perform any procedures on the substance of the appraisal; they did not check if the underlying assumptions still had any validity.[2742] They should have.[2743]

[2463] Section 5360 of the Handbook "Using the work of a specialist" contains guidance to auditors who rely on the work of a specialist (an appraiser, for example) as audit evidence when conducting an examination in accordance to GAAS. Paragraphs 5360.09. 5360.12 and 5360.14 state:[2744]

> **09.** When the auditor plans to use the work of a specialist as audit evidence, he should have or obtain reasonable **assurance concerning the specialist's reputation for competence.**
>
> **12.** The appropriateness and reasonableness of the assumptions and methods used by the specialist are the responsibility of the specialist. Ordinarily, the auditor may accept the specialist's judgment and work in this regard unless the report of the specialist, the auditor's communication with the specialist, or the **auditor's knowledge of the client's business lead him to believe that the specialist's assumptions or methods are unreasonable in the circumstances**. If the assumptions or methods used by the specialist appear to be inconsistent with those used in the prior period, the auditor would enquire into the reason for the apparent inconsistency.

[2739] PW-2908, Vol. 2, A-7 and A-8.
[2740] PW-2908, Vol. 2, pp. A-15 to A-20.
[2741] PW-1053-23, seq. p. 154; R Smith, May 16, 2008, pp. 154-155; (PW-493); Vance, April 9, 2008, pp. 114-115.
[2742] Séguin, December 12, 1995, pp. 170-176.
[2743] Vance, PW-2908, vol. 1, pp.6-2 to 6-21; Froese, PW-2941, vol. 1, pp.163 and following
[2744] PW-1419-1A (1988); PW-1419-2A (1989); PW-1419-3A (1990)

> **14.** When the auditor uses the work of a specialist, he should:
>
> (a) **Satisfy himself that**, based on **his knowledge of the business** and his knowledge of the specialist's methods, assumptions and source data, the findings appear to be reasonable; and
>
> (b) Obtain reasonable assurance that:
>
> > (i) Accounting data provided by the client to the specialist is appropriate; and
> >
> > (ii) The specialist's findings support the related assertions in the financial statements. (**our emphasis**)

[2464] In one of its 1986 publications, the AICPA provided the following guidance:

> The auditor ordinarily relies on the work of the appraiser unless the auditor's procedures lead to the belief that the appraiser's methods, assumptions, or findings are unreasonable.
>
> The auditor should test the accounting data provided by the client to the appraiser. In addition, the auditor may sometimes need to further enquire or to perform additional procedures, such as independently verifying significant data contained in the appraisal report, examining documents and other information used by the appraiser, speaking with the appraiser, and correlating the appraiser's findings to other available audit evidence, or engaging another appraiser to evaluate the reasonableness of the valuation data.[2745]

[2465] In summary, before concluding that an appraisal could be used as appropriate audit evidence, C&L had to :

- Determine that the appraiser's reputation and qualification were acceptable and to do it, they had to know who the appraiser was.
- Be satisfied that the appraiser had set forth the rationale inherent in his value estimates,
- Understand the appraiser's approach and be satisfied that such an approach was reasonable in the circumstances.
- Determine the reasonableness of the appraiser's conclusions in light of current information regarding physical characteristics or actual operations of the property.

[2745] PW-2953

[2466] All of the above is consistent with C&L's own technical guidance. In its December 31, 1982 publication relating to the valuation of real estate holdings, C&L wrote:

> If an appraisal is available, we should not accept it as a basis for establishing NRV without considering the following:
>
> i) the qualifications and apparent objectivity of the appraiser;
>
> ii) the purpose of the appraisal;
>
> iii) the apparent appropriateness of the methods and assumptions used; and
>
> iv) the apparent validity of the conclusions reached.[2746]

[2467] If they had done the appropriate work in relation to the MLV appraisals they had on hand, C&L would have found the following.

- The appraisals assumed that substantial renovations would be made to the MLV project.
- In order to maintain the Sheraton brand name, renovations to the MLV hotels were greatly needed.
- The discounted cash flow forecast used in the Mullins appraisal, and the Hughes appraisal were not applicable since the cash flow projections assumed that substantial renovations would be made, and they were not.

[2468] From the testimony of the audit staff, it appears that C&L never analyzed the assumptions contained in those appraisal reports.[2747]

[2469] Without the financial support of Castor, the MLV project was not generating sufficient operating income to even meet its first mortgage payments. In 1988, the project generated $4 million of net income before debt, but had annual interest obligations alone of $20.4 million. Real estate taxes were paid one day before the City of Niagara would have sold the property for taxes.[2748] No money was available from YH to support the MLV project.[2749]

[2470] In evaluating the YHLP loan receivable of $10 million from MLVII, the audit staff relied upon an out of date valuation of the shares of MLVII apparently carried out by

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[2746] PW-1420, AM-50

[2747] Séguin, December 12, 1995, pp. 173-176; Belliveau, April 2, 1996, pp. 276-278; Quesnel, November 24, 1995, pp. 130-134; Mitchell, April 25, 1996, pp. 115-118; April 24, 1996, pp. 181-185; Wightman, September 15, 1995, pp. 191-196 – Wightman didn't expect the audit staff to read the entire appraisal.

[2748] Prychidny, October 15, 2008, pp. 50-52; PW-1053-23, seq. p. 163 (note 3a).

[2749] Prychidny, October 15, 2008, p. 111; October 14, 2008, pp. 49-52, 72-75, 83-85. 88-90.

Thorne Riddell in 1984. The receivable secured YHLP loan 1048 in the amount of $14.1 million. There is no evidence that the audit staff even saw this valuation during the 1988 audit work. Furthermore, the receivable in the amount of $10 million does not appear on the draft audited financial statements of MLVII, which were contained in the AWPs.[2750]

[2471] By way of example, in evaluating the collectability of the loan made to KVWIL in the amount of $7.2 million, Séguin did not obtain financial statements or any other financial information on the borrower or on the guarantor, Wersebe. The only information to support his evaluation of the carrying value of the loan was the purported statement made by Smith that this loan was good. Selman opined it was not enough.

[2472] Save for the 7th draft of the unaudited financial statements of MLVII, the auditors did not obtain any financial statements of borrowers. According to Séguin, it was not necessary to obtain financial statements or other financial information concerning a borrower.[2751]

[2473] In fact, there was no basis to support the decision of the auditors to accept the carrying value of unsecured loans or loans secured by pledges of shares, accounts receivable or other financial assets, which could only be evaluated through the provision of financial information.

[2474] The failure to obtain financial statements of borrowers and of entities whose shares were pledged as collateral was a clear breach of GAAS.[2752] Moreover, the failure to adequately document the AWPs is itself a breach of GAAS.[2753]

[2475] In relation to those MLV loans which were not secured directly upon real estate, C&L failed to obtain SAAE. Selman admitted in similar circumstances that the documentation would not indicate that C&L «*completed GAAS*».[2754]

[2476] All the above was aggravated by the failure of Wightman to follow up on information and representations of management made to him in prior years and to question management properly and to follow up on information provided by management during the year-end wrap-up meeting.

[2750] PW-1053-23, seq. pp. 155-166. See PW-2908, Vol. 2, A-10.
[2751] Séguin, December 11, 1995, pp. 86-88.
[2752] Selman, May 26, 2009, pp. 77-78, 97-98, 100-102.
[2753] Selman, June 1, 2009, pp. 81-82; PW-2908, Vol.1, p. 5-30.
[2754] Selman, May 26, 2009, p. 92; PW-2908, Vol. 1, p. 5-30.

MEC

[2477] C&L failed to take into account, and to aggregate, various loans which were associated with the MEC project, such as the loan to 612044.[2755]

[2478] C&L failed to consider why interest was being capitalized on some MEC loans where no such capitalization had been foreseen in the loan agreements.

[2479] C&L failed to assess the financial ability of the various borrowers to pay, especially in respect of the high risk equity loans. Even though such information was essential to determine the collectability of the equity loans, C&L did not request nor saw any financial statements of YHDL, 97872 or 612044.

[2480] In 1988, the "Les Terrasses" project was refinanced and became the "MEC" project. C&L staff did not appear to have understood that the refinancing of the loans in connection with Les Terrasses was linked to the loans in connection with MEC. This lack of understanding is evidenced in the AWPs for loan 1042,[2756] and was repeated in 1989 and 1990 by the process of blindly bringing forward the AWPs from previous years. As a result, C&L used erroneous loan figures for prior ranking loans, since the loans prior to the refinancing no longer existed.

[2481] C&L did not ask themselves why Castor financed the equity contributions of the owners of the project.

[2482] C&L failed to consider whether the assumptions contained in the MEC appraisal that they relied upon[2757] were realistic.

[2483] C&L failed to properly audit for related parties. C&L failed to ask even the most basic of questions to ascertain who the owners of 612044 and 97872 were. The closing binders demonstrated that Stolzenberg was the incorporator and a director of 97872[2758] and numerous newspaper articles disclosed his ownership interest.[2759] Reading Hunt's testimony, the supervisor of the CHL 1990 audit that worked on the related party section, enlightens: lack of knowledge of the client's business, lack of planning and lack of supervision are clearly part of the reasons for such a failure.[2760]

[2484] Finally, all the above was aggravated by Wightman's own failure to plan and to supervise the work done by his teams, and by his failure to review their work and their audit working papers.

[2755] Wightman, October 6, 1995, pp. 79-88.
[2756] PW-1053-23, seq. pp. 213-214.
[2757] PW-1108A
[2758] PW-1102A-6; PW-2908, Vol. 1, p. 4-E-32.
[2759] PW-2925, PW-2926.
[2760] Hunt, March 28, 1996, pp. 127-132.

TSH

[2485] The project had been financed by Castor since the early 80s. C&L knew that it was refinanced a number of times, including in 1988, but C&L failed to investigate if this was an indicator that the project was in trouble.[2761]

[2486] Because the refinancing increased Castor's exposure from $75 million, at year end 1987, to more than $110 million, in 1988, C&L should have, yet did not, consider the increased risk.[2762]

> And again, the point I would just make is the knowledge, is that the... it's getting very tight, with respect to the loan and the collateral, especially when estimates are given and used in putting in the value, and certainly an auditor planning for nineteen eighty-eight (1988), this is one loan that cries out for inspection in nineteen eighty-eight (1988).[2763]

[2487] Prior to 1988, C&L knew about the relationship between Lambert and Topven: this information should have been brought forward each year, but it was not. Smith confirmed the relationship when he explained the major refinancing to the junior auditor for the 1988 audit, but the latter failed to take account of this information.[2764] There is a reference to a refinancing in the AWPs but without any detailed information.[2765]

[2488] As a result of a lack of planning, C&L failed to aggregate the TSH-related loans, which it should have. As a consequence, C&L did not realize that Castor's exposure on the project at year end 1988 (and also at year-ends 1989 and 1990) was well in excess of value estimated by Gillis.[2766] C&L relied on Management and ignored the information in their own AWPs. Wightman admitted that the information was in the AWPs and was not concealed from C&L by Management.[2767]

[2489] C&L knew that Castor marketed itself by asserting to potential and actual investors and lenders that their policy was not to exceed 75% to 80% of the estimated market value.

[2490] C&L should have realized that Castor was lending in excess of 80% of the estimated market value, and often at greater than 100% of such value and considered the negative implications.[2768]

[2761] PW-2941, Vol. 1, p. 151–152; Vol. 2, p. 88.
[2762] Vance, April 8, 2008, pp. 41-45, 95–96.
[2763] Vance, April 8, 2008, p. 95
[2764] Ron Smith, September 5, 2008, pp. 34-35.
[2765] PW-1053-23, seq. p. 168
[2766] PW-423
[2767] Wightman, September 18, 1995, pp. 103–107.
[2768] Vance, April 21, 2008, pp. 191–194, referring to Wightman's testimony on discovery, October 10, 1995, pp. 169, 174, 176; September 21, 1995,62–77, 84-85; R. Smith, October 2, 2008, pp. 7-14; PW-1053-38, seq. p. 82 (for 1988).

[2491] C&L only selected the first and second mortgage loans to Topven (1988) for detailed review for the 1988 audit and omitted the unsecured grid note loan and the Lambert loans. These were errors in the performance of auditing that should have been identified by the reviewer, had a proper review been done.[2769]

[2492] C&L should have identified that the increase in the loan balances each year was due to the capitalization of interest.[2770]

[2493] The loan documents reviewed by C&L called for the monthly payment of interest in cash.[2771] The mortgage and loan ledger cards reviewed by C&L, as well as the accounting records, disclosed that the TSH loans were all being capitalized, including the 2nd mortgage loan from CHIF.[2772]

[2494] Similarly, the systems' testing performed by C&L indicated more than $2.7 million of interest that was recorded as received but that could not be traced to either cash receipts or deposit slips for the first mortgage loan to Topven (1988). Although the same person reviewed this work as well as the investment section, there was no investigation as to this apparent discrepancy (as to whether the interest terms were being met).[2773] The audit manager could not explain why this was not brought forward to the engagement partner.[2774]

[2495] C&L did not consider why an operating hotel could not generate sufficient revenue to allow it to pay interest and fees to Castor. The TSH was not a construction project or a development project.

[2496] With respect to the overseas audit, Ford was unaware that Castor Montreal held the first mortgage.[2775] Ford sustained that she reviewed the interest received and accrued for the 1988 audit, as had been done in the prior year: then, the audit work had been documented but in the 1988 audit it was only *embedded in her brain,* as Ford said.[2776] Again, Ford's testimony is neither reliable nor credible. Ford erroneously believed that interest on the 2nd mortgage Topven (1988) loan was being paid in cash.[2777]

[2769] PW-1053-24, seq. pp. 347–361 (Audit Plan); PW-1053-23, seq. p. 263 (Confirmation Letter), Picard, December 6, 1995, pp. 109–117; Mitchell, April 24, 1996, pp. 197–203

[2770] E.g. PW-167D which confirms that the reason that the unsecured grid note loan (#1148) increased from $3.9M to $7.6M in 1988 was due to capitalized interest.

[2771] PW-1087-1 (Skyview, 1st mortgage); PW-1087-7 and PW-1087-8 (321351, pledge of shares): PW-1087-10 (Skyeboat, pledge of shares), and PW-1087-6 (Skyview grid note).

[2772] PW-167R, PW-167Q, PW-167T.

[2773] PW-1053-24, seq. pp. 321-322.

[2774] Mitchell, April 23, 1996, pp. 147–150, 159-160, 181–186.

[2775] Ford, November 7, 1995, pp. 161–165.

[2776] Ford, November 8, 1995, pp. 161–164.

[2777] Ford, November 8, 1995, pp. 147–148.

[2497] In contrast to the prior years, the Lambert loans were not selected for detailed review by Ford in 1988 (they were not selected either by her in 1989 and 1990).[2778] Given the risk on these loans[2779] and considering the questions on the project that had been raised in earlier years, these loans needed to be evaluated. Ford's error in excluding these loans from her sample was compounded by the failure to plan[2780] and the failure to review properly her work.[2781]

[2498] C&L had been provided the audited financial statements of Topven for 1983, 1984 and 1985, which disclosed a rapidly deteriorating financial condition. In 1988, (same for 1989 and 1990), C&L did not investigate why they were not provided with subsequent financial statements for either Topven or Topven (1988).

[2499] The fact that the 1986 interest on the Lambert loans was not paid until 1988 indicated to Ford a "*slow payer*". Nevertheless, Ford neither assessed the financial condition of the borrower, nor questioned whether the loans were collectible.[2782]

[2500] Ford never performed a security review of the loans to Lambert and there is no SAAE that these loans were adequately secured.

[2501] At discovery, Ford asserted that financial statements of Lambert were available to her although her AWPs do not record any mention thereof.[2783] At trial, Ford "improved" her prior testimony by asserting that the financial statements of Lambert she saw "*were of a current nature*".[2784] Twenty years after her 1989 audit work, it is remarkable that Ford conveniently recalls the "*current nature*" of those statements while looking at borrowers' financial statements was not something she did as an audit procedure: Ford's testimony[2785] is neither reliable nor credible.

[2502] The loan documents reviewed by C&L[2786] called for the annual provision of financial statements prepared in accordance with GAAP by a Chartered Accountant.

[2778] Ford, November 14, 1995, pp. 81–82; December 11, 2009, pp. 133-134.

[2779] For 1988, Lambert was indebted to Castor for $43.4M; $39.4 for 1989; and $40.1 for 1990. The Lambert loans had been on Castor's books since 1984; Lambert was not meeting its contractual obligations with respect to payment of interest.

[2780] Ford testified that when she performed the 1988 audit she was unaware that Lambert was connected to the TSH despite the information recorded in the prior years' AWPs (November 7, 1995, pp. 173–174).

[2781] Martin, December 18, 1995, pp. 12–14; September 25, 1996, pp. 41–42.

[2782] Ford, November 7, 1995, pp. 166–172.

[2783] Ford, November 14, 1995, pp. 59, 63, 67.

[2784] Ford, December 7, 2009, pp. 173–174.

[2785] Ford, November 14, 1995, pp. 79-85.

[2786] See for example, the LIQ and LEQ (PW-1053-23, seq. pp. 168–170) contain an "x" which, for that year, indicates that the auditor traced the information to the "original mortgage or loan document"

There is no indication that C&L ever requested such statements with respect to their review of the project loans.[2787]

[2503] Contrary to GAAS, C&L never considered the assumptions on which the Gillis appraisal value was based nor tested the reliability of the appraisal as audit evidence. It was not hidden from C&L that the appraisal was based on the completion of renovations within the year, on very optimistic income projections and on one sole valuation approach. Furthermore, C&L failed to note that the person who prepared the Gillis appraisal had not retained his professional accreditations at the time he issued this work.

[2504] C&L recorded a Management representation to the effect that the Constellation Hotel located near to the TSH was sold for approximately $115 million and "*therefore, value for Skyline is most likely greater than value given above*" without any independent verification of this representation and without considering the fact that the appraiser had already considered this transaction in reaching his estimate of value of $93 million for the TSH.

CSH

[2505] C&L never planned to aggregate the loans connected to the CSH and therefore failed to identify the security deficiencies on the project in 1988 (same in 1989 and 1990).

[2506] C&L ignored the information in their own AWPs which identified the need to "tie-in" the connected loans. Defendants' expert Selman agrees that this was a breach of GAAS, stating that Vance is correct when he opines that: «*C&L audit planning failed to address among other matters, the concentration of borrowers and projects, and interconnected loans made in Europe and in Canada ...Calgary Skyline.*»[2788]

[2507] C&L only selected the first and second mortgage loans to Skyview for detailed review for the 1988 audit and omitted the unsecured grid note loan and the loans secured by pledges of shares where there was a much higher risk that the loans were not collectible. There was no work performed by C&L to evaluate the value of the shares or the collectability of these loans; rather, C&L relied on Management representations with respect to value and collectability, i.e., that they were "good".

[2787] See, for example, Ford, November 15, 1995, pp. 174–177, where she admits that she knew that some loan agreements called for the provision of financial statements but she did not verify if they were provided as required.

[2788] Selman, June 1, 2009, p. 145.

[2508] The unaudited financial information indicates that going back to 1988, 321351 and Skyeboat both recorded significant deficits in their financial statements.[2789] Some of these statements even refer to Castor and Lambert as affiliated companies.

[2509] The failure of C&L to review financial statements is a breach of GAAS. Had this step been followed, undisclosed related party transactions might have been uncovered[2790] with respect to the CSH, as well as the poor financial condition of the borrowers which would have put in doubt the collectability of the loans.

[2510] There is no evidence that C&L reviewed the assumptions underlying the opinion on value by PKF. The report was prepared in February 1987 and anticipated that a major upgrade of the hotel would be finalized by February 1988, in time for the Calgary Olympics (and therefore could benefit from increased room rates and occupancy). Because C&L did not look at those assumptions, they did not realize that the values might not be reliable, even as early as February 1988, because the renovations had not been done.

[2511] Prior to 1988, C&L performed work on the $3.6 million vendor take back guarantee[2791] but never accounted for it in evaluating the exposure on the CSH project. C&L's audit procedures should have ensured that they remain aware of its existence.[2792] Both of Defendants' experts, Selman and Levi, initially asserted that this was misrepresentation by management and a deception on the auditor.[2793] Levi subsequently modified his Report and opinion, admitting that since the information was evident in Castor's books and records, it was not hidden from the auditors and there was no deception.[2794] As admitted by Defendants' expert Selman, this should have been disclosed as a contingency in the audited consolidated financial statements each year until 1990 and, as it was not, constituted a financial statement misstatement (for the statements 1985 – 1989, inclusive).[2795]

OSH

[2512] In the case of loan 1049, the AWPs for 1988 (same for 1989) merely brought forward the loan information questionnaire ("**LIQ**") from 1987. This LIQ evidenced that the loan originated in 1984. It incorrectly described the loan as a second mortgage notwithstanding the terms of the confirmation letters that were sent to C&L.

[2789] PW-465A, 321351, as at December 31, 1988; PW-466B, Skyeboat as at December 31, 1988; PW-465B, 321351, as at December 31, 1990; PW-466C, 321351, as at December 31, 1990.
[2790] PW-2908, Vol. 1, p. 4-E-46; PW-3034, p. 53.
[2791] See, for example, PW-1053-37, seq. pp. 19-20.
[2792] PW-2908, Vol. 2, p. G-8.
[2793] D-1295, p. 34, paragraph. 4.1.34; Selman, May 26, 2009, pp. 20-21; D-1347, p. 202.
[2794] Levi, January 12, 2010, pp. 43-44.
[2795] Selman, May 26, 2009, p. 20.

[2513] In the case of loan 1152, C&L failed to value this loan or to even understand that it was associated with the OSH in 1988 (same in 1989).

[2514] In the 1988 loan evaluation questionnaire ("**LEQ**"), C&L merely brought forward the LEQ from the previous year which contained references to appraisals from early 1985 that had been obtained at the time of the December 1984 financing.

[2515] In the case of the Mullins appraisal, it was predicated upon renovations being effected to the hotel. In the case of the General Appraisal Co., an appraisal of $5.6 million, Smith explained that by 1988 through 1990, this appraisal was of little use since the furniture depreciates in value each year. Furthermore, there is a double counting error in that the Mullins appraisal[2796] and the General Appraisal of Canada Limited appraisal[2797] both purport to appraise the furniture and equipment.

YH Group

[2516] The audit was not planned to address the concentration of loans to the YH group and the risks associated with such concentration.

[2517] There was no concern raised that although a YHDL audited financial statement was included in the 1987 AWPs, no financial statements were available to or reviewed by C&L thereafter.[2798]

[2518] Whiting testified that YHDHL and KVWIL were insolvent and had no assets with which to pay their debts.[2799] C&L should have understood that far greater risks were associated with equity loans made to YHDHL and KVWIL in that they were holding companies that did not carry on an active business and were secluded from the projects owned by YHDL.

[2519] C&L never ask for nor review information relating to Wersebe notwithstanding personal guarantees he had given to Castor. C&L never gathered audit evidence relating to those guarantees.

[2520] There was a failure to plan the audit in conjunction with the C&L Europe team. Ford did not select for audit review the $20 million of CFAG loans even though they represented the vast majority of the loan portfolio of CFAG and even though the audit plan in Montreal called for C&L to select approximately 85% of the loans by dollar value for detailed audit work.

[2796] PW-460.
[2797] PW-461.
[2798] Quintal, December 1, 1995, p. 92
[2799] Whiting, February 22, 2000, pp. 67, 70-79; May 9, 2000, p. 54

DT Smith Group

[2521] In the performance of their audits, and in valuing the loans in Castor's portfolio, including the loans by CHIO to the D.T. Smith Group of Companies, C&L completely ignored the financial position of Castor's borrowers, and did not ask for, nor review, the financial statements of such borrowers, in order to assess their ability to repay their loans to Castor.

- C&L never asked for, neither received nor reviewed, financial statements, audited or unaudited, of any of the D.T. Smith entities.

- C&L never asked for, neither received nor reviewed, any financial statements, or statements of net worth, with respect to David T. Smith personally, as guarantor of the CHIO loans.

[2522] C&L never considered the stage of completion of the construction projects, nor the fact that the sales of homes were far behind projections, or that there were significant cost overruns.

[2523] Even though the audit working papers of C&L contained an express reference to the effect that certain questions with respect to the loans by CHIO to the D.T. Smith entities had to be addressed, and that these questions could only be dealt with by meeting with Ron Smith in Montreal[2800], neither Mari-Beth Ford[2801], nor any other representative of C&L, ever met with Ron Smith in Montreal, or elsewhere, or with anyone else associated with Castor, in Montreal, to discuss or review the CHIO loans to the D.T. Smith entities.

[2524] At the time she performed the audits of the DT Smith loans, Ford was not aware that the shares of the DT Smith entities were owned 50% by DT Smith and 50% by Norma Smith (wife of DT Smith); nor did she make any enquiry as to who the owners of the DT Smith entities were. She testified that it was of no importance, for purposes of her audit, to know who the beneficial owners of the DT Smith companies were. She was not aware that the only guarantee that existed for the loans to the DT Smith companies was from DT Smith.[2802]

[2525] At trial, she could not recall that each of the loan agreements for the CHIO loans to the DT Smith companies stipulated that the borrower and the guarantor were to furnish financial statements.[2803] However, on discovery, Ford testified that she did not ask for financial information for any of the borrowers that she reviewed[2804] since it was not necessary for purposes of her review if she otherwise had sufficient appropriate

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[2800] PW-1053-84-5
[2801] Ford, November 14, 1995, pp. 184-185
[2802] Ford, December 8, 2009, pp. 120-121.
[2803] Ford, December 8, 2009, p. 121.
[2804] Ford, November 7, 1995, pp. 105-106.

audit evidence in her professional judgment. She was wrong – she did not have sufficient appropriate audit evidence - she should have asked for that information and she should have looked at that information.

[2526] Ford admits that, in her AWPs, she failed to document either the levels of materiality, or the risk factors used in determining the nature, extent and timing of the audit procedures.[2805] Selman acknowledged that:

> «MBF's working papers "are not very fulsome or informative", were "too brief", "below the standard of working paper preparation that would be the norm", and "without question, Ms Ford's working papers are not very good working papers in total". "They're below the norm - - - they don't meet the normal standard of working papers that I have seen in my experience.» [2806]

[2527] At trial, Ford was referred to her AWPs for year-end 1988 in respect to the Wood Ranch II project and to Castor's two loans relating thereto. She confirmed that this was one of the loans she had reviewed because it was a new loan.[2807] At discovery, she had confirmed however that she had not made any determination as to the stage of development of the Wood Ranch II project, and that she did not know whether the townhouses were completed or not when she did her review.[2808]

[2528] With respect to Dove Canyon I and Dove Canyon II project, which loans had been selected by her for review,[2809] Ford admitted on discovery: «*I do not mention a specific appraisal report, though I do note down the value – the different values of the property at the different phases of the property*».[2810] To say the least, Ford's work was of poor quality – it is reasonable to wonder if she really understood what she was doing and what had to be done. Ford confused the revised loan amounts for the Dove I and Dove II projects with what she believed to be the value of the security for those projects.[2811] She did not have available to her any appraisals for these two projects: if she had reviewed appraisals, she would have inscribed the appraisal values and not the revised loan amounts.[2812] Ford committed the same mistake for the years 1989 and 1990.[2813]

TWTC

[2529] Loan 1046 was secured by a pledge of the shares of TWTCI. Each year, the audit confirmation letters referred to such pledge. Notwithstanding that clear

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[2805] Ford, December 8, 2009, p. 127. See also PW-1419-2A, Section 5145.05.
[2806] Selman, June 11, 2009, pp. 14-16.
[2807] PW-1053-84, seq. p. 88; Ford, December 8, 2009, p. 178.
[2808] Ford, November 7, 1995, pp. 98-99.
[2809] Ford, December 8, 2009, p. 34.
[2810] Ford, November 7, 1995, p. 101.
[2811] Ford, December 9, 2009, pp. 36-47
[2812] Ford, December 9, 2009, p. 39-40.
[2813] PW-1053-83, seq. p. 114 (1989), PW-1053-81, seq. p. 78 (1990).

information, C&L described the loan as a second mortgage in each of 1987, 1988, 1989 and 1990.[2814] The 1987 AWPs were merely brought forward mechanically to 1988 and then copied for 1989 and 1990 even though the information was wrong. No attempt was made to reconcile the description of the security on the commitment letters and confirmation letters with the "understanding" that the loan was a second mortgage.

[2530] Although loan 1046 had originated in 1984, no questions were put as to why this "one-year" loan had been renewed on six subsequent occasions. No questions were posed by C&L (same for 1989 and 1990) as to why the interest was being capitalized to the loan, notwithstanding the obligation of the borrower to pay such interest and why reasonable assurance existed as to the collectability of this interest. Although the borrower in each of the years was Toronto Waterfront Developments Corp., in each of 1987, 1988, 1989 and 1990, C&L erroneously described the borrower as Toronto Waterfront Ltd.

[2531] Loan 1067 was a loan to YHDL secured by a pledge of the common shares of TWTCI owned by YHDL. Each of the audit confirmation letters sent to C&L for purposes of the audits described the security as a first pledge of issued and outstanding common shares.[2815] In each of the years 1987 through 1990, C&L described the loan as "debenture loans". This error was blindly brought forward each year.

[2532] Although all of the interest on loan 1067 was capitalized to account 046/Loan 1153 contrary to the loan agreements, C&L did not question why this unplanned capitalization of interest had occurred each year. No attempt was made to obtain SAAE to value the loan.

[2533] Although C&L referred each year to the pledge of an interest in the office and condominium tower,[2816] no effort was made to ascertain whether such security had ever been registered in respect of loan 1049. The commitment letters that C&L allegedly looked at called for legal opinions to be obtained confirming that the security was legal, valid, binding and enforceable. No such legal opinion existed; on the contrary, the opinions disclosed the opposite.

[2534] All of the interest on loan 1049 was capitalized to the loan even though the commitment letters did not provide for such capitalization of interest. It was an error on the part of C&L not to ascertain why this borrower was not paying interest as appeared on the mortgage and loan ledger card PW-167EE.

[2814] For example, 1989: PW-1053-19, seq. pp. 189, 287.
[2815] For example, 1989: PW-1053-19, seq. pp. 191, 260.
[2816] For example, 1989: PW-1053-19, seq. p. 193.

[2535] C&L referred in the LEQ for loan 1049 to a Stewart Young & Mason appraisal between $182 million and $285 million.[2817] Such appraisal does not exist. In fact, the range of values on the appraisal suggests that it could not have been an appraisal.

[2536] No attempt was made by C&L to obtain audited or unaudited financial statements of any of the three borrowers notwithstanding the undertakings of the borrowers to provide such statements in the loan agreements, and the requirement for such information in the LEQ.

[2537] No attempt was made to ascertain whether the borrowers were complying with their loan covenants, as Higgins had suggested in the peer review.

[2538] Notwithstanding a chart provided to C&L for each audit that Stolzenberg had a 2.35% interest in TWTCI, no effort was made to disclose that this was a related party transaction.[2818]

1989

MLV

[2539] For 1989, virtually all of the errors committed by the audit staff in the 1988 audit were repeated such that it is unnecessary to repeat the summary referred to above. [2819]

[2540] In particular, breaches of GAAS included the failure to aggregate all loans secured by the assets of the MLV project, the failure to accurately analyze the security available to Castor for each loan and the use of inapplicable appraisal values without any review of the assumptions contained in the appraisal reports.

[2541] Once again, no audited financial statements of MLVII were obtained and the unaudited draft disclosed increasingly alarming negative information.

[2542] Wightman once again failed to follow up on information and representations of management made to him in prior years and to properly question management, and to follow up on information provided by management, during the year-end wrap-up meeting. In addition, the notes made by him at the year-end wrap-up meeting are sparse and superficial.

[2817] PW-1053-23, seq. p. 201.
[2818] PW-1053-23, seq. p. 198.
[2819] See also PW-2941, Vol. 3, pp. 120-155.

YH Group

[2543] There was no concern raised that although a YHDL audited financial statement was included in the 1987 AWPs, no financial statements were reviewed by C&L for 1988 and 1989.[2820]

[2544] Whiting testified that YHDHL and KVWIL were insolvent and had no assets with which to pay their debts.[2821] C&L should have understood that far greater risks were associated with equity loans made to YHDHL and KVWIL in that they were holding companies that did not carry on an active business and were secluded from the projects owned by YHDL.

[2545] The lack of substantive audit work was prevalent. For example, Belliveau, the junior staff member responsible for the 1989 investment section, acknowledged that the only audit work performed on Loan 1081 amounted to relying on the client and to notint that there was a promissory note.[2822]

[2546] Nothing was done in relation to Wersebe's guarantees.

TSH

[2547] In 1989, the AWPs for the Management Contract loan 1137 indicate that the auditor was shown financial statements of the TSH that disclosed $19.4 million of gross revenue, consistent with the month end report for the TSH for December 1989[2823]. Even though this was shown to them, C&L ignored the negative information, i.e. the decline in revenue over the year, the actual income pre-debt of $298,970 as compared to the budgeted amount of $3.5 million and the net income pre-debt of negative $14.5 million). The cash flow problems of the TSH were not concealed, as Selman would have one believe.[2824]

[2548] Aside from recording the gross figure for the management fees in connection with loan 1137, C&L did not consider these financial statements in the analysis of the TSH loans whereas such financial statements should have been reviewed. C&L's failure to consider negative information in financial statements provided by the client reflects the inadequacy of the audit work and the failure to exercise independent professional judgment.

[2820] Quintal, December 1, 1995, p. 92
[2821] Whiting, February 22, 2000, pp. 67, 70-79; May 9, 2000, p. 54
[2822] Belliveau, May 23, 1996, pp. 431-441.
[2823] PW-429.
[2824] Selman suggests that Management concealed the cash flow problems of the TSH from C&L (D-1295, pp. 37-38).

[2549] Belliveau, who saw these financial statements for the management fee analysis, also did the detailed work on the Topven loans.[2825] The failure to obtain and review financial statements of borrowers for material loans was an audit error, especially in the case of the loans that had no real estate collateral such as the grid note loan.

CSH

[2550] For the 1989 audit, the three loans presenting the highest level of risk were not selected for detailed review in Montreal and the 2nd mortgage loan was not selected for review by the audit team overseas as it was no longer a "new" loan.[2826] This was both a planning and a performing failure.[2827]

[2551] The loan documents reviewed by C&L called for the monthly payment of interest in cash (apart from the reserve accounts that were depleted in 1988 and thereafter increased the exposure on the project).[2828] The mortgage and loan ledger cards reviewed by C&L, as well as the accounting records, indicated that the CSH loans were all being capitalized on the grid note loan in the Montreal portfolio, including the 2nd mortgage loan from CHIF.[2829] In 1989, an analysis of capitalized interest was performed by the audit team in Montreal and they were informed by Management of the capitalization of interest.

[2552] The loan documents reviewed by C&L called for the annual provision of financial statements prepared in accordance with GAAP, by a Chartered Accountant for Skyview. For the 1989 audit, C&L did review the 1989 financial statements of Skyview[2830], but for the sole purpose of the management contract loan. They noted only the amount paid in management fees and the gross revenue but failed to note and consider that there was a loss for the year of over $7 million, and a cumulative deficit of $11.7 million.

OSH

[2553] Failures of 1988 relating to loans 1049 and 1152 were repeated.

[2554] Ron Smith provided accurate information to the audit staff member who then proceeded to make egregious errors. Smith prepared a diagram[2831] which indicated that the appraised value was $29 million, but that $16 million was ascribed to Campeau leaving a net balance of $13 million «*after renovations to be completed*».

[2825] Belliveau, May 23, 1996, pp.496 and following

[2826] PW-1419-2A, Section 5130.24, introduced into the Handbook in October 1988, required a risk-based audit at the time of the 1988 audit, the auditors were aware that the risk of misstatement was in the loan portfolio and as part of audit planning should have focused on loans with weaker or no security.

[2827] PW-2908, Vol. 1, pp. 5-12, 5-32.

[2828] PW-1087-1 (Skyview, 1st mortgage); PW-1087-7 and PW-1087-8 (321351, pledge of shares): PW-1087-10 (Skyeboat, pledge of shares), and PW-1087-6 (Skyview grid note).

[2829] PW-167R, PW-167Q, PW-167T.

[2830] PW-467C

[2831] PW-1053-19, seq. p. 244.

[2555] The Fitzsimmons appraisal[2832] indicated that this $13 million net balance was predicated upon renovations being performed at a cost in excess of $10 million. C&L failed to question Castor as to the cost of the renovations. On the LEQ,[2833] the C&L junior staff member used the $13 million value as if it was the net value, failed to consider what the assumptions of the appraisal were, did not obtain any financial statements of the borrower and erroneously considered that the loan was covered.

TWTC

[2556] For 1989, C&L referred to a "Royal LePage Appraisal" for the condominium of $70 million and to "offers" for the land site dated December 5, 1989 of $145 million. The $70 million was merely the internal value arrived at by YH[2834] and the "offers" were, rather, a brokerage mandate given to Coldwell Banker on December 5, 1989.[2835]

[2557] C&L then added $70 and $145 and inexplicably arrived at the figure of $235 million (instead of $215 million).

[2558] In their analysis, C&L used a security value of $235 million. No one detected this clerical, but significant error. Had a review been done, as it should have to comply with GAAS, the error would have been obvious.

DT Smith

[2559] In respect of the Circle Ranch project, Ford confirmed that this was one of the loans chosen by her for review for year-end 1989. Even though it had been chosen for review, Ford was unable to direct the Court to AWPs evidencing audit work performed to value the Circle R loan or to any evidence supporting her notation: «*Appraisal to be made – approximately $15 million in value*».[2836]

[2560] On discovery, Ford was asked about the notation «*appraisal to be made*» and she testified as follows:

- at the time of her audit of this loan, she «*must have seen documents that made her happy*»;
- there was no appraisal at the time of her review;
- she made no further inquiry;

[2832] PW-462, bates p. 53.
[2833] PW-1053-19, seq. p. 247.
[2834] PW-1069-8.
[2835] PW-1069-13.
[2836] Ford, December 9, 2009, pp. 99-103.

- she couldn't recall asking for any information regarding that property, nor could she recall having any further information with respect thereto.[2837]

[2561] The Rancho Parcel II and Rancho Parcel V projects were also chosen for review for year-end 1989 but Ford neither received nor reviewed a summary or a full appraisal report for these projects.[2838]

[2562] In respect of the Rancho California project, Ford confirmed that this was one of the loans selected by her for valuation for year-end 1989.[2839] On her AWP,[2840] she recorded a value of $33.2 million under the column "Appraisal Received" representing the appraisal value of the project as if it were improved with rough-grading ready for final site preparation for finished lots, ready for construction of houses, while the "as is" value is stated by the appraiser to be $13 million only.[2841]

[2563] Ford chose the higher value without any evidence in her AWPs to support her choice or the fact that the land had been rough-graded, ready for final site inspection for finished lots, ready for construction of houses.[2842]

[2564] Ron Smith confirmed that virtually nothing was ever done on this project.[2843]

> So, with all of those delays, what happened was that he ended up having to extend the commitment in nineteen ninety (1990) and at that point in time, we put it into a holding pattern such that all we did was provide for holding the land as is, the grading had not really gone... **there hadn't been much grading**, all they were doing at that point in time was protecting the property from brush fires and keeping it at sort of a very slight mass-graded level. So, virtually nothing had been done to the project and **it was put into a holding pattern from August nineteen ninety (1990) onwards, so nothing really progressed on this project** at that point in time.[2844] (our emphasis)

[2565] Even though the audit working papers of C&L contained an express reference to the effect that certain questions with respect to the loans by CHIO to the D.T. Smith entities must be addressed, and that these questions could only be dealt with by meeting with Ron Smith in Montreal[2845], neither Mari-Beth Ford[2846], nor any other representative of C&L, ever met with Ron Smith in Montreal, or elsewhere, or with anyone else associated with Castor, in Montreal, to discuss or review the CHIO loans to the D.T. Smith entities.

[2837] Ford, November 7, 1995, pp. 249-251.
[2838] Ford, November 7, 1995, pp. 47-55, 238-240
[2839] Ford, December 9, 2009, p. 143.
[2840] PW-1053-83, seq. p. 103.
[2841] PW-1053-83, seq. pp. 133-134.
[2842] Ford, December 9, 2009, p. 148.
[2843] Ron Smith, June 11, 2008, pp. 90 and following; PW-1120
[2844] Ron Smith, June 11, 2008, p.93
[2845] PW-1053-83-5
[2846] Ford, November 14, 1995, at pp. 184-185

[2566] Had C&L met with Ron Smith, as their own audit working papers said they should have, and had a proper review of the work performed by the audit staff been done as GAAS required, C&L would have known that Ford's conclusions were wrong. C&L would have realized they could not and should not rely on Ford's work product.

[2567] Inexplicably, C&L did not consider the stage of completion of the projects, nor the fact that the construction or the sales of homes were far behind projections, or that there were significant cost overruns.

[2568] Moreover, C&L never asked for, neither received nor reviewed, any financial statements, audited or unaudited, of any of the D.T. Smith entities.

[2569] C&L never asked for, neither received nor reviewed, any financial statements, or statements of net worth, with respect to David T. Smith personally, as guarantor of the CHIO loans.

1990

MLV

[2570] By 1990, the MLV project had deteriorated to the point that it was identified in the audit planning memorandum for specific attention by the audit staff.[2847]

[2571] Castor itself had taken a loan loss provision of $5 million on the project.

[2572] Rather than having borrowers pay interest from amounts advanced by Castor, interest was simply capitalized but nevertheless recognized as revenue[2848] without any assurance of collectability.

[2573] Faced with this apparent disastrous situation, C&L nevertheless relied upon appraisals to support a value of $144 million, an increase of $14 million over the appraisal amounts used in 1988 and 1989.

[2574] Once C&L determined that Castor viewed these MLV loans as "*high risk*", that there was a shareholders' deficiency of $65 million and that Castor proposed a loan loss provision of $5 million, there was absolutely no basis for C&L to conclude that the revenue (all of which was capitalized) had reasonable assurance of collectability.

[2575] The summary notes made by Wightman during the year-end wrap up meeting reflect a specific discussion about the MLV project. Remarkably, although this project was included in the $275 million of problem loans, Wightman did not see fit to do any

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[2847] PW-1053-16, seq. pp. 260, 267.
[2848] PW-1075A, PW-1070H-1

further analysis of the carrying value of the MLV loans, nor did he request the audit staff to perform any additional procedures.[2849]

[2576] The attitude of Wightman is all the more surprising since, for the 1990 audit, he was given an aggregation of the loans of CHL and CHIF[2850] which reflected a shareholders' deficit in excess of $65 million. This aggregation was also deficient in that it did not include loans 1048 to YHLP and 1125 to KVWIL, such that the reality of the situation was even worse than disclosed in the aggregation.

[2577] As noted in the reports of Vance[2851] and Froese[2852], numerous errors were made in the AWPs.

[2578] The problems of the previous years were exacerbated by the insistence of FICAN, a secured creditor, to be paid in full: Castor was forced to advance additional funds to pay out the FICAN loan in the amount of $6 million, above and beyond advances made to pay real estate taxes as well as support payments to cover interest due to prior ranking lenders.[2853]

[2579] The unaudited financial statements of MLVII continued to disclose deteriorating operations which required substantial support from YH related entities.

[2580] Wightman himself never saw the appraisals relating to the MLV project.[2854]

[2581] In attending the year-end wrap up meeting, Wightman was not aware that Ron Smith had informed the audit staff that the loans to the MLV project were considered by him to be "*high risk*".[2855]

[2582] Furthermore, the notations made by Wightman contain errors and inconsistencies which betray a lack of understanding of the facts and the exposure of Castor to the MLV project.[2856] Wightman expected that "serious provisions" would be taken on the MLV project after 1990.[2857] Except for a lack of independence affecting negatively his judgment and objectivity, one cannot understand Wightman's failure to have required such provisions for purposes of the 1990 audit.

[2849] Wightman, February 25, 2010, pp, 46-52.
[2850] PW-1053-15, seq. pp. 159, 259.
[2851] PW-2908, Vol. 2, pp. A-15 to A-23 (MLV).
[2852] PW-2941, Vol. 3, pp. 9-17.
[2853] PW-1070F-2; PW-1070F-4; PW-1070F-5; R. Smith, May 14, 2008, p. 139.
[2854] Wightman, February 25, 2010, p. 42.
[2855] Wightman, February 25, 2010, p. 52.
[2856] PW-1053-12, seq. pp. 76-93.
[2857] Wightman, February 25, 2010, p. 92.

YH Group

[2583] There was no concern raised that although a YHDL audited financial statement was included in the 1987 AWPs, no financial statements were reviewed by C&L for 1988, 1989 and 1990.[2858]

[2584] Whiting testified that YHDHL and KVWIL were insolvent and had no assets with which to pay their debts.[2859] C&L should have understood that far greater risks were associated with equity loans made to YHDHL and KVWIL in that they were holding companies that did not carry on an active business and were secluded from the projects owned by YHDL.

[2585] Again, errors were made and not caught. Proper review required by GAAS did not take place. By way of example, for the 1990 audit of Loan 1081 to YHDHL, the junior audit staff member purported to place an "X" beside the name of the borrower on the LIQ[2860] and indicated YHDL when in fact the borrower was YHDHL.[2861] He erroneously indicated that «*CHL gets securities from % of ownership on different projects that YHDL is involved therefore no direct securities from YHDL but rather from the different projects (main collateral)*». In fact, the borrower owned no projects but was merely the holding company that owned the shares of YHDL, which in turn was insolvent.

The nasty nine loans ($40 million)

[2586] C&L failed in every conceivable way to audit the $40 million of loans, the "Nasty Nine Loans", which, if they had been written off, would have wiped out alone all of Castor's profit for the year.

[2587] In the case of the Nasty Nine loans, Quesnel reviewed them because he found the situation "bizarre".[2862] Although he considered these loans doubtful accounts and brought forward the schedules to Wightman, no further audit work was done to determine the collectability of such unsecured loans or the borrowers' financial position.

[2588] The Nasty Nine loans were made just prior to year-end.

[2589] The loans were part of the reallocation of approximately $60 million of accrued year end indebtedness.

[2858] Quintal, December 1, 1995, p. 92
[2859] Whiting, February 22, 2000, pp. 67, 70-79; May 9, 2000, p. 54
[2860] PW-1053-15, seq. p. 299.
[2861] PW-1053-15, seq. p. 327.
[2862] Quesnel, November 24, 1995, pp. 110-114

[2590] By the time of the audit, the loans had not yet been finalized and Smith advised the auditors that they were very temporary loan situations and that Castor «*hadn't received the documentation yet*».[2863]

[2591] The commitment letters for the loans do not disclose the existence of any guarantees.[2864] Smith was not aware of any guarantees being obtained and never advised the auditors that the loans were secured by guarantees.

[2592] As a matter of fact, Castor had not obtained any personal guarantees from Wersebe in respect of these nine loans prior to the completion of the audit on February 15, 1991.

[2593] There were no requests by C&L for audit confirmations in respect of the nine loans and the AWPs disclosed that C&L considered the loans to be unsecured.

[2594] C&L obtained absolutely no sufficient appropriate audit evidence to value these loans described as "bizarre" by the junior staff member. There were no credit analyses, no financial information or anything whatsoever to substantiate that the borrowers had the capacity to repay these loans.

[2595] The red loan files for the nine loans,[2865] which the auditors purport to have looked at based on their tick legend, provided no information about the borrowers' capacity to pay or the existence of guarantees.

[2596] The most basic of window dressing procedures would have revealed the circle of funds related to these year end loans. Tooke and Rancourt testified that although they had no knowledge of the Nasty Nine transactions, it was obvious to them as bookkeepers that the $40 million of cash that left Castor was the same $40 million that came back on or about the same dates.[2866] Tooke said she gave to the auditors all the books and records and supporting documents they did ask for.[2867] Moreover, in cross-examination, she confirmed she had never been told by Stolzenberg, Dragonas, Goulakos or Ron Smith to avoid topics or to refrain from discussing anything with C&L's audit staff members.[2868]

[2597] C&L correctly "*expressed uncertainty*" about the loans and placed them on their list of doubtful accounts.

[2863] R. Smith, May 15, 2008, p. 113.
[2864] PW-1064-1 to PW-1064-9.
[2865] For example, PW-1064-1.
[2866] Tooke, February 27, 2008, pp. 146, 149, 163-168; Rancourt, February 29, 2008, pp. 11-16, 20, 44, 50, 136 and following; Rancourt, March 3, 2008, pp.4-8; PW-99A and PW-173
[2867] Tooke, February, 28, 2008, p. 95
[2868] Tooke, February 28, 2008, pp. 27, 65, 89-90, 92-99

[2598] At the year-end meeting, and after having asked Ron Smith to leave them, Wightman raised with Stolzenberg the fact that the loans were problematic[2869] but he did nothing to resolve such problem before signing off on the audit. Except for a lack of independence affecting negatively his judgment and objectivity, there is no explanation for Wightman's failure to have required that further audit work be done in relation to those loans.

[2599] Essentially, C&L failed to audit these $40 million of loans which, if they had been written off, would have alone wiped out all of Castor's profit for 1990.

TSH

[2600] In 1990, the unsecured grid note loan was confirmed but a loan evaluation questionnaire was completed only for the first mortgage loan. The unsecured grid note loan 1148 was identified by the junior auditor as a doubtful account and was clearly of a higher risk than the first mortgage loan but no audit evidence was obtained to assess the collectability of this loan of $26.4 million.[2870] Such errors in the performance of auditing should have been identified by the reviewer had a proper review, in accordance to GAAS, been done.[2871]

[2601] In 1989, information had been brought forward to Wightman about the TSH, to the effect that there was about $10 million of capitalized interest in connection with Topven; and Wightman had noted in the AWPs that «*Money should be repaid in 1990.*»[2872] Wightman admitted that the money was not repaid in 1990, but he did not consider this to be a management misrepresentation.[2873] No further work was done to assess the collectability of these loans, although the audit plan for 1990 indicated the TSH as a project that «*will need to be looked at in detail*».[2874]

[2602] For the 1990 audit, both the audit staff in Montreal and Wightman should have been aware of the global exposure on the TSH.[2875] Wightman only considered the loans in Montreal, when he attempted to aggregate the TSH loans for the wrap up meeting, and he incorrectly identified the aggregate of the TSH loans as $66 million.[2876]

[2869] R. Smith, September 16, 2008, p. 215.

[2870] PW-1419-2A, Section 5130.24, introduced into the Handbook in October 1988, required a risk-based audit at the time of the 1988 audit, the auditors were aware that the risk of misstatement was in the loan portfolio and as part of audit planning should have focused on loans with weaker or no security.

[2871] PW-1053-24, seq. pp. 347–361 (Audit Plan); PW-1053-23, seq. p. 263 (Confirmation Letter), Picard, December 6, 1995, pp. 109–117; Mitchell, April 24, 1996, pp. 197–203 to the effect that they understood that all loans for which a confirmation was sent were to be included in the sample for the completion of loan questionnaires.

[2872] PW-1053-19, seq. p. 104.

[2873] Wightman, October 18, 1995, pp. 202–203.

[2874] PW-1053-16, seq. p. 267.

[2875] Vance, April 8, 2008, p. 204-205; PW-2809, Vol. 2, p. E-3; PW-2893-43.

[2876] Note: Goodman erroneously relies on this AWP and calculation by ECW as a **value indicator** for the CSH in 1990 (D-1312, p. 420).

Wightman negligently omitted the CHIF Topven 2nd mortgage loan and the Lambert loans from his analysis.[2877] C&L should have identified easily the security deficiency on this project, but they did not.

[2603] Wightman recorded the information that the Skyline Hotels were in a difficult position because of declining interest rates and the decision to cease capitalizing interest on these loans.[2878] In fact, Management did not cease the capitalization of interest during 1991, a fact evident in the general journal and the mortgage and loan ledger cards, but C&L did nothing to confirm that Management was fulfilling its commitments prior to their issuance of the share valuation letters in March and October 1991.

CSH

[2604] In 1990, C&L recorded in the AWPs that the shares of Skyview were 70% owned by Skyeboat and 30% owned by 321351. C&L also recorded the shares of Skyeboat were worth $20 million and that shares of 321351 were worth $25 million.[2879] Neither the junior auditor nor the reviewer questioned the evident mistake in these values or did any work to corroborate the value attributed to the collateral.

[2605] For the 1990 audit, C&L expressed uncertainty about the Skyview grid note, loan 1154 but, inexplicably, considered the lower ranking loans to Skyeboat and 321351 to be "good". This made no sense, according to Ron Smith.[2880]

[2606] For the 1990 audit, both the audit staff in Montreal and Wightman should have been aware of the global exposure on the CSH because the AWPs explicitly referred to the topic as well as the overseas inter-office MAPs. Nevertheless, Wightman only considered the loans in Montreal when he attempted to aggregate the CSH loans for the wrap up meeting and incorrectly identified the aggregate of the CSH loans as $53 million when, in fact, the four loans added up to $64 million.[2881]

[2607] Even without the additional exposure from the $16 million loan in the overseas portfolio, C&L should have easily identified the security deficiency on this project, but they did not.

[2877] PW-1053-12, seq. p. 77.
[2878] PW-1053-12, seq. p. 84. See also PW-6-1, Tab 23 and Tab 24 and PW-167D.
[2879] PW-1053-15, seq. pp. 287-288, 289-299.
[2880] Ron Smith, September 5, 2008, p. 166.
[2881] PW-1053-12, seq. p. 90.

OSH

[2608] In 1990, when loan 1049 was transferred to 687292, C&L indicated that the interest was being capitalized, but made no attempt to understand why the borrower was in default of its loan obligations.

[2609] C&L totally ignored the existence of the rental obligations to Campeau which constituted a prior ranking obligation that had to be met prior to the payment of any such interest.

[2610] C&L erroneously described loan 1152 as a second mortgage on the leasehold when the confirmation letter clearly indicated that the security was merely a "grid note".[2882] Although the loan called for the payment of interest by the borrower, C&L indicated that the interest was being capitalized and made no attempt to understand why this operating hotel was not generating sufficient monies to meet its interest obligations.

[2611] Furthermore, C&L was aware from the loan documents that Castor had the right to obtain revenue and expense statements, rent rolls and statements of capital expenditures from the borrower such that C&L should have requested access to such information.

[2612] In the LEQ,[2883] the C&L junior staff member inexplicably ignored that $16 million of the $29 million appraisal value was ascribed to the freehold interest of Campeau.

[2613] In addition, C&L erroneously considered that loan 1165 was in the amount of $11,114,595 when, in fact, the audit confirmation letter that they received and supposedly looked at [2884] indicated that the amount was $12,678,479. Consequently, the analysis on the LEQ was wrong by approximately $17,500,000 (the aggregate of the $16 million Campeau interest and the $1.5 million understatement of Loan 1165).

[2614] Even using their flawed figures, C&L should have arrived at a deficiency of more than $12 million rather than a surplus of $5,381,655.

[2615] C&L did not request nor review any financial information regarding the borrower or the hotel and made no attempt to understand why Castor was not receiving any cash payments from its borrower for interest and fees.

[2616] C&L did not ask any questions as to why (as recorded on the yellow cards) Castor was not only capitalizing interest and fees but, also, was funding expenses of the borrower and paying for its legal fees.

[2882] PW-1053-15, seq. pp. 281-282, 306.
[2883] PW-1053-15, seq. p. 283.
[2884] PW-1053-15, seq. p. 320.

[2617] Finally, C&L made no attempt to ascertain whether 687292 was a related party. The information that established that it was a related party was readily available and not hidden from anyone. In fact, the public corporate records clearly indicated that Stolzenberg was a director and officer of this company.

MEC

[2618] The 1986 AWPs[2885] indicate that C&L was aware of the 80% maximum loan to value ratio ("**LTV**") and took such ratio into account for purposes of the valuation of the Les Terrasses loans in 1986. C&L further recognized that the high LTV would put Castor at risk. However, in 1990, C&L disregarded the policies of Castor relating to the maximum loan to value ratio against which Castor was prepared to lend.

[2619] By the 1990 audit, C&L had already determined that the outstanding indebtedness on the MEC property exceeded the appraised value even if such analysis was erroneous in that it excluded certain loans on the MEC project, the costs to complete, the trade debt and the accrued interest.

[2620] In the AWPs of 1989, Wightman had indicated that the equity loan to YHDL (loan 1042) would be repaid in 1990. Wightman testified that he assumed that interest on the YHDL equity loan was not capitalized even though the AWPs indicated the opposite.[2886] The General Journal which was given to the auditors indicated that interest on this loan was capitalized each month in 1990 to Account 046/Loan 1153.[2887]

[2621] In his 1990 year-end notes,[2888] Wightman erroneously referred to non-existent 4th mortgages in favour of Castor in respect of the equity loans to 97872 and YHDL. It was noted by C&L that a "new" appraisal was coming and that the existing appraisal of $275 million was done in "1989" «*before Center was complete*». No attempt was made to resolve:

- why the property had not been sold and the loan not repaid in 1990, as previously represented;
- why no loan loss provisions were required even though the loans exceeded 100% of the appraised value;
- why Castor was tolerating capitalization of all interest.

[2622] Neither C&L staff members nor Wightman made any effort to ascertain why the MEC would have a higher value than the available Royal LePage appraisal when none of the assumptions on which such appraisal was based were anywhere close to being

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[2885] PW-1053-35, seq. p. 134.
[2886] Wightman, October 10, 1995, pp. 26-29.
[2887] PW-86, bates p. 000486.
[2888] PW-1053-12, seq. p. 93.

attained. C&L made no attempt to seek audit evidence to corroborate management's representations regarding the "internal" value of $300-350 million.

[2623] Given the situation in 1990, it was incumbent upon the auditors to insist upon updated appraisals. If C&L had complied with GAAS, and sought sufficient appropriate audit evidence, they would have found that the value of the MEC project was significantly lower than what management was telling them: through an updated report, Royal LePage had appraised it at $241 million, as of September 1, 1990[2889].

[2624] Moreover, C&L made no attempt to ascertain who the owners of 97872 were. Had they merely reviewed the closing binders for the refinancing or asked the most basic of questions, they could have readily ascertained that Stolzenberg controlled or significantly influenced 97872.[2890]

TWTC

[2625] C&L continued to make all of the same mistakes in 1990.

[2626] It is remarkable that while the audit staff member for 1990 redid the LEQ, he continued to add $70 million and $145 million to arrive at $235 million instead of $215 million.[2891] He continued to refer to the "offers" which, by this time, would have been 14 months old and erroneously referred to the Royal LePage appraisal.

[2627] Notwithstanding the reference in the AWPs for 1989 that the sales would be completed by April 1990, no questions were put by C&L as to why the office lands were not yet sold.

[2628] C&L considered the best TWTC loan (Loan 1149 to TWTCI) to be "*risky*" and of a "*high risk nature*", but considered the lower ranking loans to the parents of TWTCI to be "*good*".[2892] Such comments evidence a total lack of understanding on the part of the auditors and an absence of proper review.

[2629] Notwithstanding that the junior C&L staff member correctly identified that loan 1149 was of a high risk nature and that he wrote «*C&L judge that CHL could take a reserve on this loan*», no consideration was given by C&L to the fact that the lower ranking loans would necessarily also require a reserve.

[2630] In fact, nothing was done to resolve the suggested reserve on loan 1149 that had been brought forward by Quesnel.

[2889] PW-1108B
[2890] PW-1102A-6.
[2891] PW-1053-15, seq. p. 223.
[2892] PW-1053-15, seq. pp. 219, 221, 225.

[2631] Smith testified that C&L never made any recommendations to him regarding any of the loans. He added that it did not make sense that the TWTC! loan could be bad or doubtful, but that the TWDC loan and YHDL loan could be good.[2893] Finally, Smith testified that no audit staff member ever questioned him regarding the assumptions in the Stewart, Young & Mason appraisal that had been obtained by Castor,[2894] the only one that Castor had for the audit.

[2632] Once C&L judged that the best TWTC loan required a reserve, all the TWTC loans should have been placed on a non-accrual basis and C&L should have insisted that all revenue be reversed, but they did not.

DT Smith Group

[2633] In the performance of the audit, and in valuing the loans by CHIO to the D.T. Smith Group of Companies, C&L completely ignored the financial position of Castor's borrowers, and did not ask for, nor review, the financial statements of such borrowers, in order to assess their ability to repay their loans to Castor.

- C&L never asked for, neither received nor reviewed, any of the financial statements, audited or unaudited, of any of the D.T. Smith entities.

- C&L never asked for, neither received nor reviewed, any financial statements, or statements of net worth, with respect to David T. Smith personally, as guarantor of the CHIO loans.

[2634] Thus, for the year ended December 31, 1990, although the D.T. Smith Group of Companies was indebted to Castor for US$237 million, C&L failed to request, obtain, or review any financial statements for the D.T. Smith Group of Companies, and for the guarantor, and was unaware that the D.T. Smith borrowers were in default of the covenant to furnish the financial statements of the borrower(s) and the guarantor to Castor.

[2635] C&L did not consider the stage of completion of the construction projects, nor the fact that the sales of homes were far behind projections, or that there were significant cost overruns.

[2636] Even though the audit working papers of C&L contained an express reference to the effect that certain questions with respect to the loans by CHIO to the D.T. Smith entities had to be addressed, and that these questions could only be dealt with by meeting with Ron Smith in Montreal[2895], neither Mari-Beth Ford[2896], nor any other representative of C&L, ever met with Ron Smith in Montreal, or elsewhere, or with

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[2893] R. Smith, September 16, 2008, pp. 173-177.
[2894] R. Smith, September 16, 2008, pp. 163-166.
[2895] PW-1053-81-2
[2896] Ford, November 14, 1995, at pp. 184-185

anyone else associated with Castor, in Montreal, to discuss or review, the CHIO loans to the D.T. Smith entities.

[2637] C&L failed to obtain sufficient appropriate audit evidence with respect to the loans by CHIO to the D.T. Smith Group of Companies, failed to determine the borrowers' ability to repay the loans, and the guarantor's ability to cover any shortfall.

[2638] C&L should have insisted on receiving the financial statements of the D.T. Smith Group, and of the guarantor, and, failing that, should have requested permission to speak directly to the auditors of the D.T. Smith Group to determine why such financial statements were not available.

- Had they sought such permission and obtained it, they would have interacted with Strassberg and they would have learned about the significant LLP he felt the DT Smith group had to take.

- If the permission had been refused, C&L would have had to ask themselves why they were not allowed to speak to DT Smith's auditor when the borrowers were not complying with their loan covenants.

[2639] Castor's Information Memorandum advised readers that the company's policy was that «*loans are not to exceed 75% to 80% of the estimated market value*».

[2640] Many of the cash flows of the DT Smith projects, particularly those generated for the second half of 1990 and into January and February, 1991, reflected a loan to value ratio approaching, and even exceeding, 100%.[2897] Smith testified: «*... that means that we're not going to recover our loans from the sale of the units*», an indication that the project is headed for a loss.[2898]

[2641] Commissions charged by CHIO to the DT Smith group for 1988, 1989 and 1990 totalled US$27,950,000. Selman acknowledged that $15 million of those commissions were not recorded or recognized as income.[2899] Selman opined that, if C&L had noted the discrepancy between the amount of income earned by CHIO from the DT Smith commissions according to the contracts and the amount recognized as income, they should have asked for an explanation of it.[2900] In fact, C&L did note this discrepancy, as indicated in a June 13, 1990 fax from C&L in Cyprus to the attention of Bänziger, who replied on July 22, 1990 that he could not comment thereon.[2901] When confronted with evidence of payments apparently made to "D.T. Smith" and "D. Smith" from that

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[2897] See, for example, (i) Re: Dove II, PW-1114-16; PW-1114-19; (ii) Re: Dove I, PW-1115-13; (iii) Re: Laguna II, PW-1116-17; (iv) Re: San Marcos, PW-1117-6; PW-1117-8.
[2898] R. Smith, June 10, 2008, p. 174.
[2899] Selman, June 8, 2009, p. 134.
[2900] Selman, June 8, 2009, pp. 159-161.
[2901] PW-1530B; PW-1530.

account, Selman agreed that he would consider it unusual for Castor to be making payments to the CEO of a borrower that's indebted to Castor for $238 million.[2902]

[2642] At the time of performing the audit, Ford was not aware that each and every one of the DT Smith construction projects was far behind schedule in terms of both completion of construction of houses and rate of sales. C&L should also have determined the status of the D.T. Smith construction projects, but did not do so.

[2643] Moreover, Ford was not aware of the agreements with Eton Properties, whereby 50% of the profits realized from the DT Smith projects would be paid over to Eton.[2903]

[2644] In executing her work for the 1990 audit of the DT Smith loans, Ford was not aware that houses were never sold at anywhere near the projected rate, as set out in the cash flows and in the loan documentation, and that the ones that were sold from the second half of 1990 onwards were for prices far below what had been budgeted for. She did not "look at" whether houses that had been budgeted to sell for $300,000 were, in fact, selling for $190,000.[2904]

[2645] Ford did not compare actual sales to projected sales.[2905] She did not know if there were any sales reports in Schaan or Zug (where she performed her work) with respect to the DT Smith projects.[2906]

[2646] She confirmed that, at the time of her audit work she did not have a good understanding of real estate market conditions in California[2907] and did not consider it necessary to ask.[2908] More significantly, she was not aware of the auctions held in the DT Smith projects.[2909]

[2647] On discovery, when asked what valuation information was available if there was no appraisal, she replied: «*...you have valuation from the security of the promissory notes that were issued. You have a Loan Agreement that states the value of those loans*». She also testified that in instances where no appraisal was available, she saw no necessity for doing additional audit work.[2910]

[2648] At trial, Ford testified that she considered the promissory notes to be security for the loans and that she had no financial information about the borrower, or issuer, of the promissory note, but that she had a *«build-up of evidence - - from 1988 to 1989 to*

[2902] Selman, June 8, 2009, p. 158.
[2903] The agreements between Eton Properties and the DT Smith companies have been produced as PW-1405 – PW-1411.
[2904] Ford, December 8, 2009, p. 138-141.
[2905] Ford, December 8, 2009, pp. 142, 170-171.
[2906] Ford, December 8, 2009, p. 144.
[2907] Ford, December 8, 2009, p. 145.
[2908] Ford, November 7, 1995, pp. 265-266.
[2909] Ford, December 8, 2009, p. 152.
[2910] Ford, November 7, 1995, pp. 53-54.

1990, that demonstrated that these loans (i.e. the DT Smith loans) *were progressing, that they were coming to fruition and as time went on, I had no reason to doubt that the security that was given in the promissory note was a valid security.»*[2911] In cross-examination, Selman stated that in his opinion «*... the number (i.e. the stated dollar amount) on the promissory note is evidence of the existence of the debt, it's nothing more. So, nobody could take it as representing value per se.*»[2912]

[2649] At trial, Ford stated that she could not «*recall at this moment*» if she had compared the actual sales results with projected sales for any of the DT Smith loans.[2913] She acknowledged there was no evidence in her AWPs that she had looked at the number of sales for the projects.[2914]

[2650] Ford testified that when she performed her audit work, she was not aware that all records of actual sales, including sales reports, were kept in Castor's files in Montreal.[2915]

[2651] She said she had never been advised, either by Wightman or by Jean Guy Martin, that Smith was the contact person for the DT Smith loans or that the documentation for such loans was located in Montreal. She had no recollection that Jean Guy Martin had requested her to communicate with Ron Smith with respect to the overseas loans.[2916] Neither Smith nor any members of his mortgage department ever met with any C&L representatives with respect to the loans to the DT Smith companies, nor were they ever asked to provide C&L with any information.[2917]

[2652] Ford was not aware that only 70 units out of the 156 of the Wood ranch II project had been sold, of which 44 had been sold at auction at a much lower price than that which had been achieved prior to the auction.[2918]

[2653] For the Dove I and II project, she testified that she made no enquiries as to how many sales had been made: she did not compare actual sales to projected sales, and she looked at no sales reports.[2919]

[2654] In respect of Chino Hills, for year-end 1990, Ford's working paper[2920] indicates an appraisal value of $31,450,000 (representing the completed sell-out value of the project as per the appraisal report of 1988). Once again, Ford had no idea what prices had been achieved, and what units had been sold. She testified that such information

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[2911] Ford, December 8, 2009, pp. 159-160.
[2912] Selman, June 4, 2009, p. 95.
[2913] Ford, December 8, 2009, pp.. 170-171.
[2914] Ford, December 10, 2009, pp. 6-8.
[2915] Ford, December 8, 2009, p. 171.
[2916] Ford, December 9, 2009, pp. 127-128.
[2917] R. Smith, June 10, 2008, pp. 39-40.
[2918] Ford, December 9, 2009, pp. 27-28; R. Smith, June 11, 2008, pp. 41-42.
[2919] Ford, December 9, 2009, pp. 55-57.
[2920] PW-1053-81, seq. p. 78.

was not available to her (although she had previously testified that sales results formed part of the draw requests that she looked at), and she was unaware that the entire portfolio of loans from CHIO to the DT Smith companies was run entirely out of Montreal.[2921]

[2655] Ford admitted that there was no evidence in her AWPs that would establish that the appraisal value of $31,450,000 was the appropriate value to inscribe. She acknowledged that «*there is no separate working paper that shows any valuation work besides the comparison of the appraisal value to the loan balance at that date.*»[2922] Selman acknowledged it was not sufficient.[2923]

[2656] In respect of the San Marcos project, the 1990 AWPs prepared by Ford record that once again the maturity date has been extended (to November 30, 1991). Apart from recording the amount of the loans outstanding, Ford performed no audit work to value these two loans.[2924] She testified that she was unaware as to the status of sales. None of that information was available to her in Schaan: «*nothing was ever shown to me with respect to those loans.*» She sustained she had never been advised that the sales reports and other documentation supporting the progress of the DT Smith projects were retained in Montreal.[2925]

[2657] In respect of the Laguna II project, once again, the AWPs record that the maturity dates for the two loans for this project were extended from the original date of December 31, 1989: firstly to December 31, 1990, and then to December 31, 1991. Nothing evidenced audit work performed to value the loan or the security or the progress of this project in the AWPs. Ford was not aware as to the status of sales. She did not know that the prices at auction were far below the hopes of DT Smith. Her answer was: «*That information was not available to me in Schaan.*»[2926]

[2658] Ford was unaware that the Circle R Ranch project (like all other DT Smith pre-development projects) had been put into a holding pattern by year-end 1990, to be reviewed again in the summer of 1991, and that nothing had been done with this project as at December 31, 1990

[2659] No evidence in her AWPs attested to a follow up to see if an appraisal had been obtained for Rancho Parcel II: [2927] Ford's AWPs[2928] indicate that an appraisal had been received for Rancho Parcel V, but no similar indication for Rancho Parcel II.

[2921] Ford, December 9, 2009, pp. 64-65.
[2922] Ford, December 9, 2009, p. 67.
[2923] Selman, June 4. 2009, pp. 40-42, 63-64.
[2924] PW-1053-81, seq. p. 78; Ford, December 9, 2009, p. 77.
[2925] Ford, December 9, 2009, pp. 82-83.
[2926] Ford, December 9, 2009, pp. 90, 93.
[2927] Ford, December 9, 2009, pp. 111, 115, 118, 120.
[2928] PW-1053-81, seq. p. 78.

[2660] As to the Ritz Pointe project, Ford was not aware that the project had been placed into a holding pattern and that there was litigation with the municipality relating to density and the number of units that could be built.[2929] However, in her audit working paper she noted: «*Request update of additional security; loan balance exceeds appraisal value.*»[2930] Notwithstanding such a note, Ford was unable to identify evidence in her AWPs of any details with respect to an updated appraisal, such as the date, the state of the property, the value set out in the appraisal, or anything else.[2931]

[2661] In respect of Rancho California project, Ford confirmed that no additional audit work was done (over and above what she claims to have done for year-end 1989) to support using the higher appraisal value of $33.2 million.[2932] Her AWPs[2933] record that the maturity date for this loan was extended to July 31, 1991; Ford was not aware that virtually none of the offsite costs to improve the site ready for finished lots (ready for construction) had been incurred.[2934]

[2662] In respect of the Walker Basin project, the working papers for 1990 contain Ford's following notations: *«Secured promissory note $13,000,000»* and *«Assignment of Trust Deeds $5,000,000 and $5,180,000»*.[2935] There is no reference as to whether the "Secured Promissory Note" is from the borrower and Ford has no recollection as to who issued the promissory note.[2936]

[2663] Ford's working paper does not record the rank of the two trust deeds, although C&L's audit program included a determination of the rank of a mortgage and the amount of any prior ranking debt.

[2664] Ford failed to note that the $5 million trust deed, which was assigned to Castor, ranked behind a first mortgage of $5.18 million in favour of a third party. There is no reference as to who the prior ranking creditor was.

[2665] Ford failed to select the Walker Basin loans for review, even though such loans had increased by $7 million, the maturity date had been extended to July, 1991, and no appraisal was available for the previous year's audit. In her words: *«Not having an appraisal report or not following up on the appraisal report did not trigger any particular concern.* »[2937]

[2929] Ford, December 9, 2009, pp. 138, 140.
[2930] PW-1053-81, seq. p. 78.
[2931] Ford, December 9, 2009, pp. 141-142.
[2932] Ford, December 9, 2009, p. 160.
[2933] PW-1053-81, seq. p. 81.
[2934] Ford, December 9, 2009, p. 161; R. Smith, June 11, 2008, p. 115.
[2935] PW-1053-83, seq. p. 121.
[2936] Ford, December 9, 2009, pp. 163-164.
[2937] Ford, December 9, 2009, pp. 187-188.

Information C&L knew or could have known, had they comply with GAAS

[2666] The information available or that could have been available to the auditors to complete their audit, to estimate the loan loss provisions and to assess whether revenue had reasonable assurance of collectability, had they comply with GAAS, has been identified during testimony of Plaintiff's experts, and is documented in Plaintiff experts' written reports.[2938]

[2667] In the following paragraphs, and before she starts discussing the issue of fraud, the Court only draws-up a non-exhaustive wrap-up of what C&L knew, should have known or could have known about Castor's borrowers and their relationships with Castor, and about the performance, the collectability and the carrying value of Castor's loans, had they complied with GAAS.

YH group and YH Corporate loans

[2668] Stolzenberg and Wersebe were long time business partners. From 1978 and until 1987 when Wersebe transferred his Castor's interests to Stolzenberg, both were heavily involved in Castor's business and affairs. From the early 80s, they were also involved together in MLV.

[2669] After 1987, Stolzenberg became the mastermind of Castor, and Wersebe concentrated on the YH Group activities.

[2670] Interest and fees on the Castor's loans to the YH group were seldom, if ever, paid in cash: they were systematically capitalized[2939], as the accounting books disclosed.[2940] This was the case notwithstanding the loan covenants that called for monthly payments of interest. Capitalization of interest was unplanned.

[2938] For example, in the case of MLV : PW-2908, Vol. 2, A-3 to A-19 (1988), A-20 to A-29 (1989) and A-30 to A-36 (1990); PW-2941, Vol. 3, pp. 4-8, 55-59 (1988-1990); PW-3033, Vol. 2, Appendix D, pp. 1 to 48 (1988-1990). For the other projects, see the other chapters of PW-2908, vol.2, the various volumes of PW-2941 and the other appendices of PW-3033, vol. 2.

[2939] For examples: the interest on a series of loans to YHDL was being capitalized each month to account 046/Loan 1153(PW-87). Interest on the YHDL portion of the Meadowlark loan was being similarly capitalized until 1990 (see PW-1112G, analysis of Ron Smith relying on PW-167, PW-103 and PW-85, p. 673 and PW-86, p. 587. This appears every month in the General Journals.). YHDL's guarantee of the MLV debenture holders' obligations to CHIF was satisfied in a similar fashion through the inter-company Zug/Enar account (PW-100, pp. 41, 47)

[2940] PW-2908, Vol. 1, p. 5-12; PW-1485R; Vance, March 6, 2008, pp. 147-155.

[2671] In December of each year, Castor and YH proceeded to a year-end reallocation from account 046. Existing loans and new loans were part of these reallocations, as the General Journal shows.[2941]

[2672] The commitment letters and loan agreements (which C&L supposedly reviewed) called for audited and unaudited financial statements of the borrowers to be provided to Castor.[2942]

[2673] Castor's borrowers had no choice but to provide those financial statements. In turn, Castor had to make those documents available to C&L, when asked. Without SAAE, which necessarily includes financial statements of Castor's borrowers, C&L could not issue and should not have issued an unqualified audit report.

[2674] In 1987, C&L obtained audited financial statements of YHDL as at September 30, 1986: they are included in the 1987 AWPs.[2943] No subsequent audited financial statements of YHDL were issued thereafter. C&L should have asked why.

[2675] Constantly, Castor had to offer financial support to allow YH to meet its overhead and other expenses (as the correspondence files and loan ledger cards show). C&L should have asked why. At first glance, save for financial difficulties the borrowers were going through or an undisclosed related party relationship, making loans stipulating that the interest should be paid monthly and renewing them each year to reallocate unpaid interest, fees and support payments made little commercial sense, if any.

[2676] Evidence as to the financial condition of the borrowers, the net worth of the guarantor, Wersebe, and the nature and enforceability of the securities held by Castor was essential. Without receiving and reviewing current financial statements of YHDL, YHDHL, KVWIL and related borrowers, C&L could not comply with its obligation to gather SAAE in relation to the YH corporate loans.

[2677] Finally, cash from these borrowers had not been collected for years, and was not collected during the first eleven months of 1990, but $40 million came in at year-end 1990. C&L should have investigated how and why.

[2941] PW-84, bates p. 000573 (1988); PW-85, bates p. 000566 (1989); PW-86, bates p. 000485 (1990). In 1990, Account 046 became loan #1153, part of account 065, but there was no change to how the YH interest was treated

[2942] For example, PW-1058-1, PW-1063-1, PW-1054-3-1, PW-1059-6

[2943] PW-1053-27, seq. pp. 164-172

TSH

[2678] The loans to Topven, Topven (1988) and Lambert were connected to the TSH.

[2679] There were TSH-related loans in the Montreal portfolio and in the overseas portfolio.

[2680] Aggregation of all those loans was a must: C&L needed to act, to exercised professional judgment, based on a "*global picture*".

[2681] The loans were made and renewed since the early 80s without any credit review of the borrower. At first glance, this made little commercial sense, if any.

[2682] The loan documents required the monthly payment of interest, annual fees and annual financial statements. Castor's borrowers had no choice but to provide Castor with financial statements. In turn, Castor had to make them available to C&L, when asked. Without SAAE, which necessarily includes financial statements of all the borrowers related to the TSH, C&L could not issue and should not have issued an unqualified audit report.

[2683] Although the TSH was an operating property and should have been able to service its debts, interest was being capitalized on the Topven loans[2944] contrary to the loan agreements, and on the Lambert loans contrary to its loan documents, at least as early as 1984.[2945] Capitalization of interest was unplanned.

[2684] Castor was paying fees and operating expenses of borrowers (as the mortgage and loan ledger cards clearly show).[2946]

[2685] The audited financial statements of Topven included in previous years' AWPs disclosed the rapidly increasing losses being reported by this entity. C&L should have continued to obtain such financial statements or determine why they were no longer available.[2947]

[2686] The 1987 Restated Operating Results for Topven, provided by Castor to C&L for the 1987 audit, disclosed income before debt and depreciation of only $2.9 million.[2948]

[2687] The actual financial results of the hotel were below the projections on which the available appraisal was premised.[2949]

[2944] PW-1081A

[2945] PW-1053-3, sequential page 477

[2946] PW-167D.

[2947] See PW-424, PW-429, PW-430

[2948] D-138-1: Summary Income Statement entitled "Topven Holdings Ltd. 1987 Restated Operating Results" and Proforma Income Statement – 1988 Budget. See also PW-1053-93, sequential pages 153-154 (B28A and B28B).

[2688] Castor was assuming 100% of the financing risk for the TSH loans, contrary to the loan-to-value ratio of 75-80% in its promotional materials.[2950]

[2689] At first glance, and save for financial difficulties the borrowers were going through or an undisclosed related party relationship, there was little commercial sense, if any, to make loans and to renew them each year (increasing therefore Castor's exposure) to reallocate unpaid interest, fees and support payments.

CSH

[2690] The loans to Skyeboat, 321351 and Skyview were connected to the CSH.

[2691] There were CSH-related loans in the Montreal portfolio and in the overseas portfolio: all loans needed to be aggregated.

[2692] The CSH project had been on Castor's books since the early 80s and was refinanced in 1988.[2951]

[2693] As at year end 1987, the loans already amounted to $49.3 million,[2952] plus a contingent liability of $3.6 million and accrued interest receivable. Consequently, even before the 1988 refinancing, Castor's exposure exceeded the lower range of the estimate of value provided in an available appraisal or market study report (PKF).

[2694] The loan documents required payments of interest and placement fees, and remittance of annual financial statements of Skyview. Interest and placement fees were capitalized, and no financial statements were available. Why?

[2695] Castor's borrowers had no choice but to provide financial statements. In turn, Castor had to make them available to C&L, when asked.

[2696] The financial statements of Skyview, Skyeboat and 321351 all disclosed significant losses.

[2697] The financial statements of the CSH disclosed actual results far below the projections of income that the value in the appraisal was based on.

[2698] The appraisal assumed renovations, the cost of which would have to be deducted from the appraised value, to determine what amount was available as

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[2949] Given that C&L would have seen that this value estimate existed if they had read the Gillis appraisal, the Court rejects the suggestion that the information was concealed.

[2950] PW-2941, Vol. 2, p. 10.; see also PW-1057-1, PW-1057-2 and PW-1057-3

[2951] Ron Smith September 5, 2008, pp. 147-148; PW-1053-23, seq. p. 168

[2952] Based on the audit confirmation returned to C&L, PW-1053-27, seq. pp. 215-218, 230-231 (E212–E215, E227–E228)

collateral. The planned renovations were not realized even though the appraisal assumed that the renovations would be completed by February 1988.

[2699] Castor was assuming 100% of the financing risk for the CSH loans, contrary to the loan-to-value ratio of 75-80% that it asserted in its promotional materials.[2953]

[2700] Again, and save for financial difficulties the borrowers were going through, or an undisclosed related party relationship, nothing justified why loans were being made and renewed each year to reallocate unpaid interest, fees and support payments to a business in operation, which was neither a project under construction nor a project under development.

OSH

[2701] The loans associated with the OSH were in default, non-performing and the project was in severe financial difficulty. Castor was curing all such defaults from its own resources. Why?

[2702] Interest on loan 1049 was capitalized on a monthly basis to account 046.

[2703] Placement fees, interest, advances and legal fees on loan 1152 were all capitalized.[2954]

[2704] Interest on loan 1166 and on the transferred loan of 687292 was capitalized[2955] together with all placement fees, advances and legal fees.

[2705] Under the terms of the loans, the borrower had to provide annual financial statements, revenue and expense statements, rent rolls and statement of capital expenditures when requested by Castor; the borrower had to pay all accounts payable and taxes owing on the lease and FF&E, when due. [2956] None of these covenants was being fulfilled, in addition to the failure to pay interest and fees, when due. Why?

[2706] The expenditures upon which the Fitzsimmons appraisal had been premised had not been done: was the proposed value still reasonable?

[2707] Having and looking at financial statements of borrowers was a must.

[2708] Again, and save for financial difficulties the borrowers were going through, or an undisclosed related party relationship, nothing justified why loans were being made and renewed each year to reallocate unpaid interest, fees and support payments to a

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[2953] PW-2941, Vol. 2, p. 131
[2954] PW-167W
[2955] PW-167X
[2956] See for example PW-1093-1

business in operation, which was neither a project under construction nor a project under development.

MLV

[2709] There were MLV-related loans in the Montreal portfolio and in the overseas portfolio.

[2710] Aggregation of all those loans was a must: C&L needed to act, to exercise professional judgment, based on a "*global picture*".

[2711] The payment of interest and of renewal fees was not made from the cash resources of any borrower.

[2712] General Journal entries were made each month to document the capitalization of interest on the debenture holder loans to the inter-company account.

[2713] The yellow card for loan 1105[2957] documented the capitalization of interest due on loans 1126 and 1105.

[2714] The monthly journal memos documented that interest on loan 1048 was capitalized to account 046/loan 1153, on a monthly basis.

[2715] Castor was funding MLVII's interest obligations to the debenture holders primarily through account 046.

[2716] The terms and conditions of the commitment letters and extension letters, as well as the loan documentation in connection therewith, called for the payment of monthly interest, annual fees and for the supply of financial information. The borrowers were in chronic breach of all of such covenants. Why?

[2717] The loan documents required the payment of interest and fees, and the remittance of annual financial statements. Castor's borrowers had no choice: they had to provide Castor with financial statements. In turn, Castor had to make those financial statements available to C&L, when asked. Without SAAE, which necessarily includes financial statements of all the borrowers related to MLV, C&L could not issue and should not have issued an unqualified audit report..

[2718] Real estate taxes were constantly in arrears, and Castor was obliged to advance funds at the last minute to pay the taxes in order to avoid a tax sale (Loan 1105).[2958] Late payment of taxes is documented on the draft 1987 financial statement of MLVII, included in the 1988 AWPs.

[2957] PW-1074-3A

[2958] Ron Smith, May 14, 2008, pp. 139-140, 183

[2719] The exposure of CHL to the MLV project included loan 1048 to YHLP, in the amount of $14 million, and loan 1125 to KVWIL, in the amount of $7.2 million.

[2720] The operations of the MLV project were seasonal with the peak occupancy period in July and August and minimal occupancy during the winter months.

[2721] The 7th draft of the unaudited financial statements of MLVII revealed substantial operating losses in the context of and notwithstanding the very significant financial support from York Hannover related entities.[2959]

[2722] The appraisal used by the audit staff in 1988 was over 5 years old and assumed major renovations which had not been made.

[2723] The value in the Hughes appraisal,[2960] dated July 1988, was only $67.7 million without renovations.

[2724] A sale of the MLV project for a price between $90 million to $100 million (which is reflected on AWP E41[2961]) would have resulted in a very significant loss to Castor.

[2725] Statements made to Wightman during the year-end wrap up meeting of the 1986 audit,[2962] regarding refinancing, sale of the project and reduction of the MLV loans, had failed to materialize.

[2726] The Mellon Bank financing did not go through. Why had this desperately needed[2963] refinancing aborted?

[2727] Significant operating deficits were funded by Castor[2964] and the operations of the MLV project had significant problems.[2965] Castor was obliged to make systematic and ongoing support payments to lenders in an attempt to stave off foreclosure.[2966]

[2728] Again, and save for financial difficulties the borrowers were going through, or an undisclosed related party relationship, nothing justified why loans were being made and renewed each year to reallocate unpaid interest, fees and support payments to a business in operation, which was neither a project under construction nor a project under development.

[2959] PW-1053-23, seq. pp. 155-166; Ron Smith, May 16, 2008, pp. 83-89.
[2960] PW-494, bates p. 000008
[2961] PW-1053-23, seq. p. 117
[2962] PW-1053-3, seq. p. 474
[2963] See the going concern note in the draft 1987 MLVII financial statement based on the realization of such financing.
[2964] PW-1070H
[2965] See, for example, PW-1070G-2, PW-1070G-3, PW-1070G-4
[2966] See, for example, PW-1070F-2, PW-1070F-4, PW-1070F-5

MEC

[2729] The loan documentation indicated that Stolzenberg was the incorporator and director of 97872. This information was contained in the closing binders which were made available to C&L.

[2730] The loan documentation for the various loans indicated the cases where interest was payable monthly.

[2731] It was obvious from the review of the yellow cards[2967] and the General Journals that interest was being capitalized each month either to account 046 or to the equity loans 1145 and 1042.

- The General Journals that were available to Castor indicated that interest on loan 1042 was being capitalized each month to account 046.
- The General Journals disclosed that the year-end increases to loan 1042 were utilized to reclassify unpaid interest on account 046.

[2732] The disbursement of the loans was conditional upon obtaining legal opinions as to the validity of the security. In respect of the equity loan to YHDL, loan 1042, the commitment letters called for the provision of legal opinions regarding the validity of the security. Had C&L sought such legal opinions, it would have ascertained that no security had been registered in 1988 and 1990 in respect of loan 1042 and that in 1989, the security was limited to a principal sum of $14 million even though the loan amount was $24 million.

[2733] Legal opinions were available or should have been sought to ascertain whether the equity loans were secured by mortgages. In fact, loan 1145 was never secured by any mortgage in favour of Castor; rather, the only alleged "security" it held was a promissory note.

[2734] According to the commitment letters, 97872 undertook to provide annual and interim financial statements.[2968]

[2735] In the case of the second mortgage financing, the commitment letter specifically provides that each of 97872 and YHDL were required to provide audited annual

[2967] PW-167
[2968] PW-1103-5

financial statements as well as various other financial information regarding the projects.[2969]

[2736] Castor's borrowers had no choice: they had to provide Castor with financial statements. In turn, Castor had to make those financial statements available to C&L, when asked. Without SAAE, which necessarily includes financial statements of all the borrowers related to MEC, C&L could not issue and should not have issued an unqualified audit report.

[2737] C&L could have and should have ascertained whether the borrowers were satisfying their obligations to the BMO syndicate. C&L would have realized that the borrowers were not providing the equity contributions required from their own resources.

[2738] The loan documentation revealed that the project had a budget of $195 million and a completion date of January 31, 1990.[2970] The commitment letter called upon the borrowers to provide reports from the project monitor with each draw request. C&L could have and should have sought copies of the reports prepared by Helyar which indicated the extent of the cost overruns. In the same commitment letter[2971] the borrowers covenanted to «*promptly fund any cost overruns over $10M*». In fact, the cost overruns exceeded $100 million and such deficiencies were funded by Castor.

[2739] To the extent that C&L was relying on the possibility of a new appraisal being issued to overcome the security deficiency that they themselves determined for the 1990 audit, it was incumbent upon C&L to seek and obtain SAAE to justify accepting that such a new appraisal (between $300-350 million) would be issued. Had C&L insisted upon receiving an updated appraisal from Royal Lepage, it would have readily ascertained that, rather than increasing, the appraised value of the MEC had significantly decreased. Royal LePage did appraise the MEC at $241 million, as of September 1, 1990.[2972]

[2740] Palace II undertook to provide annual financial statements, revenue and expense statements and other financial information.[2973] The commitment letter called for Palace II to pay interest to CHIF. A review of the mortgage and loan ledger card in Montreal for loan 1146 clearly revealed that all interest and fees on the CHIF loan were being capitalized to a grid note in Montreal.

[2969] PW-1102A-3
[2970] PW-1102A-4
[2971] PW-1102A-4, p. 9 of Mortgage Loan Summary
[2972] PW-1108B
[2973] PW-285

TWTC

[2741] More than sufficient evidence was available to C&L to ascertain that the TWTC loans were non-performing and that the borrowers were in default of their loan covenants.

[2742] Had C&L competently reviewed the loan documentation, the General Journals evidencing the capitalization of interest to account 046/Loan 1153, the yellow cards for loans 1046 and 1149, and insisted upon receiving the financial statements that were called for in the loan agreements, C&L would have readily ascertained the problems associated with these loans.

[2743] Castor's borrowers had no choice but to provide Castor with financial statements. In turn, Castor had to make them available to C&L, when asked. Without SAAE, which necessarily includes financial statements of all the borrowers related to the TWTC, C&L could not issue and should not have issued an unqualified audit report.

[2744] Moreover, had C&L sought information regarding the use of the loans advanced by C&L, and determined the amount of prior ranking debt at the project level, C&L would have ascertained that Castor's position was highly precarious, especially in view of the fact that it could not register its security.

[2745] Furthermore, had C&L sought SAAE such as the alleged "offers" received for the TWTC lands, they would have ascertained that no offers had been received but, rather, merely a brokerage mandate had been granted to Coldwell Banker. They should have furthermore sought information as to why such mandate was being relied upon 14 months later for the 1990 audit when no sale had occurred, and when clearly the market value for the property was far below that which had been indicated on the LEQs.

[2746] Finally, once C&L ascertained the high risk nature of loan 1149, it should have sought information regarding each of the TWTC loans and, had it done so, would have been compelled to insist that those loans be placed on a non-accrual basis and no revenue recognized in connection therewith.

Meadowlark

[2747] Interest was capitalized in 1988 and 1989, 50% to account 046 and 50% to the Raulino grid note: this was fully disclosed in the books and records of Castor including the General journal entries each month[2974].

[2748] The borrowers were not complying with their loan covenants.

[2749] Castor's borrowers had no choice but to provide Castor with financial statements. In turn, Castor had to make them available to C&L, when asked..

DT Smith

[2750] All required information was available for C&L to review had they interacted with Ron Smith: loan files, correspondence files, security files, draw requests, cash flows, appraisals and financial statements.[2975]

[2751] Ron Smith was managing the DT Smith loans, and was the person to communicate with to obtain information relating thereto. As a matter of fact, Wightman thought and expected that Ford would discuss the DT Smith loans with Ron Smith.[2976]

[2752] Castor's borrowers had no choice but to provide Castor with financial statements and financial information. In turn, Castor had to make them available to C&L, when asked. Without SAAE, which necessarily includes financial information relating to the DT Smith projects, C&L could not issue and should not have issued an unqualified audit report.

[2974] PW-103; PW-1112G

[2975] Ron Smith, June 10, 2008; see for example: PW-1113C, PW-1113D, PW-1113E, PW-1113F, PW-1113H, PW-1114 (binder); PW-1115 (binder); PW-1116 (binder)

[2976] PW-1053-81-2, PW-1053-83-5, PW-1053-84-5; Wightman, February 10, 2010, p. 43-44

Fraud is not a defense in the circumstances

Positions (in a nutshell)

Defendants

[2753] If the Court concludes that their consolidated audited financial statements are materially misstated and misleading, C&L asserts they should not be held liable because they were victims of fraud and misrepresentations by management: fraud prevented the detection of misstatements.

[2754] Defendants argue that Castor deliberately concealed relevant information from them, that Castor's conduct in the context of the audit was fraudulent.

[2755] Defendants submit that the fraud was primarily intended to conceal from C&L the complete nature, extent and performance of the YH Group of loans with Castor, Castor's dealings with related parties, the $100 million debenture and the restricted cash.

[2756] Defendants describe the components of such fraud as follows:

> intentional omissions and deliberate misrepresentations to the auditors relating to such financial statements matters as: 1) the relationship between Castor and its borrowers; 2) restrictions on Castor's assets; 3) false representations to C&L made by third parties by way of false confirmations; 4) the payment of fraudulent fees in connection with Castor's loans; 5) the German bank window dressing transactions; 6) the diversion of loan renewal fees paid by DT Smith; 7) the $100MM debenture; 8) management's appraisal and knowledge of Castor's loans and the status of its borrowers; 9) the use of year end circular transactions to improve the performance of the loans; and, 10) the back dating of documents and loan agreements by the creation of fictitious agreements and transactions.[2977]

[2757] Defendants argue the Court must consider the impact of fraud on the planned scope and probable results of a GAAS audit.

[2758] Defendants suggest that evidence shows that C&L were deprived of the opportunity to exercise their professional judgment on a full set of facts.

[2759] Defendants allege that the fraud committed by Castor management and others was such that the normal application of GAAS would not have uncovered the alleged departure from GAAP.

[2977] Defendants written submissions, July 8, 2010, p. 209

Plaintiff

[2760] Plaintiff says:

- Information to perform an audit in accordance with GAAP and GAAS was accessible to C&L or could have been accessible to C&L, had C&L requested it as it should have; and
- Information that should have raised concerns, "red flags", was seen by C&L or mentioned by C&L in their audit working papers, but C&L negligently failed to act on it.

[2761] Plaintiff argues if C&L had performed their audit work and prepared their other work products in conformity with GAAP, GAAS and other applicable professional standards, unqualified audit reports and consolidated audited financial statements, and valuation letters and Certificates for Legal for Life Opinions, like the ones issued by C&L, would not have been and could not have been issued.

[2762] Consequently, Plaintiff pleads it is irrelevant whether there was a fraud or not given C&L's negligence, C&L's numerous failures to act in accordance with GAAP, with GAAS and with the other professional standards applicable to them or to their work.

Court's conclusion

[2763] In the circumstances revealed by the evidence, and even though fraud might have been a barrier to the auditors identifying irregularities, the alleged fraud and misrepresentations by Castor's management cannot serve to relieve C&L of the responsibility arising from their improper and deficient performance as accountants and auditors.

Fraud: definition

[2764] The CICA Handbook, as it read in 1988, 1989 and 1990, defines error and fraud at section 5300.43, as follows:

> **Error** refers to **mistakes** affecting the financial statements s uch as:
>
> (i) arithmetical or clerical mistakes;
>
> (ii) misapplication of accounting principles; and
>
> (iii) the oversight or misinterpretation of facts;

> **Fraud** refers to **acts committed with an intent to deceive** involving either misappropriation of assets or misrepresentations of financial information either to conceal misappropriations of assets or for other purposes, by such means as:
>
> (i) manipulation, falsification or alteration of records or documents;
>
> (ii) suppression of information, transactions or documents;
>
> (iii) recording of transactions without substance; and
>
> (iv) misapplication of accounting principles.
>
> (our emphasis)

Fraud and the auditor (1988, 1989 and 1990)

[2765] An auditor does not have the duty to detect fraud, to detect acts committed with intent to deceive.

[2766] An auditor expresses an opinion; he does not give a guarantee.

[2767] *It is the duty of an auditor to bring to bear on the work he has to perform that skill, care, and caution which a reasonably competent, careful, and cautious auditor would use.*[2978]

[2768] *An auditor is not bound to be a detective, or, as was said, to approach his work with suspicion, or with a foregone conclusion that there is something wrong. He is a watchdog, but not a bloodhound.*[2979]

[2769] *Auditors must not be made liable for not tracking out ingenious and carefully laid schemes of fraud, when there is nothing to arouse their suspicion ...So to hold would make the position of an auditor intolerable*[2980] (our emphasis).

[2770] To afford a reasonable basis to support the content of their audit report, according to GAAS, auditors have to obtain sufficient appropriate audit evidence by such means as inspection, observation, enquiry, confirmation, computation and analysis.[2981] Sufficiency and appropriateness are interrelated. Sufficiency is the measure of the quantity of audit evidence obtained and appropriateness is the measure of its quality.[2982]

[2978] *In Re Kingston Cotton Mill Company*, [1896], 2 Ch.279, Lord Lopes, at page 288
[2979] *In Re Kingston Cotton Mill Company*, [1896], 2 Ch.279, Lord Lopes, at page 289
[2980] *In Re Kingston Cotton Mill Company*, [1896], 2 Ch.279, Lord Lopes, at page 290
[2981] For 1988, PW-1419-1A, section 5100 and section 5300.01;For 1989, PW-1419-2A section 5100 and section 5300.01; For 1990,PW-1419-3A section 5100 and section 5300.01
[2982] For 1988, PW-1419-1A, section 5300.09; For 1989, PW-1419-2A, section 5300.09; For 1990, PW-1419-3A, section 5300.09

[2771] One italicized recommendation of GAAS is that *the auditor should perform substantive auditing procedures.*[2983]

[2772] The following factors influenced the auditor's judgment as to what is sufficient appropriate evidence:

- Materiality;
- Inherent risk and control risk consideration;
- The experience gained during previous audit examinations as to the reliability of the client's records and representations;
- The persuasiveness of the evidence; and
- Fraud or error found while performing the audit procedures.[2984]

[2773] The auditor recognizes that financial statements may be misstated as a result of fraud or error.[2985] Accordingly, in obtaining sufficient appropriate audit evidence, the auditor seeks reasonable assurance, through the application of procedures that comply with GAAS, that fraud and error which may be material to the financial statements have not occurred or that, if they have occurred, they are either corrected or properly accounted for in the financial statements.[2986]

[2774] If an auditor fails to adhere to GAAS, he runs a risk of not detecting a misstatement resulting either from error or fraud.

[2775] A failure to discover an error or fraud does not necessarily indicate that an auditor has failed to adhere to GAAS, but he might have.

[2776] When he encounters circumstances such as conflicting evidence on important matters, unusual transactions by virtue of their nature or complexity, particularly close to the year end, information being provided unwillingly or only after unreasonable delay, limitation in the scope of the examination imposed by management or identification of important matters that were previously undisclosed, an auditor shall question himself and wonder if the financial statements might be materially misstated.[2987]

[2983] For 1988, PW-1419-1A, section 5300.08; For 1989, PW-1419-2A, section 5300.08; For 1990, PW-1419-3A, section 5300.08

[2984] For 1988, PW-1419-1A, section 5300.10; For 1989, PW-1419-2A, section 5300.10; For 1990, PW-1419-3A, section 5300.10

[2985] For 1988, PW-1419-1A, section 5300.44; For 1989, PW-1419-2A, section 5300.44; For 1990, PW-1419-3A, section 5300.44

[2986] For 1988, PW-1419-1A, section 5300.44; For 1989, PW-1419-2A, section 5300.44; For 1990, PW-1419-3A, section 5300.44

[2987] For 1988, PW-1419-1A, section 5300.49; For 1989, PW-1419-2A, section 5300.49; For 1990, PW-1419-3A, section 5300.49

[2777] An auditor shall also be alert to the possibility that management lacks good faith when he encounters circumstances such as information being provided unwillingly or only after unreasonable delay, limitation in the scope of the examination imposed by management or identification of important matters that were previously undisclosed.[2988]

[2778] If an auditor suspects the existence of fraud or error, he needs to perform procedures to support or dispel his suspicion. Unless the circumstances clearly indicate otherwise, the auditor is not justified in assuming that an instance of fraud or error is an isolated occurrence.

[2779] The CICA handbook includes the following italicized section: *The auditor should assess the audit implications of all frauds and errors which come to his attention and consider their effect on the financial statements.*[2989]

[2780] While they do not have an obligation of result, auditors have an obligation of means and diligence. Auditors need to be aware of the possibility of material fraud. Auditors have to evaluate the risk of material fraud. They are expected to plan their audits to address the risks. They have to conduct their audits to address appropriately such risks.

[2781] When auditors do not act accordingly, and it is shown that their audit results would have been different had they discharged their obligation properly, auditors engage their professional responsibility.

Experts opinions

Defendants' experts

[2782] Two Defendants' experts expressed comments on fraud: Selman and Levi.

[2783] Selman's comments were general comments. Levi's mandate was specific to the issue of fraud.

Selman

[2784] Selman opined there was fraud, as defined by the handbook, in the 1988, 1989 and 1990 audits.

[2785] Selman suggested to the Court that, for each of the relevant years (1988, 1989 and 1990), she should consider twofold of the fraud issue:

[2988] For 1988, PW-1419-1A, section 5300.56; For 1989, PW-1419-2A, section 5300.56; For 1990, PW-1419-3A, section 5300.56

[2989] For 1988, PW-1419-1A, section 5300.52; For 1989, PW-1419-2A, section 5300.52; For 1990, PW-1419-3A, section 5300.52

- The immediate and specific impact of fraud on any identified section of the audit.

- The general impact of fraud on the audit, as a whole.[2990]

[2786] Selman explained the obligation of an auditor to gather sufficient appropriate audit evidence to meet the objectives of section 5300.17 of the Handbook[2991]. He added that once the auditor has gathered such evidence, he or she stops performing procedures.[2992]

[2787] Selman said that he had set out in his report, at paragraphs 4.1.11 to 4.1.52 and in section 6.3, what he considered to be misrepresentations amounting to fraud in the sense of the Handbook definition.[2993]

[2788] Selman mentioned that a requirement for the auditor to develop auditing procedures that were designed to detect fraud had been brought into the Handbook, as part of a normal audit, but only after the relevant years.[2994]

[2789] Even though he acknowledged that information was in Castor's accounting records, Selman said concealment could exist within the records, by misdirection, an audit not being intended to be a forensic exercise to root out the evidence of fraud.[2995]

[2790] Selman said "*Management has a responsibility to bring forward the information to the auditor that is relevant*" and "*To suggest that if the auditors didn't ask for it, it wasn't concealed or suppressed is, in my view, incorrect from the point of view of an auditor*".[2996]

[2791] Selman wrote :

- "*An auditor is expected to be aware of the possibility that fraud exists within the records that are being audited and that matters under examination are being misrepresented*".[2997]

- "*...an auditor needs to evaluate the information he sees and hears and be reasonably satisfied that it is being appropriately described. And, if he finds something that raises his suspicions he needs to probe further*"[2998]

[2990] Selman, May 5, 2009, pp.70-72
[2991] PW-1419-1A (1988); PW-1419-2A (1989); PW-1419-3A (1990)
[2992] Selman, May 5, 2009, pp. 78-81
[2993] Selman, May 6, 2009, pp.62-63, p. 95, pp.105 and following
[2994] Selman, May 6, 2009, p.66; Selman, May 19, 2009, pp.26-27
[2995] D-1295, p.239; Selman, May 6, 2009, pp.66 and following
[2996] Selman, May 6, 2009, p.121
[2997] D-1295, p. 228
[2998] D-1295, p. 230; Selman, May 6, 2009, pp.82-83

[2792] Asked to comment on the methodology and on the tapestry analogy used by Froese, one of Plaintiff's experts (the relevant extract of the testimony of Froese is reproduced later under the subheading "*Froese*" of this section), Selman said it was an interesting analogy, but that he had never seen that methodology used before.[2999]

[2793] Selman opined that account 046 was "*a normal and usual procedure*".[3000] He added "*I do not view either account 046 or these journal entries as being fraudulent in their nature or intention to conceal*".[3001]

[2794] When saying that the auditors had not been told something, Selman took for granted that, if they had been told, they would have made a note and written something, to that effect, in their audit working papers.[3002]

> and, once again, just to reiterate the code since maître Fishman wasn't here when I explained it, **when I say that they were not told, I mean that** I have not seen any evidence that they were told something which **I would have expected they would have recorded in the working papers** or otherwise would have dealt with had they...
>
> I am just simply saying that when I say that (inaudible) were not told, it's because I haven't seen any evidence that they were told in the working papers, and I do this **where I see things that I'd believe are of such significance that they would have been recorded in the working papers** or otherwise dealt with by the auditors.
>
> (our emphasis)

[2795] Selman summarized his views on management's representations as follows:

> In simple terms, the assumption is that management genuinely wants to present financial statements that are in accordance with GAAP. This is the normal experience. Contrary to suggestions otherwise, it is very rare that management wants to produce financial statements that are wrong.
>
> Now, we've talked a bit, and there's been a good deal of discussion in the case about management representations. The proper description, I think, is this. A representation by management is **not sufficient audit evidence in itself.** Management representations **include not only the representations contained in the financial statements and the formal written representations**, such as the year-end representation letter, **but the assertions and explanations about particular transactions, or in cases like this, about carrying values of assets** that he received from management. All of these are representations.

[2999] Selman, May 6, 2009, pp.76 and following
[3000] Selman, May 7, 2009, p. 23
[3001] Selman, May 7, 2009, p. 25
[3002] Selman, May 7, 2009, pp. 29-30

> **They usually require corroboration**. (...)
>
> The **representations often take the form of accounting estimates**. In the context of this case, the most significant of these accounting estimates were management estimates of Castor's loan loss provisions. So, the auditor's objective in respect to these estimates is to obtain sufficient appropriate audit evidence that provide reasonable assurance that the estimates are reasonable within the context of the financial statements as a whole, and if we look at handbook section 5305.08, we see that that is the manner in which the handbook sets it out.[3003]

[2796] On the topic of scepticism, Selman summarized his views as follows:

> So, to balance off the assumption of management's good faith, the auditor is expected to maintain an attitude or professional scepticism and in my report, I referred to the Russian proverb "Trust but verify", "doveryai, no proveryai". I lifted it, as it were, from a speech of Ronald Reagan on arm's limitation treaties. I understand he lifted it in turn from Damon Runyan (ph.), but it sets out this balancing issue of on one hand, accepting what you're being told and on the other hand, verifying it to some degree.
>
> So, it's usually described as assessing the validity of the evidence obtained and being alert to evidence which contradicts the assumption of management's good faith. Being alert does not mean being obsessively sceptical or suspicious.[3004]

[2797] Selman described the attitude an auditor had to have in 1988, 1989 and 1990, as follows: *to be alert to the possibility that fraud existed or alert to contradictory evidence, and he needs to increase, he needed to increase the depth of the audit work that was done if there was a significant indication of the existence of fraud*.[3005]

[2798] During his testimony, Selman qualified Stolzenberg as "a crook".[3006]

[2799] In his cross-examination, and for purposes of his assessment of management fraud, Selman was asked whether he had given any consideration to the close relationship between Wightman and Stolzenberg. Selman confirmed he had not, all issues of that type being part of the independence issues that the Court was herself going to address and which were outside the scope of his mandate.[3007]

[2800] Selman was also asked whether he had considered the possibility that the explanation for the various misstatements was not management misrepresentation but

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[3003] Selman, May 19, 2009, pp.23-24
[3004] Selman, May 19, 2009, p.26
[3005] Selman, May, 19, 2009, p.27
[3006] See for example : Selman, May 26, 2009, p.39
[3007] Selman, May, 26, 2009, pp.30-31, p.38

rather Wightman's lack of objectivity in performing his audit work appropriately, and he said he had not.[3008]

[2801] During his cross-examination, Selman acknowledged that his analysis of the year-end meetings was limited and restricted to Wightman's sayings and to notes included in the working papers.

> Have you considered the evidence from the record as to what questions, if any, were put by Mr. Wightman to Mr. Stolzenberg at the year-end meetings?
>
> A- Only to the extent that they've been described by Mr. Wightman[3009] and to the extent that there are any notes in the working papers.[3010]

[2802] During his cross-examination, Selman acknowledged the following: *"if a document was never asked for, never seen and there was no representation to Coopers & Lybrand as to the existence of the circumstances that the document purports to suggest, then it would have no consequence on the audit".*[3011]

[2803] During his cross-examination, Selman was asked if, to comply with GAAS, it was enough *"to walk into an audit and say show me whatever you think I should look at, and if you don't show it to me, then I'm assuming that it's not important",* and he confirmed it was not.[3012]

[2804] Selman was also asked to give examples of what an auditor would ask for or expect to find in a loan file, and he answered as follows:

> the loan files should contain such things as **evidence of** the existence of the loan, evidence as to the value of the loan**, collectibility of the loan**, matters of that nature should... one would expect to be in the loan files. [3013]
>
> **an appraisal** if you got a loan that has collateral[3014]
>
> If you had **an unsecured loan, you would be looking for such things as financial statements, net worth statements**, history of the payment of the loans, which you would get from perhaps not the loan file, but the review of the loan card in the accounting records, credit reports if those existed, that type of things.[3015] (our emphasis)

[3008] Selman, May 26, 2009, pp.31-32
[3009] Are only included examinations that took place during the 90s since Wightman only testified before this Court in 2010 (after Selman)
[3010] Selman, May 26, 2009, p.41
[3011] Selman, May 26, 2009, p.68
[3012] Selman, May 26, 2009, p.69
[3013] Selman, May 26, 2009, p.70
[3014] Selman, May 26, 2009, p.70
[3015] Selman, May 26, 2009, p.71

> The auditor would **need to know more about the circumstances of the loan.** The first question would be one of how long-standing it was. If it had been outstanding for a while, the auditor would probably look at **the payment history of the loan,** the auditor would look for **supporting evidence as to the financial capacity of the borrower and the guarantor.**[3016]
>
> **Net worth statements** of a guarantor, **financial statements of the borrower, financial statements of a parent company** if the parent company were the guarantor, generic evidence of that nature.[3017] (our emphasis)

> Q-Assuming that the value of the loan information did not exist in the loan file?
>
> A- Then they should ask for further information, until they have sufficient persuasive evidence.[3018]

> **If there's nothing in the file but** the commitment letter and the promissory note, **and the auditor doesn't ask for financial statements** if we're dealing with an unsecured loan, **then as I said I think that's a breach of GAAS.**[3019]
>
> If the **auditor asks for financial statements and he is told they don't exist,** then the auditor would naturally, I think, **ask the question** "Well, if they don't exist, what have you used as the loan officer to satisfy yourself that this loan is collectible? What have you relied on? Could you show me what you're relying on?".[3020] (our emphasis)

[2805] In a specific described context, counsel for the Plaintiff asked Selman a question about the requirement of "*persuasive audit evidence*". Selman did not hesitate to confirm that in such a context, an auditor did not have persuasive audit evidence.

> Q. - If Donald Selman is the auditor, and I'm asking your opinion, and you're auditing a thirty-five (35) million dollar unsecured loan, and all you have is a commitment letter, a promissory note and a statement from Mr. Smith that the loan is good or okay, or has been renewed for another year, would that constitute persuasive audit evidence?
>
> A- No.[3021]

[3016] Selman, May 26, 2009, p.73
[3017] Selman, May 26, 2009, p.73
[3018] Selman, May 26, 2009, p.75
[3019] Selman, May 26, 2009, p.77
[3020] Selman, May 26, 2009, p.78
[3021] Selman, May 26, 2009, p.76

[2806] Immediately thereafter, the following exchange took place:

> Q.-And if an auditor would rely on that information or loan to come to a conclusion as to the carrying value of the loan, that would be a breach of GAAS?
>
> A- Assuming that that were all the circumstances, that you have a loan that's standing on the books, it's been there for some period of time and there's no more information than the existence of a commitment letter and a promissory note, I would want more information.
>
> Q- That would be a breach of GAAS?
>
> A- Yes.[3022]

Levi

[2807] After considering all of the evidence as detailed in his written report, Levi writes under the heading "*Summary of Conclusion and Opinion*" of his report:[3023]

> 1. Wolfgang Stolzenberg managed to organize a group of co-conspirators to participate in an elaborate, complex and massive fraud.
>
> 2. Wolfgang Stolzenberg enlisted outside law firms in Canada and Europe, local accountants who had the appearance of being independent, management within Castor Holdings Ltd. at all levels, bankers, lenders, borrowers and others, as his group of co-conspirators
>
> 3. Wolfgang Stolzenberg and his co-conspirators carefully, systematically and effectively devised and executed transactions which had the effect of deceiving Castor Holdings Ltd.'s auditors (the "auditors"), creditors, bankers, certain directors and shareholders.
>
> 4. Wolfgang Stolzenberg and his co-conspirators utilized over 200 entities (some fictitious) around the world to assist in his scheme.
>
> 5. Wolfgang Stolzenberg and his co-conspirators backdated documents extensively to demonstrate the existence of transactions at times when they did not occur.
>
> 6. Wolfgang Stolzenberg and his co-conspirators created transactions which included bona-fide documentation, when in fact they were creating an illusion to deceive Castor Holdings Ltd.'s auditors, creditors, bankers, certain directors and shareholders.

[3022] Selman, May 26, 2009, p.77
[3023] D-1347, pp. 2-3

> 7. Wolfgang Stolzenberg and his co-conspirators created and, in my opinion, would have created, any document requested by the auditors or required to justify their deception.
>
> 8. Considering the extent of the fraud, the elaborate and widespread management collusion, the outside collusion and the intentional deception and misrepresentations made by Wolfgang Stolzenberg and his co-conspirators to the auditors, it is my opinion that it was not possible for Coopers & Lybrand to have detected the fraud during the performance of their year end audits in accordance with Generally Accepted Auditing Standards for 1988-1990.[3024]

[2808] During trial, Levi enunciated his definition of "co-conspirators" as follows: "*My definition is that these are people who, whether knowingly or unknowingly, wilfully or unwilfully, intentionally or unintentionally, participated with Mr. Stolzenberg in the production of documents or transactions which had the effect of concealment and deception as described in my report. It's nothing more and it's nothing less*".[3025]

[2809] In his written report, as an integral part of the concealment process, Levi adds the following characteristics of the network of individuals and entities:

> *a **network** of individuals and entities which **spanned the globe** (...)The **true identity of the principals** of these entities **was camouflaged** by having nominee shareholders, directors or officers, many of whom remain a mystery. (...) establishing many of these **entities in jurisdictions in which it is difficult or impossible to determine true beneficial ownership**, e.g. Panama, Netherlands Antilles, Switzerland and Liechtenstein (...)*
>
> *distanced the audits from Castor Holdings Ltd. and his personal companies* (i.e. Stolzenberg's companies) *by **employing different audit firms** - Coopers & Lybrand for Castor Holdings Ltd. and its subsidiaries, and KPMG for his personal companies and the York-Hannover Group, Rogoff and Company, P.C. for the DT Smith group and other unknown auditors or accountants for many of the other entities.*[3026] (our emphasis)

[2810] Levi sustained that his report demonstrated how many of the parties to the Widdrington file, and to the other files upon which the present judgment will have binding effect, "*were in fact deceived by an elaborate and complex scheme of misrepresentation, falsification and dishonest documentation which was orchestrated by Wolfgang Stolzenberg and a wide group of co-conspirators which included certain of Castor Holdings Ltd.'s officers, directors, shareholders, lawyers, investors, banks, consultants and internal accountants. In short, a scheme so well planned and executed that it could not have been detected using conventional investment analysis by its bankers, Generally Accepted Auditing Standards by its auditors or accepted financial*

[3024] D-1347, at page 19
[3025] Levi, January 27, 2010, p. 231
[3026] D-1347, p. 57

monitoring techniques by its investors. It could only have been detected through an extensive forensic investigation subsequent to its inevitable collapse, as did occur with Castor Holdings Ltd."[3027]

[2811] In his written report, Levi describes as follows the way Castor would have perpetrated fraudulent activities, the techniques it would have used:

- Transactions with secret associated entities;
- Fictitious transactions and resulting revenue reporting issues;
- False documents;
- Backdated documents; and
- Incomplete or misleading representations to auditors, investors and shareholders.[3028]

[2812] Levi asserts management fraud at Castor resulted from concealment[3029], use of the Stolzenberg's network of entities[3030], circular transactions[3031], backdating of documents and agreements,[3032] misappropriation of fees and revenues,[3033] and capitalization of interest.[3034]

[2813] Levi asserts collusion and complicity by management and third parties, including Ron Smith, Whiting and Mackay, various lawyers (namely lawyers from McLean & Kerr), Prychidny, three German banks and Bank Gotthard[3035].

[2814] In his written report, Levi opines that C&L were deceit because of:

- Castor's misrepresentations concerning the overall appraisals of loans.
- Castor's withholding knowledge of problems with the YH portfolio.
- Castor's failure to disclose the existence of the "yellow files" (correspondence files).
- Castor's failure to disclose the diversion of funds from the hotels.

[3027] D-1347, p.19
[3028] D-1347, p.46
[3029] D-1347, chapter 9.2, pp. 55-56
[3030] D-1347, chapter 9.3, pp. 57-58
[3031] D-1347, chapter 9.4 pp. 58-98
[3032] D-1347, chapter 9.5, pp.98-108
[3033] D-1347, chapter 9.7. pp. 113 -139
[3034] D-1347, chapter 9.6, pp. 108-113
[3035] D-1347, chapter 11, pp. 143-183

- Castor's failure to fully disclose the reason for the 1988 Topven restructuring.
- Circular transactions and capitalized interests.
- Management's instructions on dealing with auditors' questions.
- Misrepresentations of the ownership of 97872 Canada Inc.
- Castor's failure to disclose the ownership of TransAmerica.
- Castor's failure to disclose a $3.6 million guarantee of Four Season's mortgage.
- Collusion to produce false personal financial statements.[3036]

[2815] In his written report, Levi describes various transactions as "*fraudulent transactions*" because in his opinion their true nature, as disclosed in Castor's accounting records, was not representative of their underlying intent, as described in Castor's internal memos providing additional insight as to their purposes[3037]. He opines that the following "*fraudulent transactions exemplify the intentional deception*"[3038]:

- The 100 million transaction of 1987 (issuance of debentures).[3039]
- The 1987 year-end transaction with YHDL for $8.3 million.[3040]
- The 1988 year-end transaction with YHDHL for $1.5 million.[3041]
- The 1988 year-end transaction with KVWI for $35 million.[3042]
- The 1988 year-end transaction with YHDL for $ 20 million.[3043]
- The 1988 year-end transaction relating to TWTC for $10 million.[3044]
- An October 1988 transaction relating to Airport Corporate Center and CHR Equities for $24 million.[3045]

[3036] D-1347, chapter 12, pp. 183-203
[3037] "*what was seen in the accounting records on the surface is not the full story behind the entire transaction.*" Levi, January 27, 2010, p.121
[3038] D-1347, p. 58
[3039] D-1347, p. 58 and pp. 60 to 66
[3040] D-1347, p. 58 and pp.67-68
[3041] D-1347, p.58 and p. 69
[3042] D-1347, p. 58 and pp. 70-71; Levi January 27, 2010, pp.120-123
[3043] D-1347, p. 58 and p. 72
[3044] D-1347, p. 58 and pp. 73-76

- The 1989 year-end transaction with YHDL for $13.2 million.[3046]
- The 1990 year-end transaction for $40 million (known in this file as "the nasty nine").[3047]
- The 1991 transactions relating to the "Nasty nine transaction of 1990".[3048]

[2816] All those transactions are recorded into Castor's accounting books and records, a fact Levi acknowledges: all inscriptions were there for the auditors to see. There was no concealment of figures, but Levi says the true substance of the transactions was nowhere to be found in those books and records.[3049]

[2817] To piece together this "*well-conceived, executed and concealed fraud*, and to understand exactly how widespread the network of related and associated entities, co-conspirators and fraudulent activity extended, Levi accentuated the fact that it had taken:

- Many years of investigative work performed subsequent to the failure of Castor.
- Many thousands of hours devoted by highly trained auditors in the field of forensic and investigative auditing.
- An army of lawyers performing examinations and discoveries of individuals, companies and documents.[3050]

[2818] Levi opines that "*No auditor conducting an audit in accordance with Generally Accepted Auditing Standards could be expected to have detected such a well-conceived, executed and concealed fraud*[3051]."

[2819] Levi opines that :

- *had the auditor asked for any more audit evidence, Stolzenberg and his "co-conspirators" would have created the requested documentation and presented all of the requested transaction evidence to the auditors' satisfaction; and*
- *Had the auditors questioned any transactions, Stolzenberg and his "co-conspirators" would have provided explanations which would have been carefully designed to satisfy the inquiries and would have been corroborated*

[3045] D-1347, p.58 and pp. 77-82
[3046] D-1347, p. 58 and pp. 83-84
[3047] D-1347, p. 58 and pp. 85- 95
[3048] D-1347, p. 58 and pp.96-97
[3049] Levi, January 27, 2010, pp. 122-123
[3050] D-1347, p. 28
[3051] D-1347, p. 28

> *by other members of management, examination of documents prepared for the purpose of satisfying the auditors or by confirmation from entities involved in the transactions.*[3052]

[2820] Based on his experience in dealing with fraud, and his assessment of the evidence he had reviewed, Levi states that it would be reasonable to infer that the individuals identified in his report as "co-conspirators" would not have provided C&L with the information now available to the Court had C&L asked them questions during their audits in 1988, 1989 and 1990.

[2821] As a matter of fact, Levi takes for granted that "*evidence shows that Wolfgang Stolzenberg and his co-conspirators would have produced and did produce whatever documentation was required to satisfy the auditors in connection with concealing the fraudulent activities at Castor*".[3053] This premise explains largely his disagreements with Plaintiff's experts.

[2822] Levi writes:

> For the most part, frauds occur when **circumstances arise** which result in basically **honest people becoming desperate** and **doing desperate acts** in an attempt **to correct or prevent** the negative **impact of these undesirable circumstances**. With the benefit of hindsight and with what we now know about the activities at Castor Holdings Ltd., its story follows this classic pattern.[3054]
>
> (our emphasis)

[2823] Levi explains that there is a difference between a forensic audit and a GAAS audit. There are three levels of auditing mentioned in section 5300 of the Handbook, and relating to error and fraud:[3055]

- Level 1 which includes sections 5300.01 to 5300.41 where the auditor applies regular auditing procedures and relies on the good faith of management and the completeness of the records.
- Level 2, which includes sections 5300.42 to 5300. 59, where the auditor applies forensic procedures after he or she has encountered circumstances that cause him or her to suspect that fraud or error has occurred and where he or she has to support or dispel such suspicion.
- Level 3, when the auditor encounters or suspects fraud that may involve management and where the auditor has to reconsider his assumption of management's good faith.

[3052] D-1347, p. 31
[3053] D-1347, p.214
[3054] D-1347, p. 45
[3055] Levi, January 13, 2010, pp.85 and following ; D-1347-2

> At Level 1, the auditor stands at an ordinary GAAS audit level, but when he has to move to level 2 and level 3, pursuant to suspicions circumstances he has encountered, the forensic audit starts and the auditor's work goes well beyond what is normally expected in a GAAS audit.

[2824] Levi opined that looking at the signatures on confirmations is a forensic audit procedure, not a regular GAAS procedure[3056]. The same applies, said Levi, to the "*Probing to the bottom*" procedures of Plaintiff's experts[3057].

[2825] GAAS are not designed or intended to detect fraud, but through applying GAAS an auditor may detect fraud. Where an auditor does detect fraud, said Levi, it is generally because he has encountered circumstances that have made him move from one level of audit to the next. [3058]

[2826] On his examination of the working paper files prepared by C&L for the Castor audits of 1988, 1989 and 1990, an examination he did before he finalized his written report and appeared before the Court, Levi concludes (in his written report) there were no failures in C&L's application of GAAS which could have resulted in C&L's failure to detect the fraudulent activities which occurred at Castor.[3059] He finds nothing in the files, no circumstances, indicating that C&L should have raised concerns about the good faith of management, which would have requested them to move from Level 1 to Level 2 or Level 3[3060].

[2827] A section of the Handbook on professional scepticism came into force in 1991, further to the recommendations of the MacDonald commission[3061]. This section is not applicable to the 1988, 1989 and 1990 Castor audits. One objective of the section that discusses professional scepticism (introduced in the Handbook in 1991) was to create a greater awareness that fraud exists[3062]. However, and as Levi said, even before it came into force "*Good faith in management never meant blind acceptance of everything the client said*". [3063]

[2828] Like Selman and Goodman, Levi mentioned that there was nothing improper about Castor's practice of capitalizing interest at first glance. However, he opined that it became a fraud when Castor used the practice to create a false picture that interest was being received in cash.

[3056] Levi, January 13, 2010, p.125
[3057] Levi, January 13, 2010, p.126
[3058] Levi, January 13, 2010, p. 125
[3059] D-1347, pp. 31 and 251
[3060] D-1347, page 31
[3061] Levi, January 13, 2010, p.132
[3062] Levi, January 13, 2010, p. 148
[3063] Levi, January, 13, 2010, p.147-148

[2829] Levi acknowledged that if the journal entries for a transaction were in the company's books for the auditors to see, «*there was no apparent deceit*» on the auditors.[3064]

[2830] Levi acknowledged that a management representation letter is not considered a substitute for audit evidence – he wrote it in his written report.[3065]

[2831] Levi confirmed that there could be situations where an auditor would not have detected a fraud pursuant to his own fault because he or she had not performed the required audit procedures.

> Q.- But I'd like to back you up, if I may, because I'm sure you would concede to the Court that, hypothetically, there could be a fraudulent situation where the auditors are still liable because they didn't do their w ork.
>
> A- I would go beyond hypothetically, I think that it has in fact occurred. So...
>
> Q- So now...
>
> A- ... that's not a hypothesis, that's reality. I think there are situations where a fraud occurs by a client and the auditors did not detect it because the auditors did not perform the procedures that they should have.[3066]

[2832] Levi confirmed he had to accept there were non-performing loans in Castor's portfolio in 1988, 1989 and 1990 as one of the premises of his analysis of the situation and of his conclusions. He explained it as follows:

> I would imagine Mr. MacKay has concluded that because it was his intent to try and project that image to the auditors. (...)
>
> If he thought they were performing, he wouldn't have to try and project that image, it was there to be seen. So I have to accept that as one of the facts that existed. (...)
>
> I can't say when it occurred, I think it may have been a progression through those three years and I'm not certain that they were necessarily as nonperforming as Mr. MacKay may have suspected, but what you have is a situation where they wanted to deflect any attention from these loans by the auditors, so they created this illusion that everything was going fine.[3067]

[3064] D-1347, p. 110 re $30M circular transaction in December 1988
[3065] D-1347, p. 43
[3066] Levi, January 27, 2010, p. 131
[3067] Levi, January 27, 2010, pp.216-217

[2833] During his cross-examination at trial, Levi also confirmed the following:

- For the preparation of his report and during his testimony before the Court, he assumed and considered that C&L's audit staff had met with the GAAS standard for adequate technical training and proficiency, and that they had been properly supervised on the field during Castor's audits of 1988, 1989 and 1990.[3068]

- The expression "*doubtful account*" used by an auditor might have a different meaning at different stages of an audit, but at the end of the audit the expression means "*an account on which it has been determined that a provision should be recorded, in part or in whole, for the possible uncollectibility of that account.*"[3069]

- There are various facts relating to Wightman's involvement in companies or transactions, earlier looked at under the subheading "independence" of the present judgment, that Levi was not aware of.[3070]

- During the relevant years, 1988, 1989 and 1990, before issuing an audit report, an auditor had to do everything necessary to be reasonably satisfied that the financial statements he was opining on were not materially in error for any reason, including possible management fraud.[3071]

- He had looked at C&L's audit working papers of 1988, 1989 and 1990 as long as they were related to the transactions he was opining on in his written report (D-1347),[3072] but he had not looked at all the audit work performed during those audits by C&L.[3073]

- C&L should have sent confirmation requests in relation to the $100 million debentures, but they did not.[3074]

- Account 046 was substantially reduced at year-end through journal entries and a competent auditor would know that the borrower YHDL was not repaying accrued interests he owed in cash, but rather through non-cash transactions, namely new loans created.[3075]

[3068] Levi, February 1, 2010, p. 90
[3069] Levi, February 1, 2010, pp.139-140
[3070] Levi, February 1, 2010. pp.237 and following, Levi February 2, 2010, pp. 6 and following and exhibit PW-3095
[3071] Levi, January 28, 2010, p. 37
[3072] Levi, January 27, 2010, p.132-133
[3073] Levi, January 27, 2010, p. 133
[3074] Levi, January 27, 2010, p. 134-135
[3075] Levi, January 27, 2010, pp. 140-142, p. 146; PW-84

- Seeing that a borrower was not paying the interests on a loan which were accruing while the loan covenant was calling for monthly interest payments, a competent auditor would have noted the fact, asked questions as to why this was happening and insisted on getting an answer.[3076]

> The question would be: Why are you not collecting the interest? I see in the agreement, it says "interest to be paid", why is it not being received in cash?[3077]
>
> I don't think that would be the end of the discussion. It's not the end of the audit and I don't think it would be the end of the discussion, I would need more than "It's good, don't worry".[3078]

- Account 46 was not transformed fraudulently.[3079] "*The capitalization of interest and the journal entries used in account 46 were not only readily available to the auditor, they were scrutinized by the auditor*".[3080]

- The following facts were clear from Castor's accounting books and records of 1988: accrued interests accumulated during the year into account 046 of YHDL, those interests were capitalised into a new loan of $35 million to KVWIL.[3081] As Levi said, "*That's black and white*" [3082] That $35 million loan was reduced by $20 million through a new loan relating to Hazelton Lanes.[3083]

- Looking at exhibit PW-107, an auditor should have had a lot of questions to ask relating to accrued interest, monthly interest payments and year-end interest payments.[3084]

- Seeing exhibits PW-167 P and PW-167 Q (that were brought to his attention), Levi acknowledged he could no longer defend what he had written on page 202 of his report relating to an alleged failure of Castor to disclose to C&L a $3.6 million guarantee of Four Season's mortgage. Levi admitted that the information was there for the auditor to see.[3085]

- Levi was not aware that Castor had many loans concerning development properties where interest capitalization was foreseen right in the loan

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[3076] Levi, January 27, 2010, pp. 156-157 , pp. 205-206, pp. 207-211
[3077] Levi, January 27, 2010, p. 206
[3078] Levi, January 27, 2010, p. 211
[3079] Levi, January 27, 2010, pp. 161-162
[3080] Levi, January 27, 2010, pp. 192-193, pp. 201
[3081] Levi, January 27, 2010, pp. 172-173, 194-195
[3082] Levi, January 27, 2010, p. 172
[3083] Levi, January 27, 2010, pp.173-174, 177; PW-107
[3084] Levi, January 27, 2010, pp.179-188
[3085] Levi, January 28, 2010, pp. 51- 65 : D-1347, p. 202

agreement. Acknowledging that fact, Levi added "*I did not review the loan agreements*".[3086] In fact, to prepare his report Levi looked at transactions, but he did not look at loans.[3087]

> I don't believe I looked at any loans in my report, I looked at transactions which created a loan but I didn't look at the loan. For example, the transactions we've been talking about, I have not looked at the thirty-five (35) million dollar loan, I've looked at the journal entries, and the memorandum and documentation surrounding that which created the loan, but I did not look at the valuation of the loan or anything e lse after that.[3088]

[2834] Levi admitted: "*I have not looked at or given any opinions, nor do I feel capable of giving you opinions on the valuation of that loan. I have not looked at the audit procedures that were done to value the loans*",[3089] "*I have not dealt with those two aspects, the loan valuation or the loan loss provision*".[3090]

[2835] Levi gave the following example of what an auditor's review of a new loan could be:

> Someone who is looking at the loans is doing an analysis of the loans, goes in and sees we have a **new loan of five (5) million dollars**, and then wants to determine, okay, if we have a new loan of five (5) million dollars, is that because we issued a cheque for five (5) million dollars, they would then **go to the cash disbursements journal to determine,** have we disbursed the five (5) million dollars to create the loan.
>
> If they went and did that, they said "No, we didn't", then, they'd say, **"Okay, how did that loan originate?"**, they would go into account 65 and they would see the origin of that is account 46, that would then **take them to the journal** that we're at.
>
> So it's a reverse audit procedure, it's not looking at the general journal, because the purpose of looking at the general journal would be to determine that entries had been properly approved, that they'd been properly recorded, that, for example, if this instruction was "Record this entry to account 68", but by mistake they recorded it to account 65, that's the kind of an audit of the general journal, which is a separate audit, a completely separate aud it procedure.

[3086] Levi, January 27, 2010, p. 207
[3087] Levi, January 27, 2010, p. 212
[3088] Levi, January 27, 2010, p. 212
[3089] Levi, January 27, 2010, p. 212
[3090] Levi, January 27, 2010, p. 216. See also Levi, February 1, 2010, p. 79

> So under the example I gave you where they are doing the loan audit and they are **tracing it all the way back** in that context, this would bring them to the entries that we're looking at.[3091] (our emphasis)

[2836] Pressed to explain how and why he was qualifying "*as fraudulent*" the $35 million loan transaction of 1988 with KVWIL, Levi answered: "*It was because Mr. MacKay says that his memo was intended to conceal information from the auditor and project to the auditor a situation where loans were performing and interest was being realized by Castor and capitalized, and new loans were being created, and as well he points out the ability of Castor to raise new money. All of this goes to the credibility of the income being recorded on those loans.*"[3092]

[2837] Levi was asked to explain the reaction an auditor should have at seeing payment of interests, apparently in cash, from YH debtors in 1990, after having faced capitalization of interests on new loans through journal entries for the same debtors in 1988 and 1989. He answered as follows:

> They may **ask the question "Why all of a sudden** has a company that wasn't paying, now are they paying?", that's very possible. **Any audit procedure and any finding could generate questions. I think any significant change would generate questions.** The question then is based on the answer received, **is it plausible**, does the auditor accept the explanation, considering that they're still at the stage of relying on the good faith of management, can we accept their explanation or do we find their explanation to be a little bit too outside the realm of plausibility, such that we have to start checking a little bit more?[3093] (our emphasis)

[2838] During his cross-examination, Levi clarified his mandate as follows:

> Q- Does that cause you a problem?
>
> A- What kind of a problem?
>
> Q- In assessing the audit work that the auditors did?
>
> A- I'm hesitating because I'm not sure how to answer that. I looked at the work that was done by the auditors, I didn't assess, and again **I go back to what my objective and my mandate was, it was not to assess the work of the auditor but to assess whether the availability of the information that was withheld**

[3091] Levi, January 27, 2010, pp.148-149
[3092] Levi, January 27, 2010, p. 194
[3093] Levi, January 28, 2010, p.239-240

> **would have or could have impacted on their ability to do their work**.[3094] (our emphasis)

[2839] Levi reiterated:

- that his role as an expert had been "*to look for indicia of fraud which may have impacted on the auditors' ability to perform their audit*";
- but that it was not "*to do a determination of whether or not loans were in default, or whether there was a valuation issue, or whether there was a loan loss provision issue. Those were in the domain of other experts, it's completely outside of my expertise. Had I been asked to do that mandate, I would have refused because I'm not going to take on something that I don't myself feel competent to do.*"[3095]

[2840] To enlighten the Court as to the proper context of Levi's opinions, Levi was asked what his understanding of the professional liability of the auditor would be if the Court was to reach the following findings:

- The auditor did not exercise due care and diligence.
- Had the auditors exercised due care and diligence, they would have been able to uncover things that would have led them not to issue audited financial statements at all or not to issue them as they were issued.

[2841] Levi's answer was:

> **Based on the assumptions just enunciated**, and adding the assumption that the audit failures, whether it be in the planning stage or the supervision of staff or the execution of the audit, if those generally accepted auditing standard procedures were not followed and there was failure there which resulted in the financial statements being misstated and had the auditor done the proper procedures under GAAS, those GAAS procedures would have provided the auditor with some form of indication that there is the need to pursue transactions further which then could have resulted in detection of the fraud, because I'll state that I don't believe the standard auditing procedures, the level 1 procedures would detect the fraud, but if they had done what they should have done and level 1 would have brought them to level 2 suspecting an irregularity which required further work, and then maybe to level 3 even, **then yes, they would have been at fault for not doing level 1 properly, which would have then led them to levels 2 and 3. That would be my understanding.**[3096] (our emphasis)

[3094] Levi January 27, 2010, pp.129-130
[3095] Levi, January 27, 2010, p. 218-219
[3096] Levi, January 28, 2010, pp. 11-12

[2842] Levi said he would be surprised, and would find it hard to understand, that none of the Defendants'experts had been called upon to provide a specific opinion as to whether the work performed by C&L to value the loans in the Castor portfolio was conducted in accordance with GAAS, given his limited mandate and his understanding of the issues in litigation, which included clearly the methodology of valuing the loans and auditing the loans. [3097]

[2843] As the following exchange between counsel for the Plaintiff and Levi illustrates, Levi's mandate was confined to one topic, i.e. the identification of indicia of fraud, whether or not they could have or effectively had an impact on the audit process:

> Q. - My last question before the break, I'm going to suggest to you that your methodology is flawed, and you can certainly tell me that you don't agree, you're saying that you looked for indicia of fraud which would have made it difficult for the auditors to ascertain the true nature of the transactions. Wouldn't it have been appropriate to first determine that the auditors performed the procedures that they were supposed to perform, and then explain to the Court that they didn't get the right answer because of fraud? Why have you started with fraud and not with the audit work?
>
> A- I've tried to, I think, explain this when I looked at the... when I spoke with the methodology, and I think I referred to the decision 3, and the question was: Are the financial statements misstated, yes or no? Are they in accordance with GAAP, yes or no? If they're deemed not to be in accordance with GAAP, then why are they not in accordance with GAAP? Were there audit failures that resulted in them not being in accordance with GAAP?
>
> If it's deemed that there were audit failures not to be in accordance with GAAP, then the question is: Were those audit failures as a result of the auditors being deceived or as a result of them being negligent, or making mistakes? And if it was determined it's because they were deceived, how were they deceived?
>
> My understanding is there are other experts who addressed the issues of whether or not the financial statements are or are not in accordance with GAAP and that aspect of it.
>
> **My mandate was, are there any indicia of fraud**, and I don't believe that we have seen all the indicia of fraud and I'd believe **there are certain transactions, which I might refer to in the context of my report, which don't even impact on Castor or on the auditors** but are there to provide the Court with my view of the atmosphere that existed during these years that the auditors were performing their audit, an atmosphere of deception and concealment, hiding of documents,

[3097] Levi, February 1, 2010, p.40

> not volunteering information that the people knew the auditors would or should have to help make them make proper decisions.
>
> Did that impact on whatever faults the Court may find ultimately translated into GAAP failures on the statements? I don't know what the Court will decide is a GAAP failure, but the Court will then have my testimony and my report as to what were the fraudulent transactions that... and the deception that I've identified that precluded the auditors from identifying or carrying out their work, what precluded them from identifying related party transactions, what precluded them from identifying the cash circles as being a deceptive mechanism to imply that loans were being... were performing?
>
> I don't see**... I started at the fraud end**, you don't start at the GAAP end because if, for argument sake, there was nothing wrong with the financial statements, as I pointed out, **in some instances, a transaction had no impact on the financial statements because it was all within the same line on the balance sheet. That doesn't mean that there wasn't some fraud that occurred**. So you don't necessarily have a GAAP failure which is as a result of fraud, and every fraudulent transaction doesn't necessarily produce a GAAP failure. (our emphasis)

[2844] During his cross-examination, Levi recognised that he was not providing the Court with any opinion on the following topics for any of the three relevant years, 1988, 1989 and 1990: [3098]

- Whether Castor's loans were carried at the lower of cost and estimated realizable value.
- Whether any additional loan loss provisions were required under GAAP.
- Whether C&L obtained sufficient appropriate audit evidence to support their conclusion on the carrying value of the Castor loans.
- Whether C&L properly documented, in accordance with GAAS, the audit evidence that they relied upon in respect of the carrying value of the Castor loans.
- Whether any of the revenue recognized by Castor should not have been recorded as revenue in accordance with GAAP.
- Whether there was reasonable assurance of collectability of the revenue recognized by Castor.
- Whether notes 2, 3 and 4 to the audited consolidated financial statements were designed to convey the liquidity of Castor to readers.

[3098] Levi, February 2, 2010, pp.84- 99

- Whether economic dependence existed between Castor and any of the lenders or borrowers described in his report.
- Whether the Canadian York-Hannover group of companies was insolvent in 1988, 1989 or 1990.
- Whether the use by Castor of a Statement of Changes in Net Invested Assets was in accordance with Section 1540 of the CICA Handbook.
- Whether the audited consolidated Statement of Changes in Net Invested Assets disclosed the amount of cash used up in or provided by operations in accordance with GAAP.
- Whether there were indicia of fraud in respect of the preparation of the valuation letters.
- Whether there were indicia of fraud in respect of the preparation of the Legal-for-Life Certificates by C&L.

[2845] Levi's analysis of certain transactions was incomplete, to say the least. The following exchange, relating to his alleged failure of Castor to disclose a $3.6 million guarantee of Four Season's mortgage,[3099] illustrates, in the context of the characteristics and the limits of his mandate, the weaknesses or the flaws of the methodology he followed.

> Q.- I'd like to look at with you D-1313. Perhaps we can just pull it out. D-1313, and I don't know if you need me to give it to you, it's the Standard Practices for Investigative and Forensic Accounting Engagements. (...)
>
> Point .05 states, under the heading "General": "*IFA practitioners should identify, analyze, assess and compare all relevant information, assess substance over form, and develop and test as needed hypotheses for the purpose of evaluating the issues in the IFA engagement.*"
>
> Q.- Would it be fair to say that in respect of the three point six (3.6) million dollar guarantee issued, you did not identify, analyze, assess and compare all relevant information before you wrote your report?
>
> A- Yes.
>
> Q- And would you agree that you did not test alternative hypotheses, such as the hypothesis to the effect that the information about the existence of the three point six (3.6) million dollar guarantee was not hidden from the auditors?
>
> A- Clearly.

[3099] D-1347, chapter 12, section 12.11, p. 202

> Q- Did you consider, when you were writing this section, the possibility that the auditors actually knew about the three point six (3.6) million dollar guarantee?
>
> A- No. I think if that existed, I would have seen reference to it in the eighty-eight ('88), eightynine ('89) and ninety ('90) working paper files. Now, I'll qualify that by saying I did not look at working paper files going back to nineteen eightyfive (1985), as mentioned before. My understanding was that we were focusing on these three (3) years. If there was some mention in the prior working paper file, or if there is, for argument sake, mention in the analysis of the fee income that there's a small amount of commission income with regards to this three point six (3.6) million dollars, that is something that would have gone unnoticed.
>
> Q.-But if a guarantee is assumed in nineteen eightyfive (1985), wouldn't the logical place to go be to the nineteen eighty-five (1985) working papers to assess whether the auditors knew about the guarantee?
>
> A- I think, from the auditor's perspective, yes, absolutely. [3100]

Plaintiff's experts

Vance

[2846] Vance referred to the Handbook definition of fraud, section 5300.43.

[2847] Vance explained that the auditor's objective with respect to material misstatements caused by fraud and error was set out in section 5300.44, as follows:

> The auditor's objective in making an examination of financial statements in accordance with generally accepted auditing standards is to express an opinion on the fairness with which they present the financial position, results of operations and changes in financial position in accordance with generally accepted accounting principles. The auditor recognizes that the financial statements may be misstated as a result of fraud or error. Accordingly, in obtaining sufficient appropriate audit evidence to afford a reasonable basis to support the content of his report, the auditor seeks reasonable assurance, through the application of procedures that comply with generally accepted auditing standards, that fraud and error which may be material to the financial statements have not occurred or that, if they have occurred, they are either corrected or properly accounted for in the financial statements. The auditor has no separate or additional responsibility to detect fraud or error. The prevention and detection of fraud and error is primarily a management responsibility.[3101]

[2848] Vance opined that in 1988, 1989 and 1990, an auditor had to design its audits (to plan its audits) to detect all types of misstatements, whether they were resulting from

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[3100] Levi, January 28, 2010, pp.65-69
[3101] PW-1419-1A (1988); PW-1419-2A (1989); PW-1419-3A (1990)

fraud or error. [3102] He cited the C&L technical material TPS-A-300[3103], at paragraph 10 on page 10 and under the heading "audit Risk", where in his opinion C&L was acknowledging such an obligation to plan an audit to detect all material misstatements (resulting from fraud and error).

> The term "overall audit risk" is used to describe the risk that an inappropriate audit opinion will be issued on a set of financial statements. **For example, there is a risk that an unqualified opinion will be issued when the financial statements taken as a whole contain a material misstatement resulting from either fraud or error. We are not obligated to plan the audit to detect immaterial misstatements resulting from fraud and error.**" [3104] (Emphasis by Vance)

[2849] Vance acknowledged that an auditor did not have the responsibility to detect fraud in the relevant period (1988, 1989 and 1990). Then, the responsibility of the auditor was limited to an obligation to plan to detect material misstatements.

> No. As set out in section 5300.44, the auditor has no specific responsibility for the detection of fraud, that is solely a management responsibility in those years, nineteen eighty-eight (1988) to ninety ('90), an auditor's concern is only with respect to detecting material misstatements in the financial statements that may have been as a result of fraud.[3105]

[2850] While he agreed that the auditor's approach was not the one of a detective,[3106] Vance opined the auditor, nevertheless, ought to exercise healthy scepticism.[3107]

[2851] In the presence of "red flags", of suspicious circumstances, Vance opined an auditor should have "*probe to the bottom*".[3108] Again, he invited the Court to rely on the well-known and recognized author Anderson:[3109]

> SUSPICIOUS CIRCUMSTANCES
>
> In determining standards of care appropriate in different circumstances the courts have placed special emphasis on the auditor's responsibility to detect fraud in the event that they become aware of suspicious circumstances. English cases have been very specific on this point. The Kingston Cotton Mill decision warned:
>
> > If there is anything calculated to excite suspicion he should **probe it to the bottom.**

[3102] Vance, March 5, 2008. pp. 128 and following
[3103] PW-1420, tab 9
[3104] PW-2908, vol.1, chapter 2, pages 2-1 and 2-2;
[3105] Vance, March 5, 2008, p. 133
[3106] Vance, May 12, 2008, p. 86
[3107] Vance, March 5, 2008, pp. 140, and 146 and following
[3108] Vance, March 5, 2008, pp. 136 and following
[3109] Vance, March 5, 2008, p. 134

> Recent court decisions have reaffirmed the requirement that auditors probe deeply into areas that arouse suspicion. In the *Continental Vending* case[3110] in the U.S. in 1969 one implication of the decision was that, if auditors did not conduct their examination with extraordinary care and diligence in circumstances where there was clear suspicion of a fraud on the part of management, they could be held to be abetting the fraud and accordingly accomplices.
>
> The doctrine of probing suspicious circumstances to the utmost has been carried over into non-audit situations. In the *1136 Tenants* case the finding of negligence in failing to detect the agent's fraud was partially supported by the argument that the working papers contained notations of missing invoices that the CPA had not followed up.
>
> The judgment in the 1970 *Pacific Acceptance* case, stressing the importance of alertness for a pattern of suspicious circumstances, contains a contemporary statement on this question:
>
> > If, during an audit, there are a substantial number of irregular or unusual matters encountered by audit clerks and some, singly or in combination, indicate the real possibility that something is wrong, **then to separate each off into watertight compartments and pose the question whether it individually raises a suspicion of fraud and on receiving a negative reply asserting that it follows that the clerk does his duty if he does nothing further ...denies both the true tests of legal duty of care and of common sense...**
> >
> > Thus, if material irregularities appear, a careful auditor can normally be expected to remember and bring into consideration other irregularities,... and he might be expected to go back over past working papers, **even those of a prior audit clerk,** to bring to mind similar irregularities but whether he should take any of these steps would depend on the circumstances, particularly the seriousness and materiality of the irregularities uncovered.
>
> It is very important that auditors thoroughly document and review their work in order to meet the legal responsibility for the recognition of suspicious circumstances. In most of the court cases dealing with negligence in recognition of suspicious circumstances, the auditor's working papers themselves contained indications that things were not as they should be. The greater danger seems to be not the failure to discover and document clues but the failure to recognize them as suspicious. **A healthy skepticism should remain an important audit ingredient."**[3111] (Emphasis by Vance)

[2852] Vance cited one of C&L's internal publications that confirmed that C&L agreed that professional scepticism was and had always been an essential part of GAAS.

[3110] Extracts of this case were reproduced in C&L's AWPs (PW-1053-63C-1, sequential pages 64-71)
[3111] PW-1421-23; PW-2908, vol. 1 chapter 2, pp. 2-2 and 2-3

> Competent and sufficient audit evidence continues to be the foundation for the auditor's opinion. **Insufficient professional skepticism, illustrated by "auditing by conversation", or failing to obtain solid evidence to back up management's representations**, can lead to audit problems. In the final analysis, auditors need to step back and ask one of auditing's most fundamental questions: Does it make sense?"[3112]

[2853] Vance identified various situations ("red flags") that should have been considered by C&L as suspicious circumstances and where they should have probed to the bottom, but did not. Vance identified various situations where, in his opinion, C&L had not exercised healthy scepticism and should have.[3113]

> I think there are areas calling for healthy scepticism, as we like to call it, the first being in nineteen ninety (**1990), working paper E-65C**, which has been filed as PW 1053-15-10. (...)
>
> That's **a very serious note** for an audit staff member to make, and considering that Mr. Quesnel was not yet a CA, that is about all that a staff member at that level can do, is to raise the concern for the more senior members of the engagement team.
>
> (...)
>
> What transpired again, as I mentioned earlier, was **with these loans, there's no further documentation** in the audit file as to the disposition of these comments, either with respect to the impact of such a high level of unsecured loans or with respect to the forty (40) million dollars of year-end loans, and the examinations on discovery of Mr. Wightman indicate that he went in and discussed them with management, but he has prepared meeting notes for his discussions on February fifteenth (15th), nineteen ninety-one (1991), fairly copious notes, I might add, but there's not a mention in those copious notes of the forty (40) million dollars and **nothing else was done**.
>
> The indication that the client was okay with them or pleased with them is not audit evidence at all, and this matter was just let dropped at that point. And that's exactly what tips and tidbits 163 is talking about.
>
> **Other areas** where healthy scepticism, I think, should have been brought to bear, there was a high level of activity and especially as **the foreign portfolio grew**, to where it exceeded that of the portfolio of Montreal, with **entities (inaudible) jurisdictions and for which no financial information was being received from the borrowers.**
>
> In addition, the same issue with respect to scepticism, there were, surprisingly in my view, a **high number of confirmations signed for borrowers or lenders by**

[3112] PW-1420, tab 30: T&T 163 issued January 1991; PW-2908, vol 1. Chapter 2, p. 2-4; Vance, March 5, 2008, pp. 140 and following

[3113] For example, Vance, March 5, 2008, pp. 147 and following

> **Marco Gambazzi,** who was a director of Castor and managing director of CH International Finance NV, **and Mr. Baenziger**, who was management, he managed the operations overseas and also was a managing director of CH International Netherlands BV and a director of CH Ireland, and this is also taking into account and with the extract from Anderson about being able to remember things, in an earlier year, they had questioned **Marco Gambazzi in trust** with respect to deposit, and he sent a telex back indicating that that deposit was being **held in trust for Wolfgang Stolzenberg**, the president of Castor.
>
> That's information that an auditor should have and now, you see a **proliferation of Marco Gambazzi in trust accounts,** and obviously, scepticism should lead an auditor to at least try to obtain more detail.
>
> Another situation where I believe scepticism most certainly should have been applied is situations where the auditors, Coopers & Lybrand, would be provided with audited **financial statements of borrowers**. In the prior years, Topven Holdings, with respect to the Toronto Skyline, would provide audited financial statements. Maple Leaf Village had audited financial statements. And they were in Coopers' file, as did York-Hanover Developments Ltd. Over the period from nineteen eighty-six (1986) to about nineteen eighty-eight (1988), they slowly fell off the table and were no longer provided with audited financial statements, much less did they... The only financial statements they did get was Maple Leaf Village Investments Inc., an internal financial statements, but **there were no statements of any form examined by Coopers** for Topven or York-Hanover Development Ltd. And that's another case of doing a little probing, to **find out why**, and it's not uncommon for auditors to ask the client **"How come it's not audited?"**, (inaudible) going from audited to unaudited, and it's, you know, a very serious warning sign.
>
> And you can also... This is something you have to be careful with ethically, but you can speak to the auditors of the other firm to find out. We've had that 1situation ourselves, and all we will say is we're no longer auditors of that company, and of course, the auditor who was looking for those financial statements is then put on notice that something has gone haywire. But you can't divulge client information, but you can certainly say you're no longer auditor. If you get consent of the client to speak to the other auditor, then I think they would tell you the reason they're no longer auditors.[3114] (our emphasis)

[2854] Vance identified[3115] or acknowledged situations where Castor's management had not been or might not have been forthright. Nevertheless, by an audit in compliance with GAAS, Vance opined that C&L should have uncovered material misstatements in the consolidated financial statements of Castor for the years ended December 1988, 1989

[3114] Vance, March 5, 2008, pp. 147-152

[3115] PW-2908, vol. 1, chapter 2, page 2-5 (the "Nasty nine loan" situation)

and 1990 (departures from GAAP) of such an extent that C&L should not have issued unqualified audit opinions.[3116]

[2855] For each of 1988, 1989 and 1990, Vance's conclusion was that C&L should have either denied an opinion or issued an adverse opinion indicating the extent to which the financial statements were materially misleading.

Froese

[2856] Froese agreed that Castor management concealed, misrepresented or omitted to apprise C&L of some relevant information.[3117]

[2857] Froese acknowledged that there were some documents that Castor did not show C&L and might not have shown C&L.[3118]

[2858] Froese agreed that fraud could be either active or passive. [3119]He said it could take various forms, and recognized a few:

- Misappropriation of company assets.
- Intentional misrepresentation of financial statements.
- Artificially enhancing financial statements by changing maturity dates if it was intentional.
- Artificially recording the receipt of cash to make loans appears as performing.
- Intentional concealment of a material fact from an auditor. [3120]

[2859] Froese said "*I believe there is deceit and dishonesty and that it wasn't my role to determine whether or not there was fraud.*"[3121]

[3116] See PW-2908, vol. 1 chapter 2; Vance, March 5, 2008, pp. 126 and following; Vance, March 10, 2008, pp.136 and following (Topic: the SCFP); Vance, April 16, 2008, pp.162 and following (Topics: mandate, adequacy of the audits, differences between fraud on the company, fraud on the investors and fraud on the auditor); Vance, April 17, 2008, pp. 107 and following; Vance, May 12, 2008, pp. 30 -252; Vance, May 13, 2008, pp.16, 25-40, 58-68, 93 and following; Vance, Mai 26, 2008, pp.254-261; Vance, May 27, 2008, pp. 152 and following; Vance, June 4, 2008, pp. 230 and following; Vance, June 5, 2008, pp. 147-149, 188-195; Vance, June 12, 2008, pp. 7-55, 72, 99; Vance, June 13, 2008, pp.76 92, 173, 175, 231; Vance, July 7, 2008, pp.78 and following.

[3117] Froese, January 7, 2009, pp.78-81; Froese, January 12, 2009, pp.69-72 and 89-90

[3118] PW-2941-3, paragraphs 3-57, 3-58 and 3-200; Froese, December 8, 2008, pp.71-74

[3119] Froese, December 5, 2008, p. 102

[3120] Froese, December 5, 2008, pp. 101-102

[3121] Froese, December 5, 2008, p. 103

[2860] The above mentioned realities were taken into account by Froese. He described his mandate as follows and confirmed he had assumed there was fraud in reaching his conclusions:

- **Mandate**

  We were asked to provide our opinion on whether or not Coopers & Lybrand complied with general accepted auditing standards in relation to their nineteen eightyeight (1988) to nineteen ninety (1990) audits of Castor and asked to provide an opinion in relation to **whether or not, considering the extent of alleged fraud by management of Castor,** whether it was to such an extent that the auditors would have had sufficient information, had they complied with GAAS to detect the problem loans in spite of the fraud.[3122] (our emphasis)

- **Assuming fraud**

  In reaching my opinions in this report, I assumed that there was fraud; it wasn't the opposite. So I can understand that being an issue if you were assuming there was no fraud. But the assumption was that there are fraudulent acts.[3123]

[2861] Froese explained that an auditor can rely on management's good faith and assume that fraud has not occur "*unless there are indications or suspicions, so something raises an auditor's suspicion about fraud*", in which case the auditor has to do more work.[3124]

[2862] Froese said section 5300.56 of the Handbook was relevant to the examination of the audits since circumstances described therewith were part of the Castor's audit reality:[3125]

- Over the years, C&L audit staff members noted various circumstances where Stolzenberg or other representatives of Castor were reluctant to provide information[3126] or had imposed constraint on consultation of document[3127].

- Two separate audit teams were used - information was not shared between the teams - communications between the team members were limited, if not inexistent.

[3122] Froese, November 11, 1008, p. 184
[3123] Froese, December 5, 2008, p. 109
[3124] Froese, November 12, 2008, pp. 73-74
[3125] Froese, November 12, 2008, pp. 76-77
[3126] See AWPs of 1986 and the note of Jean Guy Martin relating to Lambert and the reluctance of Stolzenberg. Froese, December 2, 2008, p.125
[3127] In 1990, C&L was not allowed to make a copy of financial statements. C&L had to write down all the numbers (to take time for that purpose while there was very little time to do all the work)

[2863] Having two separate teams and very little communication between them, if any, is surprising, said Froese, given that CHL and its overseas subsidiaries were lending to the same borrowers or groups of borrowers. Froese cited Penny Heselton, a Montreal audit team member, who testified as follows:

> A. The client didn't want - the client wanted to keep things separate. That's all I knew.
>
> Q. And how did you know that?
>
> A . He told us.
>
> Q. Mr. Stolzenberg?
>
> A Well, actually it started off at our office.
>
> Q What do you mean?
>
> A.-The staff knew that if you went up to Europe to do the audit, you - or if you did the audit in Canada, you'd never go to Europe to do the audit there. It was just general knowledge.
>
> Q. And-how did you know that it was the client that requested it?
>
> A Hum ... General knowledge and - oh, the first morning I went and met Mr. Stolzenberg, I asked him, "If I open up a book, does it mean I can never go to Europe?" He says, "You're here; you can never go to Europe.[3128]

[2864] Section 5300.56 reads as follows:

> During his examination, the auditor may encounter circumstances which while not necessarily indicating that management lacks good faith may alert the auditor to such a possibility. Examples of such circumstances are:
>
> (a) information being provided unwillingly or only after unreasonable delay;
>
> (b) a limitation in the scope of the examination imposed by management;
>
> (c) identification of important matters which were previously undisclosed.

[2865] In Castor's case, the following circumstances have to be taken into account:

- The presence of a domineering management (Stolzenberg).[3129]

[3128] Heselton, April 26, 1996, pp. 131-132
[3129] Froese, December 8, 2008, pp. 152-154

- The evolution of Castor's business (from loans secured by mortgages to loans secured by options, pledge of shares, receivables from affiliates or management agreements, and unsecured loans).[3130]

[2866] Froese established that C&L could not blame everything on an alleged fraud by Castor's management. He opined that C&L would not have issued unqualified audit reports and audited financial statements, as they did, if they had complied with GAAP and GAAS, which they did not.

> Coopers & Lybrand should have concluded, had they added up the loans and compared them to appraisals that were available, had they looked at the right numbers in appraisals, had they requested financial statements of borrowers, they would have concluded that allowances for loan losses were required at Castor for a number of different projects and borrowers.[3131]

> I concluded that there was enough in the loan files and information that should have been requested to be able to... to make an overall conclusion that there was an issue with problem loans and a collateral shortfall for the loans.[3132]

[2867] Froese said the auditors would have come to the conclusion that Ron Smith's comment that a loan was good (as noted by the auditors in the APWs) was not a reasonable conclusion had the auditors comply with GAAS.[3133]

[2868] Froese opined that C&L should have been more sceptical on a number of items, and that they had to be to comply with GAAS.[3134]

[2869] Froese described and explained the methodology he had used as follows ("the tapestry"):

> **Description**
>
> In relation to fraud, My Lady, I looked at what was in front of the auditors, what information they had available to them to determine whether or not it was reasonable for them to conclude that there was a collateral shortfall that required allowances for loan losses.
>
> The other approach that could be taken is to look at all of the deceit, dishonesty, untold truths, to sort of look at that whole weaving together of a tapestry of dishonesty, and to examine sort of each thread that makes up that tapestry, look

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[3130] Froese, December 2, 2008, pp. 125-126
[3131] Froese, December 2, 2008, p. 126; see also, Froese, December 5, 2008, p.99
[3132] Froese, December 8, 2008, pp. 69-70, 100 and following
[3133] Froese, December 8, 2008, pp.80-82
[3134] Froese, December 8, 2008, pp. 94 and following

at it and then say "Is that sufficient to conceal from the auditors the collateral shortfalls?".

So, in my view, there's a few issues in front of the auditors. One is the more intricate the tapestry, the more threads to deceit, dishonesty, untold truths that make up that sort of tapestry of alleged fraud, the greater the chance that the auditors may be aware of some of that. The chance that it triggers that there are issues.

The other side is the auditors have chosen, based on their audit approach, to accept a few things in looking at that sort of tapestry. One is they accepted that they're two (2) audit teams and the audit teams only communicate through the interoffice memo at the end of the year. So, they have sort of two (2) looks at that tapestry, one from C&L Montreal, one from C&L Europe's audit teams, and they've chosen to plan the audits separately, to carry them out separately, to not share information other than through the interoffice memo, and so you've got two (2) chances of looking to that tapestry at what's happening behind it, and you're choosing not to communicate with each other what you're seeing, other than in that one year-end interoffice memo.

The second thing is as auditor, you've chosen not to look at who the owners of the borrowers are. You've accepted that Lambert, Skyeboat, 321351 Alberta, 612044, 97872, you've accepted that these companies are owned by European investors, because you've been told that and you've accepted that they don't need to tell you who the actual borrowers are.

You've also accepted, and whether or not the partner was aware of this or not, it's in the audit working papers, but you've accepted that when you look at the loan files, you'll only look at them in the presence of Mr. Smith if you're in Montreal. You've accepted that you'll only look at loan files for D.T. Smith in Europe when the files are in Montreal.

So, as auditors, you've chosen to not look in some places when you could have looked to gather some information.

You then look - and this was my approach, My Lady, I looked at what's on this side of the tapestry - you can look at the tapestry all you want and no matter how hard it is to see through, really the question that's important as an auditor is what's on this side of the tapestry, what do I have in front of me that can lead me to show that there's an issue with this audit, regardless of whatever web or tapestry of lies and deceit management has built.

So, on this side of the tapestry, we know we have Maple Leaf Village, an appraisal that shows a hundred and four (104) million as a future potential value, sixty-seven point seven (67.7) as a current value. The auditors chose to look at a number likely pointed to them by Mr. Smith, without reviewing the whole appraisal to see the note on the bottom saying "Look at the previous page, that's the real value, don't look at this page, it's on the previous page".

You've got loans that when you add them up total more than appraisals, and the appraisals are referred to in Coopers & Lybrand's audit working papers. You've got financial statements of borrowers that on the occasion that Coopers asks for them, something is provided to them, but you've got Coopers & Lybrand choosing in their audit strategy to not ask for financial statements for many of the borrowers.

So, they've chosen not to look at York- Hannover Developments Ltd. or KvW Investments, or YHDHL, 612044, 97872, Skyeboat, 321351 Alberta. I mean, the list goes on of the borrowers' financial statements they've chosen not to look at.

So, there's a lot of information this side of the tapestry. A lot that's available to the auditors to ask for, that they choose not to ask for.

And in my opinion, in reaching a conclusion on whether the auditors can rely on the fraud as concealing the security shortfall from them is looking at that tapestry without looking at what's in front of them as auditors. In my view, you look for what the auditors should have done, what they had in front of them in drawing that conclusion, not at the nice colours of thread in the tapestry of lies and deceit and everything else, that I'm sure is there, but it's essentially irrelevant for a lot of the collateral shortfalls that were reported on in LECG's report, in my report.

The issue of whether or not there's a scope limitation, and I was provided a few pages on Mr. Levi's report, (inaudible), where Mr. Levi suggests that by definition, not knowing the ownership of the borrowers was not a scope limitation, and in my view, it's irrelevant, My Lady, whether it's called a scope limitation or something else, Coopers & Lybrand accepted management's answer that they weren't going to know the names of the borrowers.

Whether they agreed to accept it or not, whether any auditor or expert says they should have not accepted as an answer or not, they did, and its information that in my view is important to evaluating the loan loss allowance, and also for disclosure.

I haven't reported on related party disclosure, My Lady, but I just want to make the point that if you have allowances for loan losses and those loans are to related parties, that's information a financial statement reader will consider important. Remember, we looked at materiality on the first day of my testimony, it's something that could change the minds of an informed reader. So, if an informed reader reading the statements and there's disclosure that the borrowers related to, for example, Toronto Skyline, are a related party, and you've got a forty (40) or fifty (50) million dollars loan loss allowance for that company, I think that's important information for a reader. I don't know if they're related or not, I don't know who owns Lambert, but I think that's important information for readers to know if they are related.

In relation to red flags, Mr. Levi suggests some of the items I've raised aren't red flags and I could name others, that report section is pretty brief, it wasn't the main focus of my work, and we do have memos from Jean-Guy Martin, back in his

eighty-six ('86) audit work, where he mentions that Mr. Stolzenberg was uncomfortable providing information on Lambert. We have the nasty nine (9) loans and no disclosure of who those borrowers are. If you dig into that one, you see that there's common addresses, common owners.

You have fee income in CHIO with D.T. Smith that when it flows through, I understand that the journal entries are supported, (inaudible) accounting style, with the names of where the money is going and what the commission are or the fees are.

I mention domineering management. That's one of the factors you look at as an auditor to look at whether or not there's an increased likelihood of management fraud. It's not necessarily a red flag that there's fraud, but it's a fact that you look at, on whether or not there's a potential environment or increased risk of fraud.

Same with the terms of the loans, you've gone from loans that are secured by mortgages to loans secured by options, receivables from affiliates, management agreements. You got increasing remoteness to the... to real estate in some of the collateral for some of those loans, a number that were unconditional, so there are loans that are unsecured, it's just promissory notes for them.

So, over the years, the collateral available for the loans changes, the loans shift from being mortgages that have appraisals greater than the loans, I assume, to by eighty-eight ('88), it's switched around for a number of loans.

So simply, just to conclude, in my view, Coopers & Lybrand should have concluded, had they added up the loans and compared them to appraisals that were available, had they looked at the right numbers in appraisals, had they requested financial statements of borrowers, they would have concluded that allowances for loan losses were required at Castor for a number of different projects and borrowers.

As you find things like that out, one of the things an auditor looks for, and section 5300 has a list of factors an auditor looks for, is information that comes to your attention that management hasn't told you about. If you find a number of loans that are potentially problem loans and management says everything is good, that there are no issues or no problems, that too is an indicator that you have a potential issue with management's integrity, and you'd want to do more work.

So, in my opinion, there were a number of indicators, the biggest of which would be the issues with the value of properties compared to what management is telling you about those properties, that lead you to the ability to identify properties with shortfalls, and management telling you things that don't line up with what the underlying documents show.[3135]

[3135] Froese, December 2, 2008, pp. 119-127. See also in cross-examination: Froese, December 5, 2008, pp. 111 and following

Explanation

> Well, what it does it looks at what's available to the auditors. It looks at what the auditors should have, in my view, requested. And it looks at what issues that would raise to an auditor had they requested that documents... document or documents and not been provided.
>
> So it doesn't ignore fraud completely. What it does, is look at what the auditors did and some of the paths you would take. So if you ask for, for example, financial statements of YHDL that were audited, what would you get? If you asked for... or if you asked to meet with or talk to the auditors of YHDL, what would the response be? And if the response is, "No, you can't " or the response by York-Hannover is, "No, we won't let you", it raises an issue for a red flag basically for the auditors as to whether or not there's an issue here with the information we're not getting.
>
> So I don't think it... the approach I followed ignores fraud. It considers the information in front of the auditors, but what, in my view, they reasonably should have requested.[3136]

[2870] Froese opined that C&L would have seen the need for the huge LLPs he had opined were needed in 1988, 1989 and 1990, and would have been able to establish them notwithstanding management's fraud or misrepresentations (assuming it existed), had they complied with GAAS.[3137]

[2871] As part of its knowledge of Castor's business, the lending industry, Froese opined that C&L should have known that loan files were expected to contain documentation such as loan summaries, commitment letters, correspondence with the borrower, internal memoranda providing evidence that the loan was being monitored, current audited financial statements from the borrower (or in some cases unaudited financial statements), project status reports or similar reporting for projects under development, and other documents necessary to understand the current status of the loan as at the audit date.

[2872] Froese said C&L should have sought the above documentation, including the correspondence files, and review it.

- It should not have been a problem for the audit of the overseas subsidiary taking into account Ford's testimony that she had an unrestricted access to loan files in Europe.

[3136] Froese, December 5, 2008, pp. 26-27

[3137] PW-2941, volume 1, pages 139 and following; Froese, November 25, 2008, pp.62 and following (TSH), pp. 123 and following (CSH) ; Froese, November 26, 2008, pp.59 and following (MLV), pp. 119 and following (MEC); Froese, November 28, 2008, pp. 190 and following (YH Corporate loans and the nasty nine loans); Froese, December 12, 2008, pp. 31 and following (Lambert); Froese, January 6, 2009, pp. 89 and following (MLV)

- It should not have been a problem in Montreal either; otherwise C&L would have had to consider if it was facing a scope restriction.

[2873] Lack of planning and supervision, and insufficient training and knowledge, prevented C&L from knowing about, asking for and reviewing existing and available documentation.[3138] This had nothing to do with an issue of fraud.

[2874] Froese acknowledged no Handbook section stipulated that auditors had to plan their audit to detect fraud in 1988, 1898 and 1990.[3139] However, he said that auditors had to plan their audit to detect material misstatements resulting either from error or from fraud.[3140]

Rosen

[2875] Rosen explained why he had produced an additional report concerning the issue of fraud in 2007, PW-3034: he did it further to amendments to the Defendants' plea that took place after his report of 1997 was communicated.[3141]

[2876] Rosen reiterated that C&L had to perform its 1988, 1989 and 1990 audits of Castor in accordance with GAAS, and that they had totally failed such duty.[3142] For example:

- C&L should have changed its audit strategy and audit procedures to take into account the changes in the reality of Castor (long term lender instead of short term – equity loans instead of mortgage loans), which they failed to do, whereas it was a matter of common sense.[3143]

- Management letters were "nice to have" but it did not relieve C&L from their duties. Management letters are not a substitute to gathering SAAE.[3144] An auditor has the obligation to gather SAAE: the very basis of GAAS is that management's assertions as set forth in the company's financial statements have to be verified.

- *"there's just so many places where Castor management made the evidence fully available, and yet, it was ignored by Coopers & Lybrand."*[3145]

- Facing a situation where there was an inconsistency, C&L had to "probe to the bottom", [3146] and they did not.

[3138] PW-2941, vol.1, pp. 159-
[3139] Section came into force in 1991 only
[3140] Froese, December 5, 2008, p. 142
[3141] Rosen, February 3, 2009, pp. 34-35
[3142] Rosen, February 17, 2009, pp. 35-37
[3143] Rosen, February 5, 2009, pp. 117 and following; PW-3034, pp. 9 and following
[3144] Rosen, March 24, 2009, p. 43
[3145] Rosen, March 24, 2009, p. 35

- Uncovering suspicious circumstances, C&L could not just let go[3147], and they did.

- Numerous warnings were available from the books and records of Castor and C&L's own AWPs, namely about the existence and extent of capitalized interest, financial problems of borrowers and the use of secrecy jurisdictions. C&L failed the take them into account.

[2877] Rosen opined that fraud was no excuse given the numerous failures of C&L, as revealed by the evidence reviewed, namely their failure to gather SAAE and the failure to provide a SCFP.

[2878] As Vance and Froese, Rosen listed warning signals, "red flags", which should have been identified by C&L and opined that had C&L act on them, they would not have issued their 1988, 1989 and 1990 unqualified audit reports.

In the circumstances, Fraud is not a defense

Levi's assertion as to "Co-conspirators" behaviour

[2879] Levi asserts that *evidence shows that Wolfgang Stolzenberg and his co-conspirators would have produced and did produce whatever documentation was required to satisfy the auditors in connection with concealing the fraudulent activities at Castor.* The Court disagrees.

Ron Smith

[2880] While he may not have volunteered information when C&L did not ask for it[3148], evidence shows that Ron Smith provided C&L with answers, information and documents that contradict Levi's assertion[3149].

[2881] C&L were provided with negative information by Castor (namely by Ron Smith), but the audits of Castor were never adjusted because of such information, while they should have been. As explained by Smith: «*In my reviews with the auditor, when he asked the questions and we did provide what I thought was negative information, there*

[3146] Rosen, February 3, 2009, pp. 85 -86

[3147] Rosen, February 3, 2009, pp. 86 and following

[3148] See as an example: Ron Smith, May 14, 2008, p. 92

[3149] See as examples : PW-1053-95, seq. pp. 183-231; PW-1053-97, seq. pp. 267-277; PW-1053-93, seq. p. 153; PW-1053-23, seq. pp. 155-166; PW-1053-19, seq. pp. 163-168; PW-1053-15, seq. pp. 161-162;. PW-1053-19, seq. p. 253; PW-1053-97, seq. p. 266; PW-1053-95, seq. p. 182; PW-1053-93, seq. p. 150; PW-1053-27, seq. p. 131; PW-1053-23, seq. p. 168; R. Smith, September 5, 2008, p. 40; PW-1053-23, seq. p. 117; Vance, April 15, 2008, pp. 15-18; PW-2941, Vol. 1, pp. 151-152; See also covenants specified in loan agreements.

was no difference in how he reacted with me as to when I provided him with the information that the project... or loan was acceptable.»[3150]

Prychidny

[2882] If it is true to say that, at the insistence of Stolzenberg and Dragonas, Prychidny signed a document in 1992[3151], while the date mentioned on it was 1989 and while the content was not accurate, it is something else to suggest that Prychidny would have produced or would have accepted to produce or would have upheld whatever documentation was required to satisfy C&L in connection with concealing the fraudulent activities at Castor. Prychidny explained the special circumstances of this signature, an isolated event. Without condoning Prychidny's gesture, the Court finds nevertheless his testimony credible and reliable.

Lawyers from McLean & Kerr

[2883] Four lawyers of the legal firm of McLean & Kerr testified at Defendants' initiative: Leonard Alksnis and Harold James Blake, who were partners of the firm then, and Christine Renaud and Soo Kim Lee, who were not (they were associates). The Court finds their testimonies credible and reliable.

[2884] During 1987, 1988, 1989, 1990 and 1991, Alksnis was the partner in charge of the Castor's file at McLean & Kerr. On behalf of Castor, he handled numerous legal matters relating to loans and real estate securities.

[2885] Alksnis testified on the various transactions described as year-end cash circles, including the "nasty nine loans" and he has explained McLean & Kerr's involvement in relation thereto[3152].

[2886] The only relevant involvement of Harold James Blake, Christine Renaud and Soo Kim Lee is their involvement at the end of 1990 or at the beginning of 1991 in relation to the "nasty nine" loans.

[2887] Harold James Blake testified no one ever mentioned to him that the transactions were secret or had to remain secret, or that he could not or should not talk about them if he was to receive a call from C&L or anyone else.[3153]

[2888] None of the four lawyers were ever contacted by C&L.[3154]

[3150] R. Smith, September 16, 2008, pp. 213-218
[3151] PW-463 and PW-463A; Prychidny, October 15, 2008, pp.168-171; Prychidny, November 3, 2008, pp. 86-140; Prychidny, November 10, 2008, pp.28-40
[3152] Alksnis, February 6, 2006, February 7, 2006 and February 8, 2006
[3153] Blake, June 18, 2009, pp. 200-201
[3154] Alksnis, February 8, 2006, p. 199; Blake, June 18, 2009, p.200; Renaud, January 26, 2006, p.70; Soo Kim Lee, January 25, 2006, p.196

[2889] The Court dismisses Levi's suggestion that evidence shows McLean & Kerr lawyers would have produced or would have accepted to produce or would have upheld whatever documentation was required to satisfy C&L in connection with concealing fraudulent activities at Castor.

[2890] Had C&L complied with GAAS and further investigated any of the year-end transactions, including the "nasty nine loans", as they should have, namely through communications with any of those four lawyers at McLean & Kerr after having requested and obtained Castor's consent, if and when needed, the Court has no reason to believe those lawyers would have said any more or any less than what they actually knew. Had Castor refused its consent, C&L would have had to question themselves as to the consequences of such a refusal.

The German banks

[2891] Levi asserts that three German banks were "*co-conspirators*" of Stolzenberg.

[2892] In his report, Levi writes the following which he applies to the three German Banks:

> The following description of **the open and intentional collusion by several banks** to assist Wolfgang Stolzenberg with his year end improvement of the Castor Holdings Ltd. balance sheet is nothing shor t of troubling.
>
> **Not only did the banks knowingly** provide significant amounts of money to Castor Holdings Ltd., **they did so knowing** that the **transactions were to camouflage** existing situations with related entities and would be reversed shortly after the year end.[3155] (our emphasis)

[2893] Regarding Bankhaus H . Auf hauser ("**BHA Bank**"), Levi writes:

> The Bankhaus H. Aufhauser participated with Wolfgang Stolzenberg in a series of **year end transactions** ("window dressing") which had as its **sole purpose** the **elimination of related party transactions from the balance sheet of Castor Holdings** Ltd. These transactions resulted in the conversion of indebtedness to related parties by Castor Holdings Ltd. to indebtedness to a bank. These transactions began as early as December 1985 and continued annually through to 1991 involving Castor Holdings Ltd. and or other related entities.
>
> Of note is the drastic increase in the amounts beginning in 1989, the time when the cash requirements of Castor Holdings Ltd. were escalating and the pressure was mounting to show a good balan ce sheet. [3156] (our emphasis)

[3155] D-1347, p.170
[3156] D-1347, p. 171

> By not explaining the true nature of the transaction, the bank has clearly become a co-conspirator of Wolfgang Stolzenberg in helping embellish the year end balance sheet and deceive the auditor.[3157]

[2894] Levi identifies eight transactions that would have involved Raulino, Unionmatex and Hertel Aktiengesellschaft, three entities he describes as related parties to Castor.[3158]

[2895] The first transaction of 1985 concerns Raulino. Six transactions, one every year from 1986 to 1991, concern Unionmatex. The last transaction, in 1991, concerns Hertel Aktiengesellschaft.

[2896] Regarding Bayerische Vereinsbank A.G. ("**BV Bank**"), Levi writes:

> The Bayerische Vereinsbank A.G. participated with Wolfgang Stolzenberg in a series of year end transactions overlapping the 1990 year end. These transactions had as their sole purpose the elimination of a related party transaction from the disclosure note of Castor Holdings International Finance N.V.'s financial statement and the conversion of indebtedness by Castor Holdings International Finance N.V. from a related party to a bank.[3159]
>
> This is yet another example of the control exercised by Wolfgang Stolzenberg over his co-conspirators in perpetrating his fraudulent scheme to improve Castor Holdings Ltd.'s balance sheet in all areas and to create documentation and transactions which concealled the true nature of the related party transactions from the auditors.[3160]

[2897] The transaction, in the amount of DM 8 million, involves Unionmatex.

[2898] Regarding Berliner Handels-Und Frankfurter Bank ("**BHF-Bank**"), Levi writes:

> The ING BHF-Bank Aktiengesellschaft participated with Wolfgang Stolzenberg in a series of year end transactions which had as its sole purpose the elimination of related party transactions in the disclosure note of Castor Holdings Ltd.'s financial statements. These transactions resulted in the conversion of indebtedness to related parties by Castor Holdings Ltd. to indebtedness to a bank. These transactions began in December 1983 and continued annually involving Castor Holdings Ltd. and or other related entities.[3161]

[3157] D-1347, p. 173
[3158] D-1347, p. 171
[3159] D-1347, p.174
[3160] D-1347, p. 176
[3161] D-1347, p.177

> Of note is the drastic increase in the amounts for 1989 and 1990, the time when the cash requirements of Castor Holdings Ltd. were escalating and the pressure was mounting to show a good balance sheet.[3162]
>
> These transactions, like the other bank window dressing, involved a loan from the bank to Castor Holdings Ltd. or Castor Holdings International Finance N.V. for the purpose of repaying notes payable to the respective related entity which increased the amount of bank debt on the Castor Holdings Ltd. balance sheet and eliminated related party loans on the same balance sheet.[3163]
>
> The ING BHF-Bank Aktiengesellschaft was not only assisting Castor Holdings Ltd. in falsely improving its balance sheet to eliminate related party transactions and deceive the auditor, they were also creating a balance sheet which would be viewed much more positively by the other German banks.[3164]

[2899] Levi identifies ten transactions, from 1983 to 1990. Four transactions concern Luerrsenwerft (1983, 1985, 1987 and 1990) and six transactions concern Unionmatex (1984, 1985, 1986, 1988 and 1989).

[2900] No witness asserts that the year-end transactions involving the three German banks improved the cash position of Castor. As a matter of fact, several witnesses testified that these transactions did not improve the cash position of Castor, and, in fact, had no adverse impact on the financial statements of Castor.[3165]

[2901] Representatives of the three German banks testified *viva voce* before the Court:

- Schreyer, formerly of BHA.
- Boberg, formerly of BV.
- Schoeffel, formerly of BHF.

[2902] The testimonies of those three witnesses, credible and reliable, establish that:

- The audit confirmation requests that were sent to the banks were "statements of open position", requesting the responding bank to confirm the correctness of the information set out on the attached statement.[3166]

[3162] D-1347, p.177
[3163] D-1347, p.178
[3164] D-1347, p.180
[3165] By way of example: Schreyer, August 24, 1995, pp. 54-55; August 25, 1995, p. 43; Boberg, January 14, 1997, p. 73; Rampl, August 25, 1997, p. 80-81; Reiners, May 6, 1997, pp. 138-139; Von Michaelis, February 11, 1997, pp. 66-67; Scholz, June 25, 1998, pp. 106-107
[3166] For BHA, the statements of open position audit confirmation requests, for 1988, 1989 and 1990, were filed by Schreyer as PW-3117. These 3 statements of open position had been produced by Defendants, with the permission of the Court, and were identified RVM-21 (1988), RVM-22 (1989), RVM-8 (1990). For BV, the statement of open position audit confirmation request for the DM8 million

- The banks responded, confirming the correctness of the information set out on the statement of open position requests.[3167]

    - Although the statements of open position did not request the banks to confirm whether the proceeds of the loan(s) were restricted or subject to any conditions, none of the banks considered, nevertheless, that the proceeds of such loans were restricted or subject to conditions. Had the statements of open position requested a reply, including information as to any restrictions on the use of the funds, the banks' reply would have been the same, i.e. no restriction on the use of the proceeds of the loans, because that is what the banks knew and believed.[3168]

    - There was no intention to deceive the auditor.[3169]

    - There was no "*lucrative fee*".[3170]

[2903] Riedel, formerly from Unionmatex, also testified[3171].

- Riedel was associated with Unionmatex from March 1970 to June 1995.[3172] From 1983 to 1992, Riedel was Unionmatex's managing director.[3173] He worked together with his two colleagues Clemens Broer and Rosemary Archner.[3174]

1990 year-end transaction (the only year-end transaction that BV was involved in), was produced by Boberg together with BV's reply of February 26, 1991, Exhibit PW-3128, on May 13, 2010, at p.167. Note: This statement of open position, together with the letter of February 26, 1991, is part of PW-1134, Bates No. 2572 and 2575 – the letter is in German, with no translation. A translation was furnished by Plaintiff during the testimony of Boberg and forms part of PW-3128. For BHF, the statements of open position audit confirmation requests were produced during the examination of Schoeffel: (PW-3137, for 1989; PW-3138 for 1990); PW-3137 was produced by Defendants as DR-93

[3167] These were prepared by Bänziger to whom C&L gave the control of the audit confirmation process (something the Court finds C&L should not have done). Bänziger chose to use the statement of open position form instead of a usual bank confirmation form. The same applies to the Gotthard Bank's situation.

[3168] Boberg, May 13, 2010, pp. 168-169; Schoeffel, May 14, 2010, p. 96. Schreyer, May 12, 2010, pp. 77-78, 82

[3169] Schreyer, May 12, 2010, p. 78, 82; Similar testimony with respect to the banks' replies to the audit confirmation requests can be found in several of the extracts of the examinations on discovery. By way of example, Rampl, August 28, 1997, Vol. 4, pp. 256-261; Von Michaelis, February 11, 1997, Vol. 2, pp. 53, 70

[3170] Schreyer, May 12, 2010, p. 48-50; PW-3114; Schoeffel, May 14, 2010, p. 60-62; also PW-3132.

[3171] Riedel, May 11, 2010

[3172] Riedel, May 11, 2010, p.11. p.80

[3173] Riedel, May 11, 2010, p. 59

[3174] Riedel, May 11, 2010, pp.11-12

- Before he testified, Riedel read a prior testimony rendered by his colleague Broer in another file (not in evidence before this Court), and he could attest that his testimony was to the same effect.[3175]

- Riedel was responsible for the cash management of Unionmatex. Riedel explained that the year-end transactions with Castor and German banks were done for Unionmatex's purposes. On its balance sheet, Unionmatex wanted to show deposits with German banks, not too many deposits with institutions abroad.[3176]

- To Riedel's knowledge, Stolzenberg was not involved with any of the companies, which owned Unionmatex, at least until January 1987.[3177]

- At all times, including after 1987, neither Stolzenberg nor anybody at Castor had influence on the cash management of Unionmatex.[3178]

- The deposits made by Unionmatex at German banks were never pledged or otherwise given as security to a loan made by a German bank to Castor. The only thing Unionmatex did was to give the banks an undertaking that some money would return to Castor after year-end, nothing else.[3179]

- The transactions changed nothing on the balance sheet of Castor: instead of owing money to a depositor, Unionmatex, Castor owed money to banks.[3180]

- Riedel never received any calls or communications from C&L.[3181]

[2904] During trial Plaintiff's counsel said, and they reiterated in their written submissions at the end of the trial, that "*some of the words and phrases used by Levi to describe the banks' participation in the year-end transactions are highly inflammatory, as well as defamatory*".[3182]

[2905] Levi's opinion as to the "sole purpose" of the year-end transactions, as set forth in his report, was the elimination of the disclosure of related party transactions from Castor's financial statements. In his cross-examination, Levi, however, said that his report had to be amended to read as follows: «*The sole purpose of the year end*

[3175] Riedel, May 11, 2010, pp. 24-34
[3176] Riedel, May 11, 2010, pp.13 and following, pp.70 and following, pp. 90 and following
[3177] Riedel, May 11, 2010, p. 38, p. 40, p. 44-49
[3178] Riedel, May 11, 2010, pp.40-41, pp.61-63
[3179] Riedel, May 11, 2010, pp. 51 and following, pp. 71 and following
[3180] Riedel, May 11, 2010, p.20, pp.52-53
[3181] Riedel, May 11, 2010, p.54
[3182] Written submission, July 8, 2010, p.261

transactions was the elimination of related party transactions and amounts due to directors, officers and shareholders, as well as their related parties.»[3183]

[2906] Therefore, Levi's opinion is based on the following premises, that need to be true at all relevant times:

- Unionmatex, Luerssenwerft, Hertel and Raulino were each, in its own right, related to Castor;
- Any transactions between Castor, on the one hand, and any of Unionmatex, Luerssenwerft, Raulino, or Hertel, on the other hand, should have been disclosed in Castor's financial statements, either as related party transactions, or as payments to directors, officers or shareholders.

[2907] These premises are not true as the Court will now explain.

Luerssenwerft

[2908] Luerssenwerft is a corporation that never was a shareholder of Castor even though it was one of its depositors.

[2909] C&L never considered Luerssenwerft to be a related party to Castor.

[2910] In 1988, C&L identified Friedrich and Peter Luerssen as related parties, but not Luerssenwerft.[3184]

[2911] Again, in 1990, and whereas Castor's books and records clearly showed an amount of $15.2 million outstanding to Luerssenwerft :

- Friedrich and Peter Luerssen are identified by C&L as shareholders and as related parties.
- Luerssenwerft is not identified as a related party[3185].

[2912] During his testimony, Levi said "*I never said Luerssenwerft was related*".[3186]

[2913] Referring to the year-end transactions with Luerssenwerft, Levi stated: "*No, first of all, these are not, as I said, related party transactions.*"[3187]

[3183] Levi, February 3, 2010, p. 63-74 and 100-101
[3184] Vance, April 15, 2010, p. 131-133; PW-1053-92, seq. p.162
[3185] Vance, April 15, 2010, p. 126, 128; PW-1053-88, seq. p. 163 Note: PW-1053-88, seq. pp. 152-167, seq. p 152 is the tick legend and list of CHIF's notes payable as at December 31, 1990, on which C&L identifies shareholders with a box, and related companies with a circle; seq. page 163 shows the Luerssens identified as shareholders, but does not identify Luerssenwerft, which is listed directly beneath them, as related.
[3186] Levi, February 3, 2010, p. 67

[2914] Levi's opinion that "*These transactions, like the other bank window dressing, involved a loan from the bank to Castor Holdings Ltd. or Castor Holdings International Finance N.V. for the purpose of repaying notes payable to the respective related entity which increased the amount of bank debt on the Castor Holdings Ltd. balance sheet and eliminated related party loans on the same balance sheet*" does not hold water.

Unionmatex

[2915] Unionmatex is a corporation and was never a shareholder of Castor.

[2916] In their AWPs, C&L have never identified or treated Unionmatex as a related party.

[2917] Unionmatex sued C&L in the Superior Court, district of Montreal.[3188] In their plea against that claim, dated July 31, 1996, C&L alleged that Unionmatex only became a related party to Castor in 1987.[3189] Yet, Levi refers to year-end transactions involving Unionmatex that took place in 1984, 1985 and 1986.

[2918] In his cross-examination, Levi said that he had not been made aware that a representative of Unionmatex had been examined on discovery, even though he had requested Defendants' counsel «*to have their paralegals provide me with any testimony which may be related to these transactions.*»[3190] Levi added that he had not either been made aware of the legal proceedings that had been instituted by Unionmatex against C&L, although he had requested copies of all litigation in connection with year-end transactions.[3191]

[2919] Levi was forced to acknowledge that if Castor and Unionmatex were not related parties for 1984, 1985 and 1986, he would have no choice but to change his opinion that the sole purpose of the year-end transactions was the elimination of the disclosure of related party transactions.[3192] Then, Levi said, the references to Unionmatex for the years prior to 1987 would have to be scratched out of his report.[3193]

[2920] Riedel testified that, over year-end, Unionmatex would withdraw a portion of the funds it had on deposit with Castor. The purpose was to show cash deposited with German banks on Unionmatex's balance sheet, rather than deposits with a foreign institution (Castor).[3194]

[3187] Levi, February 3, 2010, p. 117
[3188] PW-3110
[3189] PW-3111, paragraphs 192-193
[3190] Levi, February 3, 2010, p. 80 and 85
[3191] Levi, February 3, 2010, p. 98
[3192] Levi, February 3, 2010, p. 100
[3193] Levi, February 3, 2010, p. 110
[3194] Riedel, May 11, 2010, pp. 14-15

[2921] During lengthy discussions with Archner (head of Unionmatex's bookkeeping department), Riedel and Archner would determine how much money on deposit with Castor would be withdrawn over year-end, and how much of such sums would be placed with German banks, depending on the cash flow needs of Unionmatex.[3195]

[2922] Usually, it would be Archner who would contact the German banks with respect to the year-end transactions, but sometimes it would be Riedel himself.[3196]

[2923] Thus, the year-end transactions were done for the purposes of Unionmatex's balance sheet, and were effected solely for the benefit of Unionmatex.[3197] Unionmatex's balance sheet looked better if you had cash on deposit with German banks at year-end, in contrast to deposits with Castor. That was the main purpose of these transactions.[3198]

[2924] When asked if he believed that the effect would be to improve the cash position on Castor's balance sheets, Riedel replied: «*No*».[3199] Nor did he consider these transactions to be artificial or fictitious transactions,[3200] because «*it was normal business*».[3201]

[2925] Following Stolzenberg's acquisition of an interest in Unionmatex in 1987, Riedel confirmed that neither Castor nor Stolzenberg, nor any of Castor's employees, «*had any influence on our business and especially not on cash management*»,[3202] nor on the reason and decision with respect to the year-end transactions.[3203]

[2926] Riedel testified that: «*We did it for our purpose*»[3204], and he confirmed that at no time did any representative of C&L ever communicate with him, or to his knowledge, with Broer, to inquire as to the nature and purpose of the year-end transactions.[3205]

Hertel

[2927] Hertel was never a shareholder of Castor and there is no evidence whatsoever that Castor and Hertel were related parties; certainly, they were never treated as related parties by C&L.

[2928] Furthermore, the only impugned transaction with Hertel was for year-end 1991, not one of the three relevant years.

[3195] Riedel, May 11, 2010, p. 70
[3196] Riedel, May 11, 2010, pp. 68-69
[3197] Riedel, May 11, 2010, pp. 74, 90
[3198] Riedel, May 11, 2010, p. 90
[3199] Riedel, May 11, 2010, p. 20
[3200] Riedel, May 11, 2010, p. 21
[3201] Riedel, May 11, 2010, p. 24
[3202] Riedel, May 11, 2010, pp. 40-41
[3203] Riedel, May 11, 2010, pp. 40-41, 61-62
[3204] Riedel, May 11, 2010, pp. 52-53
[3205] Riedel, May 11, 2010, p. 54

Raulino

[2929] With respect to Raulino, Levi refers to only one year-end transaction, in 1985, for DM 10 million.

[2930] Levi admitted that he did not go into detail or look at C&L's AWPs with respect to any of the year-end transactions prior to 1988.[3206]

[2931] In C&L's audit working papers of 1985 for CHIF, C&L listed Raulino as a related party: [3207] this particular working paper lists notes payable to shareholders, C&L identifies Raulino as a related party and C&L indicates a balance owing to Raulino of $17 million. Faced with the content of this working paper, and taking into account the amount of the transaction he had identified as "fraud", Levi had no choice but to admit that there would not have been an elimination of disclosure of Raulino as a related party. The transaction with the German bank would only have reduced the quantum to be disclosed.

[2932] As Selman said, the issue of disclosure of related party transactions is qualitative, not quantitative: [3208] therefore, disclosure could not be eliminated even though the amount was reduced.

Management representation letters

[2933] Each year, Castor issued management representation letters to C&L stating generally that the information contained in the financial statements prepared to be correct. These letters were signed by Stolzenberg and Jurg Bänziger.[3209] Those letters stated namely that all balances with shareholders, affiliated companies and other related parties as of the end of the year had been identified and disclosed as such in the financial statements.

[2934] Some information contained in those management representation letters was inaccurate, namely information about related parties and restricted cash.

[2935] C&L was provided with inaccurate information, but management representation letters were no substitute to obtaining sufficient appropriate audit evidence, as Levi acknowledged[3210]. Inaccuracies in management representation letters do not exempt C&L from their professional obligations. To the contrary, had C&L complied with GAAS, they should have realized the information was inaccurate and moved their audit procedures, as suggested by expert Levi, from level 1 to level 2, if not level 3.

[3206] Levi, February 3, 2010, p. 91-92
[3207] PW-1053-98, seq. p. 228; Levi, February 3, 2010, p. 122-123
[3208] Selman, June 9, 2009, p. 246
[3209] D-1 and D-2
[3210] D-1347, p. 43

Year end cash circles

[2936] Starting at the end of 1987, Castor began to reallocate interest among YH loans namely through year-end circular transactions involving a number of checks exchanged with McLean & Kerr. At year-end, memos explaining the proposed transactions and outlining Castor's instructions were prepared by Mackay and were sent to McLean & Kerr, who proceeded accordingly[3211]. Castor did not disclose to C&L those memos that outlined which new loans were being used to pay interest. MacKay testified that he would never have shown these memos to C&L, as he would have been fired by Stolzenberg.[3212]

[2937] Nevertheless, C&L was aware of the capitalization of interests.

[2938] In Castor's file, what could be fraud on the investor or the lender is not necessarily fraud on the auditor. That distinction between a fraud on the reader (investor or lender) and a fraud on the auditor is well illustrated by the following comparison: Castor used the practice of capitalizing interest to create a false picture on the reader of its financial statements that interest was being received in cash, when it was not; however, Castor never hid this practice from C&L.

[2939] Suspicious circumstances existed. Furthermore, some were clearly identified and noted by C&L in their audit working papers.

[2940] Anderson, the well-known and respected authority in accounting and auditing said all experts who testified before the Court, writes:

> It is very important that auditors thoroughly document and review their work in order to meet the legal responsibility for the recognition of suspicious circumstances. In most of the court cases dealing with negligence in recognition of suspicious circumstances, the auditor's working papers themselves contained indications that things were not as they should be. **The greater danger seems to be not the failure to discover and document clues but the failure to recognize them as suspicious. A healthy skepticism should remain an important audit ingredient.**"[3213] (our emphasis)

[2941] In T&T 163 issued in January 1991, C&L wrote:

> "**Competent and sufficient audit evidence** continues to be **the foundation** for the auditor's opinion. Insufficient professional skepticism, illustrated by "auditing by conversation", or failing to obtain solid evidence to back up management's representations, can lead to audit problems. In the final analysis, auditors need to

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[3211] See for example: PW-173, PW-1056A-8; PW-1056A-9-1 to PW-1056A-9-7; PW-1056A-10; PW-1056A-11; PW-1056B-8; PW-1056B-8A; PW-1056B-9; PW-1056B-10-1 to PW-1056B-10-7; PW-1056B-11; PW-1056C-10-1 to PW-1056C-10-7; PW-1056C-11; PW-1056D-1C; PW-1056D-8

[3212] Mackay, August 26, 2009, pp. 29-30

[3213] Vance, PW-2908, vol.1, chapter 2, page 2-2 and 2-3

> step back and ask one of auditing's most fundamental questions: **Does it make sense?**"[3214] (our emphasis)

[2942] In 1988, 1989 and 1990, C&L failed to obtain sufficient appropriate audit evidence; rather, they proceeded through "*audit by conversation*".

[2943] In 1988, 1989 and 1990, C&L failed to document and review their work and to exercise professional healthy scepticism.

[2944] C&L never really stepped back and asked themselves "Does it make sense?"

[2945] Wightman admits that C&L could have refused to sign an audit report without qualification, or simply have refused to sign Castor's financial statements if C&L had been of the view that Castor's management was not taking appropriate LLPs:

> A I guess the first thing would be to assess the materiality of – the difference if - difference so - of mind so existed. Secondly would be to presumably recommend that a review be made of it, if there was a difference, and to make sure that COOPERS had all of the underlying facts relating to it to make sure that their assessment was being made in the proper manner, and with all the facts. To see whether they felt that management had applied the proper degree of focus to the situation, and failing being satisfied with all of those things, and again assuming that the provisions were not - were substantially misstated, ***I guess COOPERS could have advised that they were not prepared to sign the statements without qualification or not prepared to sign the statements at all.*** [3215]
>
> ***(our emphasis)***

[2946] Had C&L insisted on obtaining sufficient appropriate audit evidence, rather than simply accepting management's representations, they would not have been able to issue the unqualified audit reports and the consolidated audited financial statements they issued.

[2947] Had C&L documented and reviewed their work and exercised healthy scepticism, they would not have been able to issue the unqualified audit reports and the consolidated audited financial statements they issued.

[2948] Had C&L asked themselves "*Does it make sense?*", C&L would not have been able to issue the unqualified audit reports and the consolidated audited financial statements they issued.

[3214] PW-1420, tab 30

[3215] Wightman, September 29, 1995, Question 71, page 37 lines 5 to 25

[2949] To assume, as did Wightman and other C&L's audit staff members, that material matters had been cleared without any personal verification of the status of the issues and without any documentary evidence in the AWPs to support that conclusion was a fatal mistake that cannot be attributed to fraud or management misrepresentation.

[2950] Accepting the use of a SCNIA instead of a SCFP was a breach of GAAP that cannot be attributed to fraud or management misrepresentation[3216].

[2951] Levi assumed that C&L had obtained sufficient appropriate audit evidence in response to concerns they had raised: evidence shows otherwise.

[2952] As early as 1986, C&L recognized that up to 80% or 90% of Castor's off-shore revenue was comprised of capitalized interest and fees. C&L obviously understood that Castor was not receiving much of its revenue in cash.

[2953] Had C&L merely insisted upon obtaining the financial statements of borrowers called for in the loan agreements, and required by the loan evaluation questionnaires, C&L would have determined that Castor's borrowers were in default of their loan covenants, unable to meet their financial obligations to Castor, and that the loans were virtually all non-performing. In such circumstances, C&L would have had no choice but to ascertain that the purpose of the corporate loans to YH was solely to allow Castor to inflate artificially its revenue.

[2954] To illustrate the above, the Court refers to one loan made to YHDL, loan 1091 secured by an assignment of its interest in the Hazelton Lane project, but there are numerous similar situations in Castor's files:

- YHDL had to provide its audited financial statements, the audited financial statements of the Hazelton Lanes Co-Tenancy and its interim unaudited financial statements, and any other information on the project when requested by Castor[3217].
- YHDL could not and did not furnish audited financial statements or any of the other required financial information.
- YHDL failed to respect its loan covenants.
- Such a failure to respect loan covenants would have been readily apparent to any auditor conducting an audit in accordance with GAAS.

[3216] Vance, March 10, 2008, p.136
[3217] PW-1059-6, p. 4

[2955] In the context of account 046/Loan 1153, an account well known to C&L, Defendants' expert Selman acknowledged that «*it was quite obvious to the auditors that the YH companies involved were not able to pay that interest...*»[3218]

[2956] The Court agrees that Castor used the practice of capitalizing interest to create a false picture on the reader of its financial statements that interest was being received in cash, when it was not, but this practice was not hidden from C&L. It illustrates the distinction one needs to make, as Plaintiff's experts suggested, between a fraud on the reader and a fraud on the auditor.

[3218] Selman, June 2, 2009, pp. 10-11

The negligence issue as it relates to valuation letters

Positions in a nutshell

Plaintiff

[2957] Plaintiff pleads C&L knew that the purpose of the valuation letters was to set the fair market value for Castor's common shares.

[2958] Plaintiff submits C&L knew these valuation letters were being used in connection with Castor's fundraising efforts: the share valuation letters were used to induce investors and lenders to join and remain members of Castor's investment club.

[2959] Plaintiff adds C&L also knew the valuation letters were being relied upon by both current and potential shareholders, as justification for the price they bought and sold Castor's shares.

[2960] Plaintiff argues the valuation letters are clear opinions on the fair market value of Castor's common shares as at defined dates. The opinions are unrestricted and unlimited and recipients were entitled to rely upon them for the investment decisions.

[2961] Plaintiff suggests Defendants intended their opinion in the valuation letters to be the fair market value to be relied upon: in the valuation letters, they did not qualify or restrict their opinion, while evidence shows they did qualify or restrict opinions in other circumstances.[3219]

[2962] Plaintiff concludes that C&L did not follow the applicable standards and practices for the preparation of the share valuation letters. C&L was negligent and C&L should be held liable.

Defendants

[2963] Defendants argue the sole purpose of the valuation letters was to fulfill a requirement in the shareholders' agreement. They allege that the valuation letters were not intended to assist investors in their dealings with Castor but were merely intended to inform Castor's directors.

[2964] Defendants further argue that C&L was not aware that these valuation letters were provided to potential investors.

[3219] PW-1053-50B-1, seq. p. 166

[2965] Defendants add that several of the statements contained in the valuation letters were clearly management representations which did not constitute an opinion of C&L.

[2966] Finally, Defendants plead that, even if no mandatory reporting standards had to be followed when C&L completed its last letter issued in October 1991, C&L's valuation letters prepared from October 17, 1989 to October 22, 1991 were in compliance with the CICBV Code of Ethics and, most notably, articles 4.01 to 4.10 thereof dealing with the contents of valuation reports.

Additional evidence

Valuation letters: why and what for ?

[2967] During a 12-year period, between March 19, 1980 and October 22, 1991, C&L prepared and issued a series of 24 valuation letters[3220], each providing an unqualified opinion of the fair market value of the common shares of Castor but no opinion on the preferred shares or the debentures.

[2968] Those share valuation letters were prepared by Chartered Business Valuators ("**CBV**"), members of the Canadian Institute of Chartered Business Valuators ("**CICBV**"), namely by Bernard Lauzon and Jacques St-Amour,[3221] and Wightman signed most of them on behalf of C&L.

[2969] From time to time, C&L was asked to assist Castor as auditors and professional accountants in establishing the fair market value of its common shares. Except for the first valuation letter issued on March 19, 1980, it was always stated in the valuation letters that their purpose was "*to update previous letters relating to valuation of shares of Castor prepared at various dates*"[3222].

[2970] It was stated in the valuation letters updated by the valuation letters dated October 17, 1989 or October 22, 1991 that their intended use in connection with Castor's issuance of new shares was as follows:

> We understand that the **purpose** of our valuation **is** to assist you in establishing the fair market value of these shares in connection with a possible **issue of treasury shares** of the company[3223].

[3220] PW-6

[3221] PW-3037, Appendix 11; Defendants' Plea par. 402; Wightman, August 13, 1996, pp. 16, 34-35, 151-154; Kingston, March 9, 2009, pp.156-157

[3222] PW-6 (see also valuation letters dated March 10, 1986, March 4, 1987, March 9, 1988, March 9, 1989, October 17, 1989, February 28, 1990, September 28, 1990, March 6, 1991)

[3223] PW-6, valuation letter dated March 19, 1980 (see also valuation letters dated August 4, 1986, November 4, 1986, September 16, 1987, December 4, 1987, September 12, 1988)

> (...) the purpose of this updated valuation is to assist you in establishing the fair market value of these shares **in connection with further issues from treasury shares** of the company to take place on or about December 31, 1980[3224].
>
> We understand that the purpose of this update is to **report to the shareholders** of Castor at the upcoming annual meeting, to be held on March 11, 1983. The report **may also be used for** the possible **issue of additional shares**[3225].
>
> We understand that the purpose of this update valuation is to **report to the directors** of Castor at the upcoming meeting to be held on March 13, 1984. The report may **also be used for the possible issue of additional shares**[3226].
>
> (...) the purpose of this updated valuation is to assist you in establishing the fair market value of these shares in connection with possible **further issues of treasury shares** of the company to take place on or about December 31, 1984[3227].
>
> (Our emphasis)

[2971] The valuation engagement was completed by C&L as auditors and professional accountants. C&L routinely billed Castor for «*services in connection with establishing the fair market value of Castor's common shares*».[3228]

[2972] Wightman testified there was a link between the valuation letters and the mechanism referred to in the shareholders' agreement. Michael Dennis, a director and Castor's Corporate Secretary from 1988 to 1992, also mentioned such a link.[3229].

[2973] Widdrington made a connection between the October 17, 1989 valuation letter and the definition of "*valuation report*" found at page 4 of the Restated Shareholders' Agreement dated May 10, 1988:

> "valuation report" means the report of the auditors of the Company as to the fair market value of the equity shares of the Company as of the financial year end of the Company and reported to the shareholders at the annual meeting next following such year end, which report shall be prepared on a basis consistent with the assumptions used in prior years and shall be final and binding upon the parties[3230].

[2974] Wightman testified that the valuation letters were issued twice a year because Stolzenberg had major director's meetings that coincided with the issuance of the

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[3224] PW-6, valuation letter dated October 7, 1980 (see also valuation letters dated April 29, 1981, October 9, 1981, October 22, 1982, October 21, 1983)
[3225] PW-6, valuation letter dated March 3, 1983
[3226] PW-6, valuation letter dated March 6, 1984
[3227] PW-6, valuation letter dated November 14, 1984 (see also valuation letter dated March 19, 1985)
[3228] See, for example, PW-2372-26 (the invoice dated May 18, 1989.)
[3229] Dennis, September. 8, 1995, p. 67-68, PW-2378
[3230] PW-2382

letters[3231]. Dennis's testimony corroborates Wightman's testimony that the tabling of the fair market value opinions occurred at meetings of the board of directors.[3232] In fact, the issuance dates of the five last valuation letters coincided with the dates of the director's meetings[3233].

[2975] None of the valuation letters (and there are 24) refer to the shareholders' agreement: this is neither an oversight nor a mistake.

[2976] The restated shareholder agreement stipulated that the value was to be determined as at the prior year-end, being December 31. In seven of the twenty-four valuation letters issued, namely those issued on August 4, 1986, November 4, 1986, September 16, 1987, September 12, 1988, October 17, 1989, September 28, 1990 and October 22, 1991, C&L opined on value at various different dates other than December 31[3234].

[2977] Wightman denied knowing that the valuation letters were distributed to anyone other than the directors[3235]. In the circumstances thereafter described, Wightman's statement is neither credible nor reliable.

[2978] In a memo she sent to Wightman on March 2, 1983 (part of the 1982 AWPs) Christine Lengvari, a C&L employee, reported that Stolzenberg had told her that the purpose of the updated valuation letter was "*for possible new shareholders after board meeting*"[3236].

[2979] In a draft letter to Stolzenberg, found in the 1987 AWPs, Wightman stated that the purpose of the valuation letters was to assist Castor in increasing its capital.[3237]

[2980] Wightman explicitly acknowledged that the purpose of setting the fair market value was to enter and exit shareholders, as stated in a letter he sent to Stolzenberg on September 23, 1987:

> Because shareholders have come and gone over the years based on these valuations and **if you intend to raise additional capital in the future based on these valuations**, it would not be advisable to deviate the value paid significantly from our reports»[3238] (our emphasis)

[3231] Wightman, August 13, 1996, p. 106; Wightman, February 10, 2010, p. 154
[3232] Dennis, September 8, 1995, p. 67-68
[3233] PW-2378; PW-12-4; PW-14-1; PW-15, PW-51
[3234] PW-6 and PW-6-1
[3235] Wightman, February 10, 2010, p.138; Wightman, March 11, 2010, p.58, 77
[3236] PW-1053-50B-2 sequential page 493
[3237] PW-1053-50B-1, seq. pp. 166-168
[3238] PW-665-2, PW-1053-50B-1, sequential page 385

[2981] The 1989 AWPs show that shares were purchased as part of a capital increase at the price of $550,[3239] which corresponds to the value in the share valuation letter dated October 17, 1989. The valuation working papers contain many such documents showing subscriptions for new shares that referred to the subscription prices matching the values contained in the valuation letters.[3240] Moreover, AWPs also contain references to Castor's «*attempt to raise capital base*» and to increase deposits from European investors.[3241]

[2982] While Castor never had more than 14 directors, on March 8, 1991 Wightman sent to Stolzenberg 100 copies of C&L's valuation letter relating to fair market value at December 31, 1990[3242].

[2983] C&L's draft of the October 22, 1991 valuation letter, marked as «*S.V.P Urgent*»[3243], was prepared for the board meeting of October 24, 1991[3244] where Castor's directors discussed the need to raise additional funds. A special request had been made to C&L for Castor's fundraising purposes in the following circumstances:

> The Chairman reported that as a result of the current environment in the banking industry Castor had recently experienced a reduction or cancellation of certain of its credit facilities (particularly with the Japanese and French banks) which, together with the necessity for the Corporation to refinance certain of its mortgage loans (where other financing was not available to borrowers), was causing a liquidity problem for Castor, which the Chairman was working hard to solve. (...)
>
> The Chairman pointed out that the minimum target for raising funds should be $50,000,000 but ideally $100,000,000 to overcome the present situation and to look positively forward towards 1992. The Chairman also stated that further support of the present shareholders would be absolutely necessary. In that connection the Chairman reported that he had already secured additional capital subscriptions from existing shareholders for $1.5.million[3245].

[2984] Wightman testified that when Coopers prepared the valuation letter of October 22, 1991, he had not been advised that Stolzenberg had recently made a cash call on the shareholders and was organizing a board of directors meeting for that purpose.[3246] Again, this statement is neither found credible, nor reliable.

[3239] PW-1053-20, seq. p. 124
[3240] See PW-1053-50A, seq. pp. 23, 25 (National Trust purchased shares at the most current valuation letter price).
[3241] PW-1053-50A, seq. p. 75
[3242] PW-2679
[3243] PW-1053-50A, seq. pp. 14-18
[3244] PW-2400-124, PW-51
[3245] PW-51, p.3
[3246] Wightman, February 10, 2010, p. 153-154

[2985] There is no doubt in the Court's mind that C&L knew precisely why and how the valuation letters were being used: the share valuation letters were being used as a promotional tool to convince both the new and the current investors of Castor that the subscription prices were appropriate and the share valuation letters were included in the presentation packages sent to prospective investors.[3247]

[2986] In its valuation letters, C&L associated itself with information issued by Castor[3248].

The trends in performance

[2987] The trends in performance based on the book value calculation per common share as well as the fair market value opinion per common share are shown in graphic form in PW-2886 and PW-2886-1 respectively.

[2988] Looking at these trends, Defendants' expert Morrison admitted the results were "very exceptional" and that Castor's share valuation trend was more impressive than either that of the Bank of America or the Royal Bank of Canada during the same period.

[2989] In fact, over the period from year end 1984 to year end 1990, the fair market value of the common shares, as determined by C&L, more than tripled. The highest value ever ascribed to these share valuation letters was $580 per common share, as set out in the letter dated March 6, 1991, soon after the 1990 audited financial statements were issued, and it was achieved despite C&L's knowledge of a «*slowdown in the real estate market in North America*».

[2990] The value ascribed to the common shares of Castor by C&L in each of the valuation letters issued between 1989 and 1991 comprised a premium over the book value of such common shares. Morrison acknowledged that the reason that an investor would ever pay a premium over book value is primarily based on a forward-looking assessment of the future value of a given asset.[3249]

[2991] Less than 4 months before Castor's collapse, C&L continued to extol the virtues of Castor's business and to opine that the common shares had a value between $550 and $580.

[2992] The historical performance evidenced by C&L's opinions of value revealed to readers that Castor had successfully weathered a downturn in the economy that occurred in the early 1980s which suggested that Castor's management could steer Castor through tough times as well as have it benefit from a strong real estate market.

[3247] Simon, June 16, 2009, p. 53
[3248] PW-1419-2A, Section 5020, namely 5020.01 and 5020.04
[3249] Morrison, October 5, 2006, pp. 47-49

The valuation letter of October 17, 1989

[2993] On October 17, 1989, Defendants issued a share valuation letter for the value of Castor's common shares as at October 1st 1989.

[2994] Under a subheading "Scope of investigation", C&L namely wrote:

- *We reviewed the audited consolidated financial statements of Castor for the five years ended December 31, 1988 and the internal unaudited consolidated financial statements of Castor for the nine months ended September 30, 1989.*
- *We have discussed with officials the current make-up of the assets and liabilities and the estimated earnings for 1989*
- *In 1987, two debentures of $50 million each were issued.*
- *In 1988, a $10 million convertible subordinated debenture was issued to a shareholder. This debenture was to mature on September 30, 1994 (...) Commencing April 1, 1989, the debenture holder had the right to convert the debenture into equity units of the company. This right was exercised on September 30, 1989 and a portion of the debenture (...)was converted into (...) common shares based on $500 per common share(...)*
- *A dividend of $40 per common share was declared at the annual meeting in May 1989 and paid in July to all shareholders of record as at December 31, 1988.*

[2995] The share valuation letter of October 17, 1989 states the following under the caption Scope of Investigation: "*we reviewed the consolidated financial statements of Castor for the five years ended December 31, 1988 and the internal unaudited financial statements of Castor for the nine months ended September 30, 1989*". Nevertheless, Wightman was categorical: C&L did not perform a Section 8200 review[3250] of the unaudited interim financial statements at September 30, 1989 and C&L was not engaged to do such a review[3251].

[2996] Under the subheading "Main considerations in establishing value", C&L wrote:

- *Management estimates that net earnings in 1989 will amount to approximately $ 28 million, up from March's original forecast of $ 26 million.*
- *Consolidated net earnings of Castor amounted $22.2 million for the year ended December 31, 1988 compared to $16.1 million in 1987.*

[3250] PW-1419-2A
[3251] Wightman, February 10, 2010, pp. 150-151

- *For the nine months ended September 30, 1989, unaudited consolidated net earnings of Castor amounted to $21.5 million compared to $ 18.5 million for the corresponding period of the preceding year.*

- *The book value per common share, as at September 30, 1989, is $355.28 (Appendix)*

- *The major Canadian public trust companies are generally trading in the range of a price/equity ratio of 1.5 to 2.0.*

- *We understand that the company intends to maintain future dividend payments at $40 per share while retaining a greater portion of earnings to increase retained earnings and further improve the financial position of the company.*

[2997] Under the subheading "Opinion", C&L wrote:

- *In our opinion, the fair market value of the common shares of Castor, on or about October 1, 1989, is in a range of $525 to $ 550 per share.*

Between October 17, 1989 and October 22, 1991

[2998] In the 1990 AWPs,[3252] C&L recorded: «*As per S. Goulakos, the increase in rates is due to the deterioration of the economy over the past year and the difficulties faced by the real estate market. Banks just aren't willing to lend out money at prime rates for risky ventures....*».

[2999] C&L's internal materials provided, by year end 1990, that:

> «economic conditions similar to those that arose in 1982 are again having significant impact on the real estate industry. ... **The audit significance of appropriately assessing NRV increases as real estate markets decline**"[3253] and "Realizable values for real estate have dropped sharply in many areas of the country over the last several months. In many cases, this represents the reversal of a boom market ... **The real estate market problems affect** not only developers and other direct investors in real estate, **but also those who have made loans secured by real estate** .... This is the **time to be careful and conservative in assessing real estate values**.»[3254]

[3000] In 1990, despite specific knowledge of the problems with the economy, C&L began to vary the relationship between the price/equity ratio attributed to the common shares of Castor and the corresponding ratio accorded to public trust companies. In 1991, at a time when the price/equity ratio attributed to major Canadian public trust

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[3252] PW-1053-13, seq. p. 222
[3253] PW-1420, Tab 33, paragraphs 1 and 27 (in particular)
[3254] PW-1420, Tab 29, paragraph 2 under "*Valuation of Real Estate*"

companies had decreased to 1.0, C&L used a ratio as high as 1.4 for Castor, or more than a 40% premium over publicly traded trust companies.

[3001] At the wrap-up meeting between Wightman and Stolzenberg held on February 15, 1991, it was abundantly clear that Castor was not benefiting from the downturn in the economy and that there were problem loans in the Montreal portfolio representing millions of dollars. As a result of such problems, Castor's management undertook to take certain actions with respect to the MLV project during 1991: «*Capitalize no more interest or fully reserve*». Castor's management did not comply with their undertaking: interest continued to be capitalized on these loans throughout 1991 and such capitalized interests were part of the alleged net earnings[3255].

The valuation letter of October 22, 1991

[3002] On October 22, 1991, Defendants issued a share valuation letter for the value of Castor's common shares as at September 30, 1991.[3256]

[3003] Under the subheading "Main considerations in establishing value", C&L wrote:

- *Management estimates that net earnings in 1991 will amount to approximately $25 million, down from March's original forecast of $34.25 million, as the result of a decrease in the spread of interest rates.*
- *Consolidated net earnings of Castor amounted to $31.2 million for the year ended December 31, 1990 compared to $28.4 million in 1989.*
- *For the nine months ended September 30, 1991, unaudited consolidated net earnings of Castor amounted to $ 18.7 million.*
- *The book value per common share, as at September 30, 1991, is $455.77 (Appendix)*
- *Despite the slowdown in the real estate market in North America, management does not expect major adjustments to the company's mortgage portfolio or to the net earnings. In fact, because of the slowdown additional opportunities may be provided for Castor.*
- *The major Canadian public trust companies are currently trading at a price/equity ratio of approximately 1.0 compared to a range of 1.3 to 1.6 last year.*
- *We understand that the company intends to maintain future dividend payments at $40 per share while retaining a greater portion of earnings to increase retained earnings and further improve the financial position of the company.*

[3255] See PW-167
[3256] PW-6-1, Tab 24, at 4

[3004] Under the subheading "Opinion", C&L wrote:

- *In our opinion, the fair market value of the common shares of Castor, on or about September 30. 1991, is approximately $550 to $580 per share.*

[3005] Defendants' valuation working paper file for this opinion on value included a document entitled «*L'industrie canadienne de fiducie, prêt et épargne*»[3257] which indicated:

> «De plus, la valeur de l'indice autant du secteur fiducie, prêt et épargne que celui de l'ensemble des entreprises publiques a commencé à diminuer à partir de septembre 1989 et d'une façon plus prononcée en janvier 1990 à cause de la récession économique au Canada.
>
> (...)
>
> En 1990, la rentabilité des sociétés de fiducie a beaucoup diminué suite à l'augmentation du nombre de prêts douteux et certaines sociétés importantes de fiducie opéraient même à perte. A cet égard, Standard Trustco Limitée, une des importantes sociétés de fiducie, a déclaré faillite en avril 1991.»

Valuation and Professional standards

[3006] The CICBV Code of Ethics came into effect in June 1989[3258].

[3007] The disclosure standards for reports, CICBV 91-1, came into effect in June 1992[3259].

[3008] C&L's internal technical policy statement TPS-A-602[3260] purports to set forth formal control procedures for valuation assignments. The definition of a valuation assignment defines a valuation assignment as follows, at article 2:

> A **valuation assignment** for the purpose of this policy statement **is any assignment** in which the Firm will be called upon to either express an opinion on or estimate the absolute or relative value of any asset or right. On occasion, such assignments may require assigning a negative value to a disability, such as in an assignment to give a professional opinion on the quantum of damages suffered by an injured party. A valuation assignment for the purpose of this policy statement **would not include instances where the Firm is required to give an opinion as to whether or not a value has been properly determined by reference to a clear and uncontested formula previously agreed between the parties at interest**." (our emphasis)

[3257] PW-1053-50A, seq. p. 44-46
[3258] Kingston, March 10, 2009, p. 79-81
[3259] Kingston, March 10, 2009, p. 79-81 and 103
[3260] PW-1420-1B, issued on September 1, 1977 as revised on December 14, 1987

[3009] At trial[3261], Wightman suggested that C&L's mandate for the purposes of the valuation letters more closely identified with "*instances where the Firm is required to give an opinion as to whether or not a value has been properly determined by reference to a clear and uncontested formula previously agreed between the parties at interest*".

[3010] Such a suggestion constitutes an afterthought when we know that during discovery Wightman was not even aware of this technical policy statement.[3262] Moreover, it is a proposition that does not hold water given the content of the valuation letters[3263] and Wightman's own testimony that the method of valuation «*varied from time to time depending on circumstances and what the Valuations Department felt was most appropriate considerations*»[3264].

[3011] Section 5020.07 of the Handbook[3265] reads as follows:

> When a public accountant associates himself or herself with information by performing services in respect of that information, the public accountant discharges his or her professional responsibilities by:
>
> (a) complying with the related rules of professional conduct of his or her provincial Institute;
>
> (b) complying with applicable standards in this Handbook; and
>
> (c) determining whether he or she has appropriately communicated the nature and extent of his or her involvement with the information.

[3012] Sections 5020.08 and 5020.10 of the Handbook[3266] stipulate that a chartered accountant must follow the reporting standards of the Handbook relating to services when he or she associates himself with information relating to those services.

[3013] Since it is important that the content of any communication issued by a chartered accountant not imply that a service was performed when it was not, sections 5020.09 and 5020.10 of the Handbook invite an accountant, when he or she performs services in respect of information - and there are no reporting standards in the Handbook relating to those services - to consider whether a communication is necessary or not in order to avoid any misunderstanding by the client or third parties as to the nature and the extent of the accountant's involvement with that information.

[3261] Wightman, February. 10, 2010, p. 144-149 (see page 147, lines 8 to 15)
[3262] Wightman, August 13, 1996, p. 20
[3263] PW-6
[3264] Wightman, August 13, 1996, p. 65 (see lines 5 to 8)
[3265] PW-1419-2A
[3266] PW-1419-2A

Overview of experts' opinions

[3014] Experts for both the Plaintiff and the Defendants concur that year after year, the audited consolidated financial statements and the share valuation letters disclosed results that were nothing less than spectacular.[3267]

Plaintiff's experts

John Kingston

[3015] John Kingston ("**Kingston**") has a Bachelor of Commerce, from Queen's University, which he received with honours in 1975. He has two professional accreditations: he has been a fellow chartered business valuator ("**FCBV**") since 1982, and he is a fellow Chartered Accountant ("**CA**") registered with the Ontario Institute of Chartered Accountants since 1977[3268].

[3016] In 1975, Kingston began articling with Price Waterhouse and was in their audit group from 1975 to 1978. During that period, he also became part-time involved with the valuation group, a new group that emerged within Price Waterhouse. In 1979, he was asked to join that group on a permanent basis, which he did.

[3017] In 1981, Kingston was asked to join a competing accounting firm, Ernst & Whinney, with the specific mandate to create a valuation group for them.

[3018] In 1985, Kingston became a partner of Ernst & Whinney. With one of his partners, he created a set of policies and standards for valuation mandates and built up the valuation group.

[3019] Through the product of several mergers, Ernst & Whinney became KPMG.

[3020] Over the years, in terms of size, Kingston worked on valuation of companies from a sole proprietorship through partnership through large multinational corporations. In addition, in terms of industry, his assignments went from food industry to real estate, to financial institutions, to manufacturing operations, and to high-tech corporations. He was not a specialist of any particular area; rather, his expertise allowed him to handle valuations in almost every area.

[3021] In November 1999, when he left KPMG, Kingston established his own company, eMerging Capital Corp., focusing on emerging high growth companies. eMerging Capital Corp. primarily assists companies in sourcing capital so that they can continue

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[3267] Lowenstein, March 21, 2005, pp. 134-135; Lowenstein, March 23, 2005, pp. 61-62; Morrison, October 5, 2006, pp. 112-113; Morrison, October 10, 2006, pp. 198-199; Morrison, October 11, 2006, pp. 15-16
[3268] Kingston, March 9, 2009, pp.14-15; see also PW-3036

to survive and renders valuation opinions or estimates depending on the requirement of the client; occasionally, it renders accounting services.

[3022] Kingston is the author of a number of articles and textbooks. His textbook *Valuation of Businesses* was published in 1986, and was used by University of Toronto and York University. It was also listed on the recommended list of the Canadian Institute of Chartered Business Valuators.

Kingston's opinion

[3023] Kingston expressed the opinion that the share valuation letters were clearly an opinion on the fair market value of Castor's common shares, without any qualifications or restrictions whatsoever. Those letters were the result of the exercise of professional judgment,[3269] not the mere application of a pre-established formula[3270]. They were not estimates.

[3024] Kingston said the expression "fair market value" is well known and used in many publications.

[3025] Whether the reporting format is an opinion letter, a mini-report or a comprehensive valuation report, Kingston explained an opinion requires that all the work necessary to stand behind such an opinion be done, because it is assumed that all such work has been done. The reporting format does not take anything away from the value of the opinion; the reporting format is just a means of further disclosure of what was actually done by the valuator to arrive at his conclusion[3271].

[3026] Kingston pointed out C&L's dual capacity stipulated in each valuation letter *as auditor and professional accountant*, and explained its importance in terms of seriousness and reliability of the end product: as he said about a company, after management, the next most informed group of people are probably the auditors[3272].

[3027] Kingston emphasized that C&L did not place any limitations on the ways in which the share valuation letters could be used.[3273] Therefore, as CBVs, the authors would clearly understand that the readers would consider that the opinions expressed were unqualified, without any restrictions or limitations attached.

[3028] Kingston opined that C&L's internal material for valuation purposes, including C&L's checklist, which was in force at least since 1982[3274], was consistent with what valuators, including him, were using during the 80s[3275].

[3269] Kingston, March 9, 1989, pp. 66-67
[3270] Kingston, March 9, 2009, pp.66-67
[3271] Kingston, March 9, 2009, pp.67-68
[3272] Kingston, March 9, 2009, pp.71-72
[3273] Kingston, March 9, 2009, pp. 72-73, 116
[3274] PW-2314

[3029] Kingston pointed out that C&L's own material stipulated namely that:

- The checklist (an outline to assist the valuator to ensure that he has undertaken all the work that should be considered) should be used in every valuation assignment[3276];
- There should be a preliminary list of information required to proceed with engagement;
- All worked done should be documented in working papers;
- To the extent C&L felt there was not sufficient information provided to them in terms of their analysis, C&L had to note a restriction on the scope of review in the valuation letter;
- The report should include a definition of fair market value;
- C&L should summarize the general economic conditions at the valuation date as well as the short-term economic outlook at that time;
- C&L should obtain industries' statistical data and comparable, public and private companies' statistical data where available, and prepare a summary of this information;
- C&L should do a comparison of ratios between the valued company and the selected comparative industry group. C&L should do a review of the profitability and a review of the leverage;
- C&L should examine a reconciliation of income per financial statements and taxable income for the two years preceding a valuation date, for unusual or non-recurrent reconciling items;
- C&L had to ensure all restrictions and qualifications are clearly set out in the file and in the report, including a restriction that the report is not intended for general circulation, a restriction that the report should be used only for the stated purpose and a restriction in case of inability to expose the company to market;
- C&L had to consider the suitability of including a disclaimer paragraph noting that C&L had not carried out an audit or that C&L had not sought external verification of information provided by management[3277].

[3275] Kingston, March 9, 2009, pp.114, 121-122
[3276] PW-1420-1B (TPS-604)
[3277] PW-2314 ; Kingston, March 9, 2009, pp.122 and following

[3030] Even though there were no codified and binding professional standards until 1989 for the CBVs, Kingston opined that in the CBV community, most people knew each other and knew their respective practices and policies, which were fairly consistent between major firms.[3278]

[3031] Kingston testified that the CICBV 1989 Code of Ethics and the 1992 CICBV standard 91-1 were a codification of the existing practices and policies at the time C&L wrote its various valuation letters. The existing practices and policies of the 80s, he admitted however, were not mandatory standards before the Code of Ethics and the standard 91-1 came into force[3279].

[3032] Kingston opined that C&L did not follow the applicable practices and policies for the preparation of the share valuation letters, a proposition stated as correct by Selman if the Court was to conclude that the letters were valuation letters[3280].

[3033] Kingston expressed the opinion that C&L did not follow the applicable practices and policies in many respects, including, *inter alia*:

- the very limited and insufficient working papers in support of each of the valuation letters[3281];
- the very limited and insufficient analysis to support C&L's opinions[3282];
- the absence of rationale to support the valuation method chosen by C&L to evaluate the shares of Castor[3283];
- the lack of analysis of the financial statements in terms of trends and ratios[3284];
- the absence in the C&L working papers of a list or a summary of the questions discussed with management and answers provided thereto[3285];
- the failure of C&L to document in their working papers any discussions to reconcile their conclusions on the results of different valuation methods[3286];
- the failure of C&L to conduct any comparability review on the trust companies selected as comparable to Castor.[3287]

[3278] Kingston, March 9, 2009, p. 99
[3279] Kingston, March 10, 2009, p. 81 and 99 and following
[3280] Selman, May 25, 2009, p. 76
[3281] Kingston, March 9, 2009, pp.89 and following
[3282] Kingston, March 9, 2009, pp. 89-90
[3283] Kingston, March 9, 2009, pp.90-91
[3284] Kingston, March 9, 2009, pp.89-90
[3285] Kingston, March 9, 2009, p.90
[3286] Kingston, March 9, 2009, pp.87-88
[3287] Kingston, March 9, 2009, p. 90

[3034] Kingston concluded: «*In summary, there is just a consistent lack of analysis and review, including comparability review, undertaken to support the conclusions on fair market value. The working papers are [...] in contravention of a number of different CICBV policies. They are in contravention of C&L's own checklist.* »[3288]

[3035] Kingston did not attempt to determine the fair market value of Castor's shares at any stated date. His role was to provide an opinion to the Court on the valuation work performed by C&L. However, after having identified numerous errors committed by C&L and, in an attempt to demonstrate to the Court the impact of such mistakes on the calculation of the fair market value of Castor's shares, Kingston demonstrated that C&L should have concluded that the fair market value of Castor's shares could be as low as nil for the period between 1988 and 1991.

Lowenstein

[3036] Lowenstein, a plaintiff's expert on reliance, noted the following paragraph in the valuation letter dated October 22, 1991:

> "Despite the slowdown in the real estate market in North America, management does not expect major adjustments to the company's mortgage portfolio or to the net earnings. In fact, because of the slowdown additional opportunities have been provided for Castor."[3289]

[3037] And Lowenstein opined that "*for a conservative careful institution or organization, such as a major accounting firm* (such as C&L), *to incorporate that in a valuation report suggests that before doing so -- one would expect that before doing so, they would be very confident in that statement.*" [3290]

Defendants' expert Selman

[3038] Selman discusses the valuation letters in his written report, but as he reiterated during his cross-examination on qualification, he did not consider those valuation letters as valuation reports[3291]. In fact, Selman opined that the standards were not applicable to the valuation letters in this case; Selman believed the valuation letters were intended to meet the requirement of the shareholders' agreement[3292].

[3039] If the Court was to conclude otherwise, Selman acknowledged, he had no quarrel with the practices and policies described by Kingston[3293].

[3288] Kingston, March 9, 2009, p. 91
[3289] PW-6-1, Tab 24, at page 4
[3290] Lowenstein, March 21, 2005, p.189 (see lines 13 to 17)
[3291] Selman, May 4, 2009, p.187
[3292] Selman, May 22, 2009, p.124 (see lines 7 to 9)
[3293] Selman, May 22, 2009, p.136

[3040] Selman agreed that the valuation letters did not accord with the Canadian Institute of Chartered Business Valuators standards.[3294]

[3041] Selman indicated that Coopers & Lybrand had not signed the letters as CBVs or stated that they were prepared by Coopers & Lybrand acting as CBVs. Rather the valuation letters were signed by C&L as auditors and professional accountants[3295].

[3042] Selman mentioned the definition of "*fair market value*" included in the restated shareholders agreement.

> "*fair market value*", when applied to shares of the Company, means (i) in respect of preferred shares, the stated capital amount thereof,. and (ii) in respect of equity shares, the fair market value thereof conclusively determined by the applicable valuation report, plus an amount equal to the anticipated dividends, if any, referred to in such report and deducted in determining fair market value which are attributable to the equity shares for which fair market .value is being determined hereunder, if such dividends have not been paid on such equity shares prior to the closing of the sale and purchase thereof;[3296]

[3043] This being done, Selman opined that there were many definitions of the expression "*fair market value*", since shareholders of a company need not use the definition of fair market value used by valuators or the legal definition of fair market value[3297].

[3044] Selman said it would have been clear to any reasonably experienced investor that these letters were not comprehensive valuations of Castor's stock and did not contain the type of analysis that a reasonably experienced investor could rely on.[3298]

[3045] Selman added that the comparison of a private company's stock with publicly traded stocks was, of itself, superficial[3299] and that a comparison with the major Canadian trust companies was not useful[3300].

[3046] Finally, Selman pointed out that what C&L had done was not a review within the meaning of Section 8020 of the Handbook, contrary to what other experts had suggested.

[3047] Selman stipulated that if the audited financial statements were materially misstated and misleading, so were the valuation letters.

[3294] Selman, May 22, 2009, p.136
[3295] Selman, May 22, 2009, p.126
[3296] PW-2382
[3297] Selman, May 22, 2009, pp.127-128
[3298] Selman, May 22, 2009, p.125, 130
[3299] Selman, May 22, 2009, p.131-132
[3300] Selman, May 22, 2009, p. 131

[3048] In cross-examination, Selman said:

> That's why I have said all the way through this thing that I view these things as a chain of letters that remain there to meet the requirements of a group of shareholders under a shareholders agreement, and they were nothing more.
>
> So I don't see, reading the whole of the letter that someone would be with... an experienced person would review it as a opinion of value prepared in a normal fashion. **The wording is unfortunate, no doubt**, but I still don't believe that the letters are intended to express that or do they imply that to somebody who's experienced in reading it[3301]. (our emphasis)

[3049] When asked what he meant by "*the wording is unfortunate, no doubt*", Selman added "*it would have been nice if they had used some terminology that indicated that it was a limited expression*"[3302].

[3050] Cross-examination revealed that Selman had significantly softened his remarks in his 2008 written report, as compared to his 1998 report, concerning C&L's responsibility for the content of its valuation letters, those changes being done according to Selman to "*improve*" his report[3303].

- Although Selman had previously stated that the valuation letters did not meet the standards of the Canadian Institute of Chartered Business Valuators and the valuation practice,[3304] he omitted that statement from his 2008 report.
- Selman made a statement in paragraph 6.06 of his 1998 report that Wightman was not a member of the CICBV and not personally bound by its standards. He omitted that statement from his 2008 report.[3305]
- Although his 1998 report stated that C&L's comparison to trust companies was insufficient and not valid,[3306] Selman's 2008 report states that the comparison was merely "superficial" and not "useful".[3307]
- Selman's previous text that the valuation letters did not address the different risks between Castor and the trust companies was omitted from his 2008 report. He similarly omitted text that interprets a decrease in Castor's investors' yields to mean that the implied risk of the Castor shares was being described as significantly decreasing.[3308]

[3301] Selman, May 25, 2009, p.79
[3302] Selman, May 25, 2009, p. 79
[3303] Selman, May 25, 2009, pp.127, 128, 129, 133 and 134
[3304] PW-3049, paragraph 6.06
[3305] PW-3049, p. 179; Selman, May 25, 2009, pp. 124-127; May 26, 2009, pp. 185-186
[3306] PW-3049, paragraph 6.2
[3307] D-1295, p. 378
[3308] Selman, May 26, 2009, pp. 177-180. See PW-3049, paragraphs 6.02, 6.03

- Selman excluded, from his 2008 report, the following statement from paragraph 6.04 of his 1998 report[3309]:

  «Notwithstanding, I am of the view that it would have been better to issue them with a clearer warning that the expression of opinion was based on very limited assumptions and might not be appropriate for the reader's purposes.»

[3051] It is noteworthy that Selman was not prepared to acknowledge that saying the following was a criticism of C&L :"*it would have been better to issue them with a clearer warning that the expression of opinion was based on very limited assumptions and might not be appropriate for the reader's purposes*".[3310].

[3052] It is also noteworthy that Selman was unable to explain why all the other above mentioned changes had been made to his report.[3311]

Analysis and conclusions

Misleading information and overstated valuation

[3053] The key elements of the methodology followed for determining the fair market value of Castor's shares are apparent from the contents of the letters themselves: the financial statements of Castor, audited and non-audited, the net earnings, the 100 million debentures transaction and the $40 million of dividends are such key elements.

[3054] The corollary of the conclusions previously reached regarding the consolidated audited financial statements, the net earnings and the 100 million debenture transaction, are that :

- C&L used materially misstated and false information;
- Castor's common shares could not and should not have been valued as they were;
- The valuation letters issued between January 1, 1988 and October 22 1991 presented inappropriate and misleading information.

[3055] Even though the "fair market value" of Castor's common shares at October 1st 1989 and September 30, 1991 has not been precisely established - and in the circumstances, it was not necessary- the Court does not hesitate to conclude that the fair market value of Castor's common shares, as of these dates, was nowhere close to

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[3309] Selman, May 25, 2009, pp.127-128
[3310] Selman, May 25, 2009, p.10,131-132
[3311] Selman, May 25, 2009, pp. 51-52, 127-129, 131; May 26, 2009, pp. 151-157, 171-176

the values mentioned in the valuation letters dated October 17, 1989 and October 22, 1991.

Purpose and valuation letters

[3056] There was a link between the valuation letters and the restated shareholder agreement, i.e. the valuation letters were used as the "valuation report" mentioned in the restated shareholder agreement. Therefore, to provide this tool might have been one of the purposes for which C&L's services were retained, but it was not "*The purpose*", as Defendants suggested.

[3057] Defendants' position that the valuation letters would have been issued for the sole purpose of the shareholders' agreement does not hold water:

- The letters were issued more often, and on different dates, than the restated shareholders' agreement mandated;
- All the valuation letters contain specific wording as to purpose;
- None of the twenty-four valuation letters refer to a shareholders' agreement; and
- C&L admitted that a purpose of the valuation letters was to «*assist the company in establishing the fair market value of its shares in connection with further issues of treasury shares of the company*».[3312]

Nature of opinion

[3058] A basic reading of the share valuation letters reveals that they are unqualified opinions by C&L of the fair market value of Castor's common shares.

[3059] Without a definition of "fair market value" mentioned in the valuation letters, reference to the definition used by valuators is appropriate.

Negligence

[3060] C&L were negligent.

[3312] Defendants' Plea dated July 31, 1998, paragraph 401.; Decision of this Court on May 20, 2009 (transcription May 20, 2009, pp.6-30 and Trial minutes May 20, 2009); leave to appeal denied, P. Dalphond J.A. dated October 7, 2009 [2009] QCCA 1890; decision dated February 3, 2010, [2010] QCCS 453; leave to appeal denied, decision A. Rochon J.A. dated April 16, 2010, [2010] QCCA 714

[3061] The Court shares Kingston's point of view, Kingston's opinions, which rest on an appropriate understanding of the evidence.

[3062] Selman's opinions, resting on the basic premises that the sole purpose of the valuation letters would have been to comply with the terms of a shareholders' agreement and that C&L was ignorant of any other use, do not hold water.

[3063] The valuation letters were valuation reports of the fair market value of Castor's common shares to be used and used for fund raising purposes and C&L knew it. In the absence of disclaimers, qualifications or restrictions, readers were allowed to take them at their face value, as valuation of the fair market value of Castor's common shares prepared by auditors and professional accountants.

[3064] Notwithstanding the clear and precise internal policies and practices in force at C&L at all relevant times, there were no disclaimers, no qualifications and no restrictions in C&L's valuation letters. C&L never once mentioned the shareholders' agreement in the twenty-four valuation letters it issued.

[3065] The absence of disclaimers, of qualifications, of restrictions and of mention of the shareholder agreement was not an oversight; it was a conscious gesture.

[3066] Playing with words was far from complying with C&L's own standards and with applicable policies and practices of valuation.

[3067] C&L associated themselves with Castor's financial information and general information, with Castor's unaudited financial statements and with perspectives on the state of the economy, on the state of the lending business and on its opportunities for Castor. Contrary to section 5020 of the Handbook, they did not appropriately communicate the nature and extent of their involvement with the information, while such a communication was necessary to avoid misunderstanding.

[3068] The Court of Appeal acknowledged that, even though the provisions of the Handbook or of the CICBV are not binding on the Court, such dispositions are useful to determine if there is a fault:

> «On nous a également fait longuement état des pratiques comptables généralement reconnues et des dispositions du Code de déontologie des comptables agréés. Eu égard à ces normes qui, si elles ne lient pas le Tribunal, ont cependant une **utilité indiscutable** dans la détermination de la faute, je suis d'avis que les comptables intimés ont effectivement commis des fautes civiles.»[3313]

[3313] *Caisse populaire de Charlesbourg c. Michaud,* [1990] J.Q. no 673 at 8 (Qc. C.A.). See also *Malo v. Michaud*, [1993] R.R.A. 760 at para. 78, AZ-93021590, J.E. 93-1551

[3069] It is true to say that C&L's valuation letters were not comprehensive reports, in the format. Nevertheless, they were unqualified professional opinions issued by a well-known and respected chartered accounting firm having, as Castor's auditors since its inception, full and detailed knowledge of Castor's business and Castor's financial situation.

[3070] Therefore, having issued twenty-four valuation letters on Castor's common shares fair market value attesting to exceptional results, C&L cannot reasonably argue that readers should have granted very little credibility, if any, to their valuation letters. As my colleague Justice Benoît Emery wrote:

> «[29] [...] Ainsi, un professionnel ne peut affirmer qu'un terrain est propre à la construction d'un édifice pour ensuite plaider que le degré d'analyse est à ce point superficiel qu'il ne faut pas accorder beaucoup de crédibilité à la conclusion.
>
> [30] [...] Si tant est que le niveau d'analyse du type Phase I est à ce point superficiel, le tribunal est d'avis que le professionnel ne peut alors certifier qu'on peut ériger sur ce sol un édifice de type résidentiel, commercial ou industriel. Face à une conclusion aussi affirmative, une personne raisonnablement informée comme l'acheteur en l'espèce est en droit de s'attendre au bien-fondé de cette assertion. D'ailleurs, même si le rapport P-2 est adressé à la venderesse, la défenderesse savait que ce rapport allait être utilisé pour les fins de la transaction avec la demanderesse.»[3314]

[3071] Before lending its name and reputation to any statements in a valuation letter, C&L should have done the appropriate work to satisfy itself of the accuracy of any such statement. Otherwise, C&L should have included clear and precise disclaimers, qualifications or restrictions into its valuation letters.

[3072] While an accountant who prepares a simple balance sheet may not be responsible if the numbers provided to him by his client are false, the same cannot be said of a share valuation letter, where the auditor attaches his professional opinion to the statement without qualification or restrictions, attesting therefore to third parties that he has followed the appropriate procedures and verified the accuracy of the information that he has provided[3315].

[3073] As Kingston explained, there were many steps C&L ought to have taken before issuing their valuation letters that C&L did not take. For example :

[3314] *3979687 Canada Inc. c. Les Consultants LBCD Inc.* [2010] QCCS 905, paragraphs 29-30 (j. Emery), AZ-50616047, J.E. 2010-664

[3315] *Caisse populaire de Charlesbourg* c. *Michaud*, [1990] R.R.A. 531 at 2 (Q.C.A), AZ-90011568, J.E. 90-814

- C&L were aware of the increased risk to Castor's portfolio because of the downturn in the real estate market well before they issued the October 1991 valuation letter and they acted as if such risk did not exist.

- In 1990, Wightman recorded the information that Hotels were in a difficult position because of declining interest rates and recorded the decision to cease capitalizing interest on these loans.[3316] In fact, Castor's management did not cease the capitalization of interest - which is evident in the general journal and the mortgage and loan ledger cards - but C&L did nothing to confirm that management was fulfilling its commitments prior to their issuance of the share valuation letters in March and October 1991.

[3074] Playing with words is not acceptable; everyone has to face its doings.

[3316] PW-1053-12, seq. p. 84. See also PW-6-1, Tab 23 and Tab 24 and PW-167D

The negligence issue as it relates to Legal for Life Certificates

Positions in a nutshell

Plaintiff

[3075] Plaintiff argues that:

- The Court has judicial notice of the various statutes under which the Legal for Life Opinions were issued. Therefore, no evidence was needed.
- If the Court concludes that the audited financial statements were materially misstated, she must conclude that the Legal for Life Certificates were misstated as well.
- By incorrectly certifying that Castor met the requisite tests to enable it to hold itself out as a safe and creditworthy investment worthy of Legal for Life Status, Defendants acted negligently and committed a fault.

Defendants

[3076] Defendants argue that:

- The Court does not have judicial notice of the various statutes since, for article 2809 CCQ. to apply, the statutes needed to be specifically alleged in the proceedings, and they were not.
- There is no evidence of the standards for the preparation of Legal for Life Certificates, nor of the criteria dictated by the various statutes under which the Legal for Life Opinions were issued. Therefore, it cannot be said that Legal for Life Certificates contained errors and were materially misleading.

Additional Evidence

[3077] Simon's principal responsibility was to find depositors or lenders. For that purpose, he maintained and updated information material that Castor had available[3317].

[3317] Simon, April 23, 2009, p. 113

[3078] Firstly, he developed relations with various European banks and their subsidiaries in Canada and the United states[3318].

[3079] Secondly, he explored the market of financial institutions such as trust companies, insurance companies or pension funds and found that in order to invest in Castor those institutions needed a Legal for Life Opinion[3319].

[3080] The tests of eligibility for Legal for Life Status were derived from the *Canadian and British Insurance Companies Act* ("**CBICA**"). Particularly, section 63 CBICA limits investments to companies that meet the tests provided therein.[3320]

[3081] Financial results on a period of five consecutive years were needed to obtain a Legal for Life Opinion[3321]. Therefore, after the 1983 audited financial statements were completed, Castor sought a Legal for Life Opinion[3322].

[3082] C&L prepared a letter confirming that Castor met the tests. C&L's certificate was conveyed to Castor's legal counsel McCarthy Tétrault. McCarthy Tétrault sought to verify with the various provincial jurisdictions through local counsel that Castor, based on C&L's certificate, qualified for investments by trust companies, insurance companies, trustees, pension funds, and that those financial institutions could invest money with Castor without resorting to a special provision[3323].

[3083] That done, McCarthy Tétrault issued a Legal for Life Opinion to the effect that Castor's shares or notes could legally be acquired by various financial institutions governed by various statutes listed in their Opinion[3324] .

[3084] From 1984 and thereafter, C&L and McCarthy Tétrault repeated the exercise each year and provided Castor with a Legal for Life Status.

[3085] These Legal for Life Opinions were addressed and provided to Stolzenberg, as Castor's chief executive officer. The various statutes on which Castor's lawyers opined[3325] required that the auditor of the company confirm the necessary financial information. The Legal for Life Opinions issued by McCarthy Tétrault were based on Legal for Life Certificates issued by C&L.[3326]

[3086] In their Legal for Life Opinions, McCarthy Tétrault explicitly stated that they had received and examined C&L's certificate on which they were relying.

[3318] Simon, April 23, 2009, pp.114-115
[3319] Simon, April 23, 2009, p.116
[3320] PW-1420-1B, TPS-A-405
[3321] Simon, April 27, 2009, p.102-103
[3322] Simon, April 23, 2009, p.117
[3323] Simon, June 16, 2009, pp.69-70
[3324] PW-7
[3325]
[3326] PW-7

[3087] The document provided by Castor to any potential investor was the Legal for Life Opinion itself, not the certificate of the auditor[3327].

[3088] Simon used Legal for Life Opinions, specifically to raise money from insurance companies, trust companies, pension funds and trustees, but he also used the information memorandum and the Legal for Life Certificate, contained in the Legal for Life Opinion, as general marketing tools since having such Legal for Life Status said something about the creditworthiness of Castor and the quality of an investment in Castor[3328].

[3089] As Simon said, Legal for Life Status was useful as a form of endorsement of the credit quality of Castor since Castor did not have a rating from any rating agency.[3329]

[3090] Legal for Life Opinions enabled Castor to attract investments from institutional investors, such as pension funds and generally gave Castor the appearance of being a safe investment.

[3091] Castor's brochures including the five-year summary of the audited financial statements and the reference to Castor's Legal for Life Status were being used by lenders and investors contemplating doing business with Castor.[3330] Wightman kept such brochures in his office[3331] and on occasion, distributed them to third parties contemplating doing business with Castor.[3332]

[3092] The Legal for Life Certificates were a «*significant affirmation of the financial health of the company*»[3333] which were intended to be relied upon by third parties «*as a form of endorsement of the credit quality of Castor*».[3334]

[3093] While Wightman denied at trial knowing the use of the Legal for Life Certificate,[3335] the evidence is clear that he knew[3336] and, in fact, used the Legal for Life Status to promote Castor.[3337]

[3094] While Wightman would not admit the general impact of this designation on the perception of Castor as a safe investment, he found it relevant to explain Castor's Legal

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[3327] PW-2374
[3328] Simon, June 16, 2009, pp.75-76, 79, 80, 81 ; see PW-2473, PW-2474-2 and D-187
[3329] Simon, June 16, 2009, p.81 (see lines 11 to 18)
[3330] PW-1057-1, PW-1057-2, PW-1057-3; Wightman, March 11, 2010, pp. 36-38; Wightman, September 13, 1996, pp. 109-110
[3331] Wightman, March 11, 2010, p. 38
[3332] Wightman, February 10, 2010, p. 131
[3333] Lowenstein, March 21, 2005, p. 159, line 9
[3334] Simon, June 16, 2009, p. 81
[3335] Wightman, February 10, 2010, p. 139
[3336] Wightman, March 10, 2010, pp. 85-86
[3337] PW-1053-6, seq. p. 103-105

for Life Status to one of his partners at C&L in Germany whose client was considering depositing with Castor:

> «Castor is not a bank in Canada, but is a mortgage lending company and is qualified for issuing notes to major institutions in Canada including life insurance companies, pension funds, trust companies, etc.»[3338]

[3095] C&L's technical policy statement, TPS-A-405, implies that due to the complexity, professional judgment must be exercised in determining eligibility for this significant status.[3339]

[3096] C&L's internal policy on the preparation of such certificates recognized the goals of obtaining Legal for Life Status indicating that «*most corporate issuers attempt to establish their securities as being legal for life because insurance companies represent a large share of the investment market and because eligibility under these provisions is often considered to indicate a certain level of quality and liquidity in the security.* »[3340]

Experts' opinions

[3097] Vance opined the Legal for Life Certificates contained errors and were materially misleading[3341].

[3098] As he explained, with respect to the misleading nature of the 1988 certificate, Castor would not have met the required tests for Legal for Life Status had the audited financial statements reflected the required loan loss provisions.[3342] The Legal for Life Certificates were all based on compliance with specific tests over a five year period which depended on the results in the audited financial statements and subsequent calculations.

[3099] Lowenstein explained Legal for Life Opinions was a validation that the company had had a strong five year record, sufficiently strong that the company's securities would qualify as an investment for major financial institutions[3343], a validation of the financial health of Castor.[3344]

[3100] Because the certificates are prepared for the very purpose of being relied upon for investment decisions, particularly by investors that require safe investments, their preparation, according to Plaintiff's expert Lowenstein, required «*the same level of care*

[3338] PW-1053-6, seq. p. 103
[3339] PW-1420-1B: "*the tests set out in the act to determine the eligibility of corporate securities are lengthy and complex and present a number of difficulties of interpretation.*"
[3340] PW1420-1B, TPS-A-405
[3341] Vance, March 5, 2008
[3342] Vance, March 5, 2008, p. 101
[3343] Lowenstein, March 21, 2005, p.153
[3344] Lowenstein, March 21, 2005, p.155, 159, 163

that an auditor is expected to exercise in signing an opinion letter of financial statements».[3345]

Conclusions

[3101] The Court has judicial notice of the various statutes mentioned in the Legal for Life Opinions of McCarthy Tétrault[3346].

- Those statutes are either federal legislation, Quebec legislation or legislation from various other Canadian provinces;
- From the proceedings, it was obvious the Legal for Life Certificates were at issue as well as C&L's work relating thereto. Defendants knew it and cannot seriously argue they would have been caught by surprise;
- Article 2809 of the CCQ applies.

[3102] The misstatements in the Legal for Life Opinions were the direct consequence of the misstatements in the certificates provided by Defendants.

[3103] Castor's Legal for Life Status accomplished the goal of indicating the credit worthiness of Castor and the quality of an investment in Castor.

[3104] It was reasonably foreseeable to C&L that third parties would rely on this status as indicating «*a certain level of quality and liquidity*» because same is explicitly foreseen in C&L's internal policy on Legal for Life certification.[3347] Indeed, this was the purpose of obtaining Legal for Life Status.

[3105] The mistakes made in the audits of Castor's financial statements were repeated when the auditors mechanically produced the Legal for Life Certificates. This resulted in C&L negligently representing that Castor had passed the required tests and was worthy of Legal for Life Status, when it should not have been.

[3345] Lowenstein, March 21, 2005, p. 159, lines 19 to 21
[3346] Article 2809 CCQ
[3347] PW-1420-1B, TPS-A-405

Reliance issue

Positions in a nutshell

Plaintiff

[3106] Plaintiff explains the initial deposit of Widdrington ($200,000) was a short-term deposit to retain high liquidity. Although, submit Plaintiff, it is correct to say that Widdrington relied in part on his confidence in Stolzenberg in making this initial deposit, nevertheless Widdrington did do other due diligence. The nature of this deposit of $200,000 was entirely different from the following investments.

[3107] Plaintiff submit that Widdrington's investments were long-term major investments, that Widdrington proceeded to a far more extensive due diligence and that respected and well known experts who did review it concluded that it was a due diligence more than appropriate in the circumstances.

[3108] Plaintiff says unqualified audit reports and audited financial statements, share valuation letters, and Legal for Life Certificates were determinative of Widdrington's decisions to make his investments in Castor. Plaintiff highlights every business presents risks but very few have a track record similar to Castor's based on more than 10 years of clean audit reports, audited financial statements and valuation letters showing what expert witnesses have described as outstanding"[3348], "highly impressive",[3349] "spectacular"[3350], and even "magnifique" results.[3351]

[3109] Reasonably, exit ability was not perceived by Widdrington as a deterrent to make his investments; in their valuation letters, C&L had assessed the market ability and expressed the opinion there were sufficient shareholders to create a market should exiting become necessary.

[3110] Finally, Plaintiff concludes that Widdrington did what he had to do as a director of Castor from the day he became a director, in March 1990, until the end.

Defendants

[3111] Defendants submit the determinative reason why Widdrington made his investments in Castor was not his reliance upon C&L's representations. Other factors,

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[3348] Lowenstein, March 21, 2005, page 137, line 25

[3349] Morrison, October 10, 2006, pp. 218-220, (at p. 220 lines 22 to 25); Morrison, October 11, 2006, pp. 9-21, at pp. 14-16

[3350] PW-2405, pp. 6-7

[3351] Lajoie, November 19, 2009, pp. 128-131 (at p. 131, line 5)

the most important of which were Stolzenberg's strong personal influence on Widdrington and the latter's eagerness to develop a close relationship with Stolzenberg and become a director of Castor, played the leading role in his investment decisions, to the point of relegating C&L's representations to a simple after the fact pretext.

[3112] Defendants submit that Widdrington was a very sophisticated investor, from whom a high standard of prudence and care would have been expected. Acting against the better advice of his team of advisors, Defendants argue Widdrington behaved recklessly and did not complete a reasonable due diligence prior to making his investments in Castor.

[3113] Defendants plead that it is not reasonable for Widdrington to allege having relied on C&L's representations in those circumstances. According to Defendants, numerous contradictions in Widdrington's testimony, and the rather strange explanations he offered on certain key elements, should totally discredit his testimony as to this alleged reliance.

[3114] Defendants add that when Widdrington became a director of Castor he had duties to discharge which, had he discharged them, would have allowed him to be provided with information his advisors had repeatedly asked for in their due diligence process but never received.

[3115] Finally, Defendants conclude that Widdrington has only himself to blame for his loss.

Additional evidence

[3116] Before reviewing the additional evidence relating to the reliance issue, the Court finds it useful, through a further "who's who section", to introduce lay witnesses and expert witnesses who testified mainly on this issue: Widdrington, Heinz Prikopa ("**Prikopa**"), George Taylor ("**Taylor**"), Fred Fitzsimmons ("**Fitzsimmons**"), Paul J. Lowenstein ("**Lowenstein**"), Stephen A. Jarislowsky ("**Jarislowsky**), Donald C. Morrison ("**Morrison**") and Alain Lajoie ("**Lajoie**").

[3117] The Court will also introduce Bill Wood ("**Wood**") who did not testify before this Court but was consulted by Widdrington before he made his investments in Castor.

Who's who

Widdrington

[3118] In 1953, Widdrington obtained his Undergraduate Degree in Economics with honours from Queen's University. In 1955, Widdrington obtained a Master's degree in Business Administration from the Harvard Business School[3352].

[3119] Widdrington started as a salesman at Labatt in 1955[3353] and occupied various positions throughout the years: regional manager, general manager and senior vice-president[3354].

[3120] In 1972, Widdrington was named Vice-President, Corporate Development of John Labatt Limited ("**Labatt**"). In 1973, he was named President and Chief executive officer, positions he held until 1989. He was also Chairman of Labatt's board from 1987 to 1991. During his 16-year tenure, Widdrington was responsible for leading Labatt's very aggressive and highly successful expansion through the acquisition of numerous other companies.

[3121] Given the numerous acquisitions made by Labatt throughout his tenure, Widdrington had a good understanding of financial statements as well as a strong ability to evaluate a wide variety of business situations and investment opportunities. He was also familiar with prudent investment due diligence procedures[3355].

[3122] As shown in annual reports of Labatt, from 1980 to 1989[3356]:

- Widdrington personally signed Labatt's financial statements in his capacity of director of the company; and
- From 1981 to 1987, Widdrington was a member of Labatt's audit committee[3357].

[3123] Widdrington's experience on Labatt's audit committee provided him with first-hand experience working with auditors in connection with the audit of financial statements.

[3124] Widdrington's exposure to business and finance was not limited to his key roles at Labatt[3358].

[3352] PW-12-1
[3353] Widdrington, November 29, 2004. p.72
[3354] PW-12-1; Widdrington, November 29, 2004
[3355] Widdrington, December 13, 2004
[3356] D-590-80 to D-590-89
[3357] D-590-85, at page 31
[3358] PW-12 and Widdrington, November 29, 2004

[3125] Widdrington was a member of the board of no less than 20 companies during his career, which included the Canadian Imperial Bank of Commerce (1986-2001), Canada Trust Co Mortgage Company (1977-1986), Olympic Trust of Canada (1983-1999), Huron & Erie Mortgage Corporation, Toronto Blue Jays Baseball Club (1991-1996), Brascan (1979-1994) and the SNC-Lavalin Group Inc. (1991-1999).

Prikopa

[3126] From 1962 to 1966, Prikopa was employed as a general accounting clerk at John Leckie Industries, a company in marine supplies[3359].

[3127] From 1966 to 1971, Prikopa completed studies to become a certified management accountant[3360].

[3128] From 1966 to 1968, Prikopa was employed at McCurdy Radio Industries in Toronto as a Cost Accountant[3361].

[3129] From 1968 to 1970, Prikopa was Assistant Controller for Remington Rand, a division of Sperry Rand at the time, in Toronto[3362].

[3130] In 1970, Prikopa joined Labatt where he was employed for a total period of approximately 21 years[3363].

- He started in 1970 with the Laura Secord Division, which was a division of Labatt, in the capacity of Budget Manager. He then became National Planning Manager and Division Controller, a position he occupied until 1978.

- In 1978, he moved on to the Labatt corporate office in London, Ontario, first in the position of Assistant Corporate Controller, from 1978 to 1979, then as Corporate Controller until the end of 1982.

- From 1982 until the fall of 1991, when he left Labatt, he occupied different financial positions as Manager, Pensions Fund Investments and Investor Relations.

[3131] From 1971 to 1976, on a part time basis, Prikopa completed a B.A. in economics and sociology at York University[3364].

[3359] Prikopa, December 4, 1997, pp.9-12; PW-2389
[3360] Prikopa, December 4, 1997, pp.9-12; January 12, 2005, pp. 13-15; PW-2389
[3361] Prikopa, December 4, 1997, pp.9-12; PW-2389
[3362] Prikopa, December 4, 1997, pp.9-12; PW-2389
[3363] Prikopa, December 4, 1997, pp. 9-10; January 12, 2005, pp. 19 and following and PW-2389
[3364] Prikopa, December 4, 1997, pp.9-12; January 12, 2005, p.10-11; PW-2389

[3132] In 1981, Prikopa took the executive management course at the University of Western Ontario, an intensive course that lasted six whole weeks[3365].

[3133] In 1985, Prikopa started studying to become a Chartered Financial Analyst, but he stopped after the first year of studies and did not complete the second and third[3366].

[3134] During his career, Prikopa was a member of various professional associations and he sat on numerous committees[3367].

[3135] In 1984 or 1985, Labatt's Chairman, Peter Hardy, suggested that Widdrington deal with Prikopa for his personal financial matters[3368].

[3136] Prikopa provided Widdrington with written reports on material Widdrington would receive that involved tax matters, investments and boards of directors' books[3369].

[3137] According to Widdrington, Prikopa was invaluable for keeping track of his personal affairs and he trusted him. While Prikopa worked for Labatt, Widdrington did not pay him for services. When Prikopa left Labatt in 1991, Widdrington paid him $1,000.00/month and charged the invoices back to Labatt. When Widdrington testified at trial before Justice Carrière, in 2004, Prikopa was still handling his personal affairs for remuneration[3370].

[3138] In 1997, when he testified on discovery, Prikopa was currently employed as Director, Pensions and Risk Management, by Gulf Canada Resources in Calgary, where he worked until 2002[3371].

Taylor

[3139] Taylor left school very early, before completing high school, and went to work for a trustee in bankruptcy, a small firm in Chatham, Ontario[3372].

[3140] Through correspondence, Taylor completed high school. He had planned to study to become a Chartered Accountant but he did not follow his plan. By the time he finished high school, he had a family and had to find a job that provided more remuneration[3373].

[3365] Prikopa, December 4, 1997, pp.9-12; January 1, 2005, p. 14; PW-2389
[3366] Prikopa, December 4, 1997, pp.9-12 ; January 12, 2005, p. 16; PW-2389
[3367] Prikopa, January 12, 2005, pp. 16 and following
[3368] Prikopa, December 4, 1997,pp.9-12
[3369] Prikopa, December 4, 1997, pp.9-12
[3370] Widdrington, November 29, 2004
[3371] Prikopa, December 4, 1997; Prikopa, January 12, 2005, pp. 18-19
[3372] Taylor, January 20, 2005, pp. 9-13
[3373] Taylor, January 20, 2005, pp. 9-13

[3141] In 1960, Taylor started working at Labatt in a junior accounting capacity, and studied at night for his RIA designation (Registered Industrial Accountant), that he obtained in 1965, which subsequently became a CMA designation (Certified Management Accountant)[3374].

[3142] Taylor took a number of university courses in Vancouver, at the University of British Columbia, and also at the University of Western Ontario. A few years later, Taylor completed the Management Development program at the University of Western Ontario and subsequently, he took the Management Development program at Harvard Business School[3375].

[3143] While he does not have a formal degree, Taylor spent a considerable amount of time studying the subjects associated with his profession[3376].

[3144] Taylor was promoted several times over the years, becoming Vice-President Finance of the Labatt's parent company in 1977, then Executive Vice-President, in 1984, and finally Labatt's Chief Executive Officer[3377].

[3145] Taylor has been on a number of commercial boards and non-profit organization boards. In each case, without exception, Taylor sat on the audit committees and most frequently chaired the audit committees, although not exclusively[3378].

[3146] During the 80s, Taylor was already tremendously experienced in analyzing financial statements: the preparation of financial statements that he would be responsible for, and the financial statements that he would review in due diligence activities or in the perspective of becoming more knowledgeable about a competitor. [3379]

[3147] During the 80s, Taylor was the principal individual who interacted with the auditors of Labatt. Taylor dealt with the planning of the audit, the administration of the audit from the corporation's perspective, and he had discussions with the auditors on an innumerable number of tax matters and accounting matters, disclosure issues and other matters[3380].

[3148] According to Widdrington, Taylor was honest, resourceful, smart and trustworthy[3381]. Widdrington and Taylor's relationship was not a friendship as such but rather a very close relationship between business associates[3382].

[3374] Taylor, January 20, 2005, pp. 9-13
[3375] Taylor, January 20, 2005, pp.9-13
[3376] Taylor, January 20, 2005, pp.9-13
[3377] Taylor, January 20, 2005, pp.13 and following
[3378] Taylor, January 20, 2005, p. 21
[3379] Taylor, January 20, 2005, p. 27
[3380] Taylor, January 20, 2005, p. 27
[3381] Widdrington, November 29, 2004
[3382] Taylor, January 20, 2005, p. 35

Fitzsimmons

[3149] Fitzsimmons was an employee of Price Waterhouse Coopers. One of his duties, in that capacity, was to do forensic accounting or investigation of issues identified by Heenan Blaikie in relation to the present litigation. From 1992 to 1998, Fitzsimmons devoted most of his time to that mandate[3383].

[3150] Acting on behalf of C&L, Fitzsimmons met with many of the persons who testified in this case and with many others whose names have been mentioned even though they did not testify.

[3151] Taylor is one of those persons with whom Fitzsimmons met in 1998.

Lowenstein

[3152] Lowenstein holds the following degrees and designation: Bachelor of Arts from McGill University, Master's degree in Business Administration from the University of Michigan, and Chartered Accountant designation from the Institute of Chartered Accountants of Quebec.[3384]

[3153] From 1965 to 1969, Lowenstein worked for Edper Investments Ltd. ("**Edper**"), the trust set up for the family of Edward and Peter Bronfman, the children of Allan Bronfman, the brother of Sam Bronfman[3385].

[3154] Edper was known as one of the sources of capital for both public and private companies. At the time, it was a firm that had approximately $100,000,000 in assets, which was significant in the early 60s. Edper would be constantly approached with investments opportunities, both for public and private companies[3386].

[3155] From 1969 to 1980, Lowenstein was President of Kauser, Lowenstein & Meade Ltd. Lowenstein was co-founder of that firm with Messrs.' Ronald Meade and Stephen Kauser and they were later joined by a fourth partner named Eric Baker. They acted as an advisor to private family groups and institutional investors on investments that they had made. They were a bridge between the entrepreneurial community and the investment community. They worked for some sophisticated family groups such as the Steinberg family and the Cummings family; they worked for several high net worth investor groups[3387].

[3383] Fitzsimmons, January 23, 2006, pp. 22-23
[3384] PW-2403
[3385] Lowenstein, March 21, 2005, p. 11
[3386] Lowenstein, March 21, 2005, p. 15
[3387] Lowenstein, March 21, 2005, pp. 15 and following

[3156] Analyzing the investment opportunities made available by private companies, as opposed to public companies, represents the bulk of Lowenstein's career[3388].

[3157] Lowenstein never met Widdrington.

Jarislowsky

[3158] Jarislowsky graduated in engineering from the University of Cornell in Ithaca, New York, in 1944.

[3159] From there, he entered the American army and studied Japanese with the army for nine months. He came back and took a Master's degree in Far Eastern culture at the University of Chicago.

[3160] He went on to Harvard Business School and, in 1949, he got his Master's degree with distinction.

[3161] In the 50s, he started teaching investment analysis at McGill University and was still teaching investment analysis, in various universities, when he testified in 2005.

[3162] In 1955, he formed Jarislowsky, Fraser & Company. In 2005, he still was the CEO and Chairman of the company which was about to celebrate its 50th anniversary.

[3163] Jarislowsky, Fraser & Company are investment counsel for private and institutional accounts and they have grown from a firm managing a hundred dollar investment (in 1955) to a firm managing 50 billion dollars of investment funds (in 2005)[3389]. Jarislowsky, Fraser & Company attracts clientele from Canada and abroad, mainly represented by pension funds, endowment funds and private individuals[3390].

[3164] Jarislowsky was the chief security analyst of Jarislowsky, Fraser & Company for about 40 years. He visited about a hundred companies or more a year, especially in Canada, and knew the executives of many of them.

[3165] Over the years, Jarislowsky investigated financial statements of large public companies and also of private companies which he got involved in. Jarislowsky was a board member of approximately ten private companies (as a director). As such, he had to analyze financial statements and to make sure that the executives operated within the guidelines of the Board[3391].

[3388] Lowenstein, March 21, 2005, p. 23 (line 17)
[3389] Jarislowsky, April 4, 2005, p.15
[3390] Jarislowsky, April 4, 2005, p.15
[3391] Jarislowsky, April 4, 2005, p.17

[3166] Over the years, Jarislowsky was on the audit committee of various organisations, namely SNC-Lavalin, Goodfellow Inc., Swiss Bank Corporation and Daily Telegraph of London[3392].

[3167] Jarislowsky has seven honorary degrees, doctorates, from Canadian universities[3393]. He has received many honours and distinctions.

[3168] In 2005, 50-60% of Jarislowsky's personal net worth was still associated with Jarislowsky, Fraser & Company[3394].

[3169] For a period of time, both Jarislowsky and Widdrington were directors of SNC-Lavalin.

Morrison

[3170] From 1959 to 1964, Morrison trained as a Chartered Accountant with Deloitte Haskins & Sells in Toronto.

[3171] Morrison became a Chartered Accountant in 1962[3395] and obtained his diploma in finance and accounting the same year, from Western Business School.

[3172] From 1964 to 1972, Morrison worked for the Royal Bank of Canada, in Montreal and Toronto, where he occupied various positions dealing with credit and financial analysis, acquisitions and due diligence.

[3173] In 1972, Morrison joined the Canada Development Corporation ("**CDC**"), where he was initially Chief Financial Officer, then Executive Vice-President and finally number two operating officer for four years[3396]. Financial analysis and due diligence for investment purposes were essentially at the core of everything he did during those years.

[3174] From 1976 to 1979, Morrison worked at Burns Fry, an upper medium size investment firm, where he was a major shareholder and a senior officer. His primary function was to be a Director of Corporate Services and his responsibilities included again financial analysis and due diligence for investment purposes, and most particularly in private companies[3397].

[3392] Jarislowsky, April 4, 2005, pp.18-19
[3393] Laval University, University of Montreal, Queens University, Windsor, McMaster, University of Alberta, and Concordia.
[3394] Jarislowsky, April 4, 2005, p.19
[3395] Morrison, October 3, 2006, p. 15
[3396] Morrison, October 3, 2006, p. 36
[3397] Morrison, October 3, 2006, pp. 44-47

[3175] From early 1979 to early 1980, Morrison was Senior Vice- President and head of the Bank of Nova Scotia's Corporate Banking Division, but moving there had been a mistake. He gracefully resigned and they parted company on a mutually acceptable basis.

[3176] He took a sabbatical year. Things developed meanwhile and thereafter, he decided to continue on his own. Morrison accepted a Visiting Professorship for a year at the York University Graduate Business School. He worked on development of an Executive M.B.A. program there and taught a final term M.B.A. course in business strategy and policy. He was asked to sit on boards of private companies and was approached increasingly to do general consulting work. Morrison participated, on his behalf or on behalf of other investors, in a number of private investments[3398].

[3177] Morrison started in 1983 to spend more time doing litigation support. Before he filed a report in the Widdrington case, Morrison had never filed an expert report on due diligence required of a private investor[3399].

[3178] Morrison has generally been regarded as an expert in banking and the majority of projects he has worked on dealt primarily with banking[3400].

[3179] Morrison knew Widdrington : "*I knew him personally. I did business with him on one occasion, or we had business discussions. (...) In the late 1980s he was one of Canada's premier CEOs and I had the highest regard for him*"[3401].

Lajoie

[3180] Lajoie became a Chartered Accountant in 1978[3402].

[3181] Lajoie holds a M.B.A. degree from the University of Western Ontario that he received in 1983[3403].

[3182] Lajoie joined the firm Arthur Andersen, which he left in 1986[3404].

[3183] Except for Leclerc Juricomptables, his professional society, Lajoie has no investment in private corporations. All of his personal investments are in public corporations and were made through a specialized broker who is handling them on his behalf[3405].

[3398] Morrison, October 3, 2006, pp.51-54
[3399] Morrison, October 3, 2006, pp. 89-92, 105
[3400] Morrison, October 3, 2006, p.105
[3401] Morrison, October 3, 2006, p. 94
[3402] Lajoie, October 16, 2006, p. 16
[3403] Lajoie, October 16, 2006, p. 20
[3404] Lajoie, October 16, 2006, pp. 22 and following
[3405] Lajoie, October 16, 2006, p. 54

Wood

[3184] At all relevant times, Bill Wood, a chartered accountant, was the Ernst & Young engagement partner on the Labatt audit. Widdrington relied on him for his personal tax and financial planning, not only for himself but also for his wife and daughter. Wood also provided advice on personal investment matters. Widdrington did not personally pay Wood for his services: Wood's fees were assumed by Labatt. From 1995 to 2004, after Widdrington left Labatt, Labatt continued to pay Wood for the services rendered to Widdrington.[3406]

Widdrington and Stolzenberg's First Encounter –

[3185] Widdrington met Stolzenberg for the first time at the Davos Symposium in January 1986. At the same symposium, Widdrington also met James Binch ("**Binch**") of Trinity.

[3186] When Widdrington first met Binch, they hit it off right away because they had a lot in common and they became friends[3407]. This led Widdrington to become a director of Trinity in 1987, where Stolzenberg was also involved as a director.

[3187] Widdrington felt Stolzenberg was "very smart" and "a great salesman" with a strong ability to "work the room"[3408].

1986

[3188] Following his first encounter with Stolzenberg in January 1986, Widdrington met with him for lunch or dinner, namely on July 22, 1986[3409].

[3189] Widdrington arranged for Taylor to meet Stolzenberg to discuss the possibility of Labatt's Pension Funds investing in Castor[3410]. This meeting took place in August 1986 over lunch at Labatt's offices. Stolzenberg made a presentation on Castor, discussed business strategy and performance and provided Taylor with Castor's financial statements. At the conclusion of the meeting, Taylor turned the package over to Prikopa for his review.

[3190] Taylor had a favourable opinion of Stolzenberg but, nevertheless, Labatt's Pension Funds did not invest in Castor since it would have requested a very fundamental change in policy. Labatt's policy required that the pension funds be

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[3406] Widdrington, November 29, 2004
[3407] Widdrington, December 14, 2004
[3408] Widdrington, December 14, 2004
[3409] Widdrington, December 14, 2004 and D-593
[3410] Widdrington, December 14, 2004, pp. 109 and following

managed through third-party managers, and that no decisions on individual investments be made internally[3411].

1987

[3191] When he attended monthly meetings at CIBC, Widdrington would enquire about Castor with someone in the financial area. The news and comments were always fairly positive or positive.

[3192] On January 21, 1987, Martin Dufresne, Senior Vice-President, Corporate Banking at CIBC, called Widdrington and further sent him a fax, in which he confirmed that Castor was a very legitimate company, with a very legitimate business approach.[3412]

[3193] In December 1987, Simon met with Ms. Diana Brett, Account Manager with the CIBC in Montreal and sent her financial information for purposes of obtaining a credit facility for Castor[3413]. Subsequent to December 1987, the CIBC submitted a proposed term sheet outlining the main conditions of a line of credit that it was prepared to extend to Castor. After reviewing the term sheet, and discussing it with Stolzenberg, Castor felt that the CIBC was imposing certain conditions they would not agree to comply with, therefore Castor did not accept CIBC's offer[3414].

[3194] The main conditions found unacceptable by Castor were essentially that the CIBC wanted a fully secured line of credit and wanted to see information on the mortgage portfolio which went beyond what Castor was prepared to provide[3415].

[3195] Widdrington did not know Diana Brett or her colleague Brian Perron[3416] and he was never made aware of any meetings or dealings between the CIBC and Simon.

[3196] In a letter dated August 25, 1987[3417], Widdrington invited Stolzenberg to attend Labatt's annual meeting of September 11 and 12, 1987. Taylor confirmed that this was an internal Labatt function with very few outsiders, if any, invited as special guests[3418]. In fact, Stolzenberg was the only outsider invited at this Labatt function[3419].

[3411] Taylor, January 20, 2005, pp. 27-30
[3412] PW-2377
[3413] Simon, April 28, 2009, pp.130-134; D-620-1 and D-620-2
[3414] Simon, April 28, 2009, pp.133-134
[3415] Simon, April 28, 2009, pp. 152-153
[3416] D-620-1
[3417] D-618
[3418] Taylor, January 20, 2005, pp. 120-122
[3419] Widdrington, December 15, 2004

1988

[3197] During 1988, Widdrington would have had meetings and other contacts with Stolzenberg:

- According to Stolzenberg's agenda, Stolzenberg and Widdrington had a lunch meeting on January 6, 1988 at the Toronto Yacht Club[3420] but Widdrington did not recall this meeting[3421];
- According to a letter, Widdrington was invited to Castor's board of directors' dinner on March 21, 1988[3422], but Widdrington did not recall whether or not he attended this particular meeting. Widdrington however stated that he did attend one board dinner prior to becoming a director of Castor[3423];
- Widdrington had lunches or dinners, three or four times with Stolzenberg; Widdrington considered Stolzenberg was an interesting individual with a good sense of humour[3424];
- On June 27, 1988, Widdrington invited Stolzenberg to attend the opening night of the Stratford Festival, in Ontario, for purposes of introducing him to Mr. Merv Lahn of Canada Trust[3425];
- On August 15, 1988, Widdrington invited Stolzenberg to attend Labatt's' Annual Meeting on September 7-8, 1988[3426].

The 1988 deposit of $200,000

[3198] On their way to Connecticut to a Trinity board meeting aboard Stolzenberg's private jet, Widdrington asked Stolzenberg if he could find a short-term investment vehicle for him.

[3199] Widdrington had received positive feedback on Castor from CIBC's officials[3427] confirmed in writing by Dufresne, a Vice-president of the CIBC[3428]. Moreover, Taylor was impressed with Castor's solid track record and was of the opinion that a three-month deposit would not involve any sort of risk for Widdrington.

[3420] D-621
[3421] Widdrington, December 15, 2004
[3422] D-622
[3423] Widdrington, December 15, 2004
[3424] Widdrington, December 15, 2004
[3425] Widdrington, December 15, 2004; D-625-1 and D-625-2
[3426] D-626; Widdrington, December 15, 2004, pp. 315-317
[3427] Widdrington, November 29, 2004
[3428] PW-2377

[3200] On October 11, 1988, Widdrington sent Stolzenberg a cheque in the amount of $200,000 payable to Castor[3429] in connection with a term deposit in the same amount for a three-month period extending from October 12, 1988 to January 12, 1989.[3430]

[3201] Widdrington's deposit in Castor was evidenced by a very short letter, PW-34, that Widdrington addressed to Stolzenberg on October 11, 1988, which reads in part as follows[3431]:

> Dear Wolfgang:
>
> As per our discussion of last week, enclosed please find my cheque in the amount of $200,000.
>
> Once you have had an opportunity to do so, for my own record keeping purposes, I would appreciate it if you would let me know how the money is being invested."

[3202] Widdrington did not have precise knowledge as to how his money was going to be invested[3432] and he had not seen financial statements or other specific financial information regarding Castor prior to making this $200,000 deposit[3433].

[3203] As it turned out, this first deposit consisted of a promissory note issued by Castor which was thereafter renewed from time to time and eventually rolled into Widdrington's equity investment in Castor in December 1989.

1989

[3204] Widdrington continued to have informal meetings and other contacts with Stolzenberg.

The 1989 investment

[3205] On December 13, 1989, Widdrington met with Stolzenberg at The York Club in Toronto where the latter approached him to become a director of Castor and to invest approximately $1,000,000 in the company[3434]. At this lunch meeting, Widdrington was provided with the following documents by Stolzenberg:

[3429] PW-34
[3430] PW-35
[3431] PW-34
[3432] Widdrington, December 15, 2004
[3433] Widdrington, December 15, 2004
[3434] Widdrington, November 29, 2004

- a letter dated December 12, 1989 inviting him to invest in units consisting of a mixture of shares and debentures of Castor[3435] with the following attached documents: interim financial statements as at September 30, 1989; a five year forecast; a valuation letter from C&L dated October 17, 1989 regarding the fair market value of Castor's common shares; a schedule of Shareholders' Positions as at December 1st ; a schedule of 1989 Capital Increase; a letter showing subscription details and a subscription form.

- Castor's Audited Consolidated financial statements for the year ended December 31, 1988[3436];

- Castor's consolidated financial statements for the five years ended December 31, 1988[3437];

- The list of senior management and board members of Castor[3438].

[3206] The package did neither include a Legal for Life Opinion nor a Legal for Life Certificate issued by C&L.

[3207] Stolzenberg told Widdrington Castor needed some Canadian directors to sit on its board and he specified that the requirement to become a director was to make, at least, a million dollar investment in the company.[3439]

[3208] Following his December 13, 1989 lunch with Stolzenberg, Widdrington did a cursory review of the package of documents received and thereafter handed the package to Prikopa[3440].

[3209] On December 14, 1989, Prikopa reviewed the documentation[3441] a copy of which was also given to Wood.

[3210] On December 14, 1989, in the afternoon, Widdrington met with Prikopa to obtain his preliminary reaction[3442].

[3211] Prikopa viewed that his role which was to look at the materials from a financial point of view, would provide a second independent view on the merits of a $1,000,000 investment[3443].

[3435] PW-10
[3436] PW-10-1
[3437] PW-10-2
[3438] PW-10-3
[3439] Widdrington, November 29, 2004
[3440] Widdrington, December 16, 2004
[3441] Prikopa, January 12, 2005, p. 45-46
[3442] Widdrington, November 30, 2004, p. 12
[3443] Prikopa, January 12, 2005, p. 92

[3212] Prikopa learned that the annual director fees would be $30 000, which appeared to be a normal size fee[3444].

[3213] From his analysis of the available material, Prikopa identified that:

- The invitation to Widdrington to become a director and shareholder was not an off invitation to make an investment but rather a part of a $25,000,000 capital offering by Castor to existing stake holders and any new investors[3445];

- C&L had issued a valuation letter of Castor's common shares dated October 17, 1989[3446]; the valuation letter provided a good degree of comfort to Prikopa. In order to have an understanding of where the company was and in order to be able to express an opinion on the valuation of the common shares, he was looking at updated results, right up to the date of the proposed investment, through a valuation report from the company's auditors[3447], with the audit work done by C&L, as well as the review by C&L of the interim results of Castor. Prikopa could not wish for better and more reliable information[3448]. Moreover, the content of the valuation letter, over and above the value itself, was extremely positive and comforting (a strong endorsement by the auditors)[3449].

- the key highlights of the audited financial statements for the last completed year were : a clean unqualified audit opinion from C&L, one of the big five accounting firms for which he had a lot of respect[3450]; a very sizeable growth in the asset base[3451]; an ability to raise substantial funds on the liability side[3452]; a very strong growth on the net earnings side[3453]; short-term commitments by Castor and a reasonably good maturity matching between assets and liability[3454] ;

- the five-year consolidated audited financial statements ending December 31, 1988 showed: a very, very strong growth record over this five-year period on a solid consistent basis one year after the next[3455]; a significant growth of bank lendings to Castor which showed the ability of Castor to manage these

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[3444] Prikopa, January 12, 2005, p. 94-96
[3445] Prikopa, January 12, 2005, p. 98
[3446] Prikopa, January 12, 2005, p.102
[3447] Prikopa, January 12, 2005, p. 102, pp.148 and following
[3448] Prikopa, January 12, 2005, pp. 151 and following
[3449] Prikopa, January 12, 2005, pp. 151 and following
[3450] Prikopa, January 12, 2005, p. 106
[3451] Prikopa, January 12, 2005, p. 108-112
[3452] Prikopa, January 12, 2005, p. 112
[3453] Prikopa, January 12, 2005, p. 112
[3454] Prikopa, January 12, 2005, pp. 114-125
[3455] Prikopa, January 12, 2005, pp.128-130

monies and provide a fair rate of return to its lenders[3456]; a very solid balance sheet situation with a fairly good shareholders' equity position[3457]; leverage consistent with normal leverage of the industry, not over-extended but at the same time good enough to provide good returns[3458]; a very positive earnings growth in a time frame where there was volatility in the markets and interests rates which showed that management group was able to manage this business and were doing a very successful job [3459].

- The unaudited financial statements for a 9 month period ending September 30, 1989 showed same progress still apparent in the current year[3460].

- The Castor history document provided information from Castor's inception and up to September 30, 1989 – a very positive performance history since every year showed positive growth of quite a substantial size notwithstanding the challenging situation of the early 80s [3461].

- The list of management and directors showed a solid and diversified group with good credentials[3462].

[3214] Prikopa's impressions were "*very, very strong positive impressions*"[3463].

[3215] Prikopa prepared a hand-written memo for Widdrington and gave a copy to Wood[3464]. Widdrington suggested to Wood and Prikopa that they call Stolzenberg the next day in order to get answers to any questions they might have[3465].

[3216] On December 15, 1989, in the afternoon, Stolzenberg, Wood and Prikopa participated in a telephone conference call. During this call, they discussed various issues, including Castor's portfolio diversification and shareholders' exit options. Stolzenberg undertook to provide a copy of the shareholders' agreement to Prikopa. The call lasted approximately 15 to 20 minutes[3466].

[3217] Following this call, Prikopa finalized his memo to Widdrington[3467].

[3218] In his memo, Prikopa dealt with risk factors and possible concerns as follows:

[3456] Prikopa, January 12, 2005, p. 129-131
[3457] Prikopa, January 12, 2005, p. 131
[3458] Prikopa, January 12, 2005, p. 133
[3459] Prikopa, January 12, 2005, p. 134
[3460] Prikopa, January 12, 2005, p. 136 and following
[3461] Prikopa, January 12, 2005, p. 144 and following
[3462] Prikopa, January 12, 2005, p.180
[3463] Prikopa, January 12, 2005, p.184
[3464] Prikopa, January 12, 2005, p. 184
[3465] Widdrington, November 30, 2004, p. 14
[3466] Prikopa, January 12, 2005, pp. 188-192
[3467] PW-43-1

"1. A $ million investment is of substantial size relative to your portfolio and will be totally locked in – no provision for exit – money will be totally at risk of business – pay back only from long run earnings.

2. Business is doing very well but greatly sensitive to financial market conditions – i.e. interest rates, exchange, etc., and particularly ability to continue to make strong spreads of 3% between loans placed and cost of borrowed money. Major risk is always spreads and quality of loans made, i.e. risk of loan loss.

3. What is the quality of present loan assets? How good are they – are there any shaky loans in portfolio?

4. Much of money invested in mortgages, etc., matures in 1990 and 1991 (close to 85%) – will company be able to redeploy these monies (about $1.1 billion) back into market with the same good 2% spreads?

5. How well do you know the management and how the company conducts its business – the material or Financial Statements don't tell about that: -

- Where is most of money employed – America, I guess? –
- Where is most of borrowed money sourced from – From Europe maybe?
- What is the average quality of loans made – I assume they operate in the higher rate higher risk loan market – the 13% average rate earned and 3% spread suggests higher loan risk. –
- How does company deal with exchange factor in business? Is it hedged at a risk or used as a bet to take money on it? –
- What are company's long run plans on leverage?
- Will it be maintained at present level? –
- How well does management and board work together –
- Is it a close knit group network?
- Is much of the business generated through this network? –
- What is the level of integrity brought to business deals?

6. Do you trust management and have total confidence that this group will run a successful business for years to come? At present cash return, you will need to count on at least 5 to 10 years of business success to get your money back."

[3219] Monday morning, December 18, 1989, Prikopa and Taylor met early to discuss the possibility of Widdrington investing in three or four units of Castor.

[3220] Prikopa prepared a handwritten analysis[3468] comparing the financial implications of investing in three or four units and concluded that, on a cash flow basis, it would be more advantageous to invest in three units only.

[3221] Later the same morning, another meeting was held at which Widdrington, Prikopa and Wood were present[3469].They dealt with the outlining of Prikopa, comments

[3468] PW-43-2

on the proposed investment, and on the financial information which had been remitted by Stolzenberg to Widdrington.

[3222] Right after this meeting, Widdrington consulted Taylor[3470]. Without audited financial statements, Taylor would never have recommended that Widdrington enter into the investment.[3471]

[3223] The following factors, some more important than others, participated in Widdrington's assessing whether he should become a director and shareholder of Castor[3472].

- He had a good impression of Stolzenberg.
- He had information from the CIBC which indicated that Castor was a tightly and conservatively run company.
- Taylor had a positive impression of Stolzenberg and Castor.
- Sitting on the board of Trinity with Stolzenberg gave him a positive impression of Stolzenberg.
- His experience in making the deposit of $ 200,000 with Castor was very positive in that it showed that Castor handled it in a very professional manner.
- He had the audited financial statements which were accompanied by a clean auditors' report and reflected a 10 year successful track record. He also had the unaudited financial statements of September 30, 1989, which he thought were reviewed by C&L, and looked very good.
- He had the valuation letter prepared by C&L.
- He discussed this investment with his advisors, Prikopa, Wood and Taylor, all knowledgeable individuals on whose advice he had relied for many years and who were all opining that the investment was worthwhile.

[3224] Widdrington was essentially looking for a long-term investment opportunity,[3473] and his review of the valuation letter disclosed an increase in the fair market value of the shares, from less than $200, a few years earlier, to an estimated range of $525 to

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[3469] Prikopa January 12, 2005
[3470] Prikopa, January 12, 2005
[3471] Taylor, January 20, 2005
[3472] Widdrington, November 30, 2004
[3473] Widdrington, November 30, 2004

$550.[3474] Based on the experience of the past, there was lots of room for growth in the value of these common shares in the future, which precisely interested Widdrington.[3475]

[3225] Wood and Taylor took the position that it was a good opportunity for Widdrington to invest in Castor and to become a director of Castor. After having received such supportive opinions, Widdrington decided to go ahead.[3476]

[3226] Widdrington invested in 10.75% convertible debentures, in 8% preferred shares and in common shares of Castor, in the form of four units of $282,600 each, for a total investment of $1,130,400, including his original investment of $200,000, plus the accumulated interest thereon.[3477]

[3227] Widdrington informed Prikopa of his intention to go ahead with a four unit investment. He instructed Prikopa to call Castor's office and inform Castor of his intentions, which Prikopa did[3478].

[3228] On December 20, 1989, Prikopa received a copy of the shareholders' agreement[3479] that he remitted to Labatt's Legal Department for review[3480].

[3229] On December 22, 1989, a fax was sent to Prikopa enclosing information he had requested on the mortgage portfolio[3481].

[3230] Widdrington's instructions to transfer the money to Castor, and the actual money transfer to Castor, took place on December 28, 1989, after all requested information had been received[3482].

[3231] When Widdrington decided to invest in Castor, he was seeing his tenure as CEO of Labatt coming to an end and was looking for new challenges, as well as new sources of income. He was looking for a long-term investment opportunity.[3483] Widdrington perceived that, as a director of Castor, he would progressively learn about Castor's type of business, and as shareholder, there was a lot of room for growth in the value of his common shares in the future.[3484]

[3474] Widdrington, November 29, 2004
[3475] Widdrington, November 29, 2004
[3476] Widdrington, November 30, 2004
[3477] PW-11-1; PW-11-5; PW-11-6
[3478] Prikopa, January 12, 2005
[3479] PW-2382
[3480] Prikopa, January 12, 2005
[3481] PW-10-5
[3482] PW-11-2; Widdrington, December 16, 2004
[3483] Widdrington, November 30, 2004
[3484] Widdrington, November 29, 2004

1990-1991

[3232] In a memorandum to Widdrington dated May 20, 1990, following the release of the audited financial statements for the year ended on December 31, 1989, Prikopa again concluded that Castor was doing well[3485] and highlighted the solid return on shareholders' equity as well as the solid consistent growth in revenue and earnings of five years past.

[3233] Throughout 1991 up until Widdrington's decision to subscribe for additional shares of Castor in October 1991, the interim financial statements disclosed that Castor's results were holding up in spite of the difficult business environment.[3486]

[3234] On September 3, 1991, Prikopa prepared a memorandum dealing with the six-month interim financial statement, in which he concluded[3487]:

> «Peter, Castor's financial report for 6 months to June shows results are holding up fairly well at this year's halfway mark, considering the difficult business environment.»

[3235] Legal for Life Opinions were included in the Directors' Books received in connection with Castor's Board meetings and Widdrington understood what such letters meant.[3488] Two such Legal for Life Opinions were provided to Widdrington[3489], based on the Legal for Life Certificates issued by C&L on February 16th, 1990 and February 15th, 1991 respectively.

[3236] Although Widdrington did not rely on the Legal for Life Opinions when making his initial investment, they were a factor considered by him and his investment advisor, Prikopa,[3490] which contributed to his decision to maintain and increase his investment in 1991.

The 1991 investment

[3237] On October 25, 1991, Widdrington made a second equity investment in Castor, at which time he subscribed for one unit, composed of common shares, preferred shares and a convertible debenture, for a total subscription price of $292,560.[3491]

[3485] PW-44-1
[3486] PW-46; PW-47
[3487] PW-46
[3488] PW-12; PW-14, Widdrington, November 30, 2004; Widdrington, December 1, 2004
[3489] PW-12, Tab 12, dated March 22, 1990 and PW-14, Tab 11, dated March 22, 1991
[3490] Prikopa, January 12, 2005; Prikopa, January 13, 2005
[3491] PW-19: "1991 Capital Subscription Form" dated October 25th, 1991 signed by Widdrington, with copy of a cheque dated October 25th, 1991 to Castor in the amount of $292,560.

[3238] This second investment was preceded by a letter from Stolzenberg, dated September 25, 1991, requesting an increase of the capital base of Castor.[3492] The letter, accompanied by the interim financial statements as at June 30, 1991, outlined the circumstances that necessitated such call for capital, and referred to the banks' tightening of credit lines for real estate activities, and a desire on the part of Castor to show strength to the banks and outside investors. The letter was also accompanied by C&L's valuation letter dated March 6, 1991, establishing a current fair market value of $580 per common share. The C&L valuation letter specifically states: «*Based on this valuation, the proposed subscription price for common shares is $580.00.*»

[3239] Widdrington believed that the strategy put forward by Stolzenberg of raising new capital, seemed to make sense, and was consistent with what Castor had done in the past to raise equity.[3493]

[3240] When he received the letter[3494], Widdrington gave it to Prikopa who prepared a memorandum, wherein he concluded that this was a good investment for Widdrington.[3495] In accordance with Prikopa's advice, Widdrington decided to wait until he had attended the Castor Board meeting on October 24, 1991, and until he had had the opportunity to discuss this matter with Stolzenberg and other members of the Board, before making his decision.[3496]

[3241] C&L's valuation letter dated October 22, 1991[3497] which Widdrington received at the Board meeting of October 24, 1991, and which indicated the fair market value of Castor's common shares as at September 30, 1991, was the critical factor which impelled him to make his second equity investment.[3498]

[3242] Widdrington believed that the other shareholders and directors of Castor were going to participate in that capital subscription. He acknowledged that, as compared to the valuation letter dated March 6, 1991, the fair market value ascribed by C&L to the common shares of Castor, had decreased slightly, as a reflection of the more difficult business conditions.[3499] However, the book value of these shares had substantially increased since the March 6, 1991 valuation letter, and C&L's letter of October 22, 1991 stated that because of the slowdown in the real estate market in North America,

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[3492] PW-17
[3493] Widdrington, December 2, 2004; For the reference to the company raising more capital in the past see also PW-16-3 Tab 6; PW-51, p. 4
[3494] PW-17
[3495] PW-47; Widdrington, December 1, 2004
[3496] Widdrington, December 1, 2004
[3497] PW-18, Tab 6
[3498] Widdrington, December 2, 2004
[3499] Widdrington, December 2, 2004

additional opportunities would be available to Castor,[3500] an assertion that made a strong impression on Widdrington.[3501]

[3243] Widdrington's decision to buy an additional unit in October 1991 was taken in a context where the overall impression about Castor's performance was very positive. The value of the units for this new capital call was listed at $292,560 per unit, as compared with the price of $282,600 per unit which he had paid for his first equity investment approximately a year earlier. For him, this confirmed that the value of the units had gone up approximately $10,000 in that period of time, and this in turn reflected the increase in the value of the shares that had been determined by the several valuation letters issued by C&L over that same period.[3502]

[3244] Audited financial statements and valuation letters were similarly key to Widdrington's decision to make his second equity investment in October 1991.[3503]

[3245] Prikopa supported Widdrington's decision to proceed with said investment,[3504] something he would not have done if the valuation letter or the financial statements had raised any concern.

[3246] Prikopa testified that the size of Widdrington's investment in Castor, in the context of what he wanted to achieve with his portfolio, was within prudent limits.[3505]

Board of directors

[3247] When he was first approached by Stolzenberg to become a director of Castor, during their December 13, 1989 meeting, Widdrington told Stolzenberg that he did not have experience or broad in-depth knowledge of mortgages and real estate market.[3506]

[3248] Castor's Board included international and experienced directors with diverse talents.[3507] Widdrington regarded this as an opportunity for him to make a positive contribution in the future.[3508] A director acquires his knowledge as a learning process.[3509] It is a common situation that the directors who compose the board of any given company have different and complementary strengths, and it is normal for directors to lean on each other and rely on each other's respective specialty.[3510]

[3500] PW-18, Tab 6, p. 4
[3501] Widdrington, December 2, 2004
[3502] Widdrington, December 1, 2004
[3503] Prikopa, January 17, 2005
[3504] Prikopa, January 13, 2005
[3505] Prikopa, January 17, 2005
[3506] Widdrington, November 29, 2004
[3507] PW-43-1
[3508] Widdrington, November 30, 2004
[3509] Prikopa, January 17, 2005
[3510] Jarislowsky, April 5, 2005

[3249] For Widdrington, the role of a director in general, and his role as director of Castor in particular, consisted in ensuring that the company had direction, a game plan, and the right people in place to carry it forward; such a role did not require directors to know a great deal about the specifics of the business.[3511] Widdrington did not view his role as director as requiring him to examine the nuts and bolts of the business. It was up to the auditors to examine the financial details, and the auditors would bring any areas of concern to the attention of the directors.[3512]

[3250] Widdrington was an "outside director" at Castor and Prikopa did not expect him to have the kind of knowledge of the company that an inside director would have. As an "outside" director, Widdrington had to rely on representations of management and disclosure of auditors for verification of management's representations.[3513]

[3251] Castor's board did not discuss individual loans or individual loan decisions: Stolzenberg had full authority and the full confidence of Castor's directors and he basically made the final decisions on those matters.[3514].

Widdrington, Trinity, Stolzenberg and Castor

[3252] From late 1987 until early 1992, Widdrington was a director of Trinity Capital.

[3253] He was asked by Binch to become a director of Trinity to advise on the opportunity of different investment ventures for the company. Widdrington did not invest in Trinity, either as a shareholder, or otherwise, and he received a remuneration of $5,000 per year, for attending two or three directors' meetings.[3515]

[3254] Widdrington was not involved in, or inquired about the day-to-day operations or the financial matters of Trinity; he was not on the company's payroll and he had no management responsibilities.[3516]

[3255] While still a director of Trinity, Widdrington progressively distanced himself from the company when Trinity started to become involved in the landfill business because, as a director and eventually chairman of Laidlaw which was involved in that business, Widdrington did not want to be in a conflict of interest. From the very beginning, he voiced his disapproval of Trinity getting involved in the landfill business which he considered to be completely out of Trinity's league.[3517]

[3511] Widdrington, November 30, 2004
[3512] Widdrington, December 1, 2004
[3513] Prikopa, January 13, 2005; Prikopa, January 17, 2005, pp. 112-114
[3514] Dennis, September 8, 1995, pp. 38-39
[3515] Widdrington, November 29, 2004
[3516] Widdrington, November 29, 2004
[3517] Widdrington, November 29, 2004; Widdrington, November 8, 1995

[3256] Widdrington always considered Castor and Trinity as completely separate companies[3518] and it never occurred to him that they could constitute related parties in accounting terms[3519].

[3257] While Widdrington acknowledged that by the Board meeting of June 26, 1990 he was aware that Trinity was not doing very well financially,[3520] he never considered Trinity's loans to be bad loans. From the beginning of his involvement in Trinity, he consistently voiced his concern that the company was getting involved into too many businesses and in businesses that it should not have been in. However, Widdrington believed Trinity could be righted reasonably quickly if the company just stuck to the elements of the business and stopped running around trying to be everything to everyone.[3521]

[3258] Widdrington was not so much concerned with the financial aspects of Trinity as with the operational aspects of the company.[3522]

[3259] Had there been any concerns about the quality of Castor's loans to Trinity, if this had ever been an issue, Widdrington thought it would have been discussed with the auditors of Castor and, in case of a "bad loan", that there would have been a loan loss provision. To put things in perspective, Widdrington noted that, as of May 1990, Castor had assets of approximately $1.6 billion compare to Trinity's loans totalling approximately 14 million[3523].

[3260] Prior to 1992, Widdrington was not aware of the specific details of Trinity's financing[3524]. While Trinity's board was a very active Board, Binch confirmed that on the financing side of the proposed transactions "*the dialogue in the Board meetings was, in the main, not that expository, except if there was something substantive or significant*"[3525].

[3261] No officer of Trinity could borrow or lend money for the account of the corporation without the specific approval of the board of directors.[3526] Loans extended by CHIO or CH Ireland to Trinity were sometimes approved through written resolutions, some of which were signed by Widdrington.

[3518] Widdrington, December 15, 2004
[3519] Widdrington, December 13, 2004
[3520] Widdrington, December 15, 2004
[3521] Widdrington, December 15, 2004
[3522] Widdrington, December 15, 2004
[3523] Widdrington, December 15, 2004
[3524] Widdrington, December 14, 2004
[3525] Binch, October 30, 2001, pp.209-212
[3526] D-594 Article 7

[3262] The minutes of Trinity's board meeting of October 5, 1988[3527] and the briefing book for said meeting[3528], which Widdrington reviewed as a director, had sections relating to the Stanwix transaction and information relating to CHIO financing.

[3263] The minutes of Trinity's board meeting of June 29, 1989[3529] at the offices of Labatt in Toronto had a section on the Cadiz landfill transaction also funded by CHIO.

[3264] By the time Widdrington made his equity investment in Castor in December 1989, he had been a director of Trinity for slightly over a year-and-a-half and, as such, had heard names such as CHIO being mentioned at Trinity board meetings[3530].

[3265] The material relating to Trinity's Board meeting of June 26, 1990, received and reviewed by Widdrington, included information relating to Trinity's financing through Castor's subsidiaries[3531]. Then, Widdrington had been appointed to Castor's Board.

[3266] As at June 1990, Widdrington did recall a discussion concerning Trinity's financial status, but not the specifics of such discussion, and was aware of CHIO and CHI's relation to Castor[3532].

[3267] In fact, funding of Trinity was provided mainly by Castor's subsidiaries.[3533]

Taylor – Fitzsimmons

[3268] Taylor recalled meeting with an investigator for C&L by the name of Fred Fitzsimmons but not the specific topics they would have discussed[3534].

[3269] Fitzsimmons testified that in 1998 he met with Taylor and prepared a written report subsequently[3535] . In cross-examination, Fitzsimmons acknowledged that:

- He interviewed many people.[3536]
- He did not recall the length of his meeting with Taylor.[3537]

[3527] D-602
[3528] D-603
[3529] D-605
[3530] Widdrington, December 17, 2004
[3531] D-610, D-611 and D-612
[3532] Widdrington, December 15, 2004
[3533] Binch, October 30, 2001, pp. 201-202
[3534] Taylor, January 20, 2005
[3535] D-671
[3536] Fitzsimmons, January 23, 2006, p. 23
[3537] Fitzsimmons, January 23, 2006, p. 37

- In other occasions he had asked the person he had interviewed to review his "*résumé*" and correct anything that would not be accurate, but that he did not do it with Taylor.[3538]

- In various occasions, when he had asked the person to review a "*résumé*" he had written, the person had edited such "*résumé*" (actually added statements or deleted statements that appeared in it).[3539]

- In various occasions, he recorded his interviews but he had not recorded the interview with Taylor.[3540]

- He could have made mistakes while recording what he thought Taylor was telling him.[3541]

- The words included in his report were not the exact words of Taylor[3542] but rather Fitzsimmon's impressions and understandings.[3543]

Experts' evidence

Plaintiff's experts

Lowenstein

[3270] In 1998, when Lowenstein authored his report, he had been the «*chairman and owner of a financial service and merchant banking firm for twenty years*».[3544]

[3271] Lowenstein concluded that: «*I am of the opinion that Mr. Widdrington conducted sufficient due diligence by relying on the Audited Consolidated Financial Statements, unaudited interim financial statements of Castor as well as the valuation letters, discussions with his advisors and obtaining other relevant information. It was reasonable for Mr. Widdrington to have relied primarily upon Castor's Audited Consolidated Financial Statements and the share valuation letter dated October 17, 1989; March 6, 1991 and October 22, 1991.*»[3545]

[3538] Fitzsimmons, January 23, 2006, pp. 28, 33, 44-45
[3539] Fitzsimmons, January 23, 2006, p. 33
[3540] Fitzsimmons, January 23, 2006, p. 33
[3541] Fitzsimmons, January 23, 2006, pp. 40-41
[3542] Fitzsimmons, January 23, 2006, p. 41
[3543] Fitzsimmons, January 23, 2006, pp. 42-50
[3544] PW-2404, p. 1.
[3545] PW-2404, p. 5.

[3272] Lowenstein characterized Widdrington as a "*sophisticated high net worth private investor*" because of Widdrington's business and investment expertise and because of Widdrington's net worth[3546].

[3273] Lowenstein opined that a reasonable private investor at the time of Widdrington's initial investment would have assumed that C&L was in a position to have detailed knowledge of Castor's operations, financial position, and method of conducting business[3547] : C&L could not have issued unqualified auditors' reports, nor could they have produced a valuation letter, such as the one they did produce, without being in that position. Accounting firms of C&L's reputation did not issue valuation letters without understanding in depth the nature of the company they were valuing.

[3274] Lowenstein opined that a reasonable sophisticated high net worth private investor, when provided with the unqualified audited financial statements and the valuation letter by C&L, would have invested in 1989, as Widdrington did, and would have supported the company and increased his investment in 1991, as Widdrington also did.[3548]

[3275] Lowenstein acknowledged that the concerns and risks outlined in Prikopa's memo were valid and he explained that it was Prikopa's role to bring them all to Widdrington's attention[3549].

[3276] Lowenstein confirmed the shareholders' agreement was an important document to consider prior to making an investment in Castor since Castor was a private company and since the agreement would set forth the terms and conditions enabling an investor to sell his shares. He would have recommended reading the agreement and getting legal advice[3550].

[3277] Lowenstein confirmed that he had experience as a director of industrial, financial services, and venture capital companies. He was also a director of two publicly traded companies. He further stated having experience in corporate governance and added that he was a "student" of this and updated himself on this issue[3551].

[3278] Lowenstein testified that it was important for Widdrington to know more about Castor as a director than as a shareholder.

[3546] Lowenstein, March 23, 2005; PW-2404
[3547] Lowenstein, March 21, 2005; PW-2404
[3548] Lowenstein, March 21, 2005; PW-2404
[3549] Lowenstein, March 24, 2005; PW-2404
[3550] Lowenstein, March 24, 2005
[3551] Lowenstein, March 24, 2005

[3279] As a director, Lowenstein would have obtained as much information as he could over time; he would have carefully read the board materials provided prior to meetings; he would have done as he testified: "*listen attentively, you don't ask a lot of questions, you don't come in like a bull in a china shop*"[3552]; he would have expected any significant issue or major change to be brought forward by management to the board[3553].

Jarislowsky

[3280] Jarislowsky confirmed the shareholders' agreement was an important document to consider prior to making an investment in Castor since Castor was a private company and since the agreement would set forth the terms and conditions enabling an investor to sell his shares[3554]. As Lowenstein, he would have recommended reading the agreement and getting legal advice[3555].

[3281] Jarislowsky confirmed that, at the time, Stolzenberg was known as a highly respected financier and entrepreneur and that he apparently had the confidence of many international and Canadian banks and financial institutions, given the bank loans and facilities Castor got[3556].

[3282] Several times, Jarislowsky said Prikopa's memo was a very good analysis of the major risks in this kind of investment, adding that he did not think he would have done it much better himself[3557].

[3283] Jarislowsky opined that Widdrington was primarily misled as a result of his faith in the accuracy of the audited financial statements of Castor, and as a result of the share valuation letter, all of which disclosed a healthy and fast growing company with an uninterrupted string of success. He mentioned reliance in Stolzenberg as a secondary cause, but disagreed with Defendants as to its relative significance.[3558]

[3284] Answering a question put to him in cross-examination by C&L's counsel relating to reliance, Jarislowsky said:

> My feelings is that both Stolzenberg, My Lord, and the auditors knew what the real situation was, that's my basic feeling. But they did not divulge it to other people and they consistently raised new money in order to make sure that they weren't going over the cliff, and they raised money from the same people to

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[3552] Lowenstein, March 24, 2005
[3553] Lowenstein, March 24, 2005
[3554] Jarislowsky, April 4, 2005
[3555] Jarislowski, April 4, 2005
[3556] Jarislowsky, April 4, 2005
[3557] Jarislowsky, April 4, 2005
[3558] Jarislowsky, April 4, 2005

> whom they gave incomplete and unreliable information. I would even go further (...)I believe that both parties (Castor and C&L) knew what they were doing (...) I'm not sure whether everybody at Coopers & Lybrand knew what was being done but I'm sure that the main partners and the support staff knew because the most important item of any corporation of this type is the solvency of its loan portfolio and the cash revenue and the maturities on a cash basis should have given the picture to both Stolzenberg and the auditors. That's my view.[3559]

[3285] Jarislowsky did not believe that a typical individual high net worth investor would have done any more due diligence than Widdrington.

[3286] Jarislowsky concluded that, based on the work of C&L, it would have appeared that Stolzenberg «*had led Castor to spectacular results*» and that «*any individual investor, basing himself on the audited results and on the share valuation letter, would have concluded that this was a sound operation. The company had come through good and less good years with flying colours. The auditor's report was clear and unqualified*».[3560] In Jarislowsky's words: «*Why would one expect Widdrington to not trust the audited financial statements of such a prominent international firm as Coopers & Lybrand? I myself would have also accepted it at face value. I know of no shareholders who disregard an audited statement of a major accounting firm in favour of their own private investigations*».[3561]

[3287] Both Lowenstein and Jarislowsky considered that Defendants' experts imposed a burden of due diligence on Widdrington that far exceeded what could be expected of an individual investor, *albeit* one who became a director, and in fact would obviate the need for the auditors.

[3288] Jarislowsky described the Lajoie report as «*an outline of how a trained analyst would proceed to a full "due diligence" for a major merger or an acquisition when having full access to the "war room" of a corporation*» and also noted that the nature of the due diligence advocated by Mr. Lajoie, «*essentially requires expertise in several professional disciplines*».[3562]

[3289] Jarislowsky would expect a prudent director to know about the company's key officers and employees[3563].

[3559] Jarislowsky, April 4, 2005
[3560] PW-2405, p. 7
[3561] PW-2405, p. 11
[3562] PW-2405, p. 10
[3563] Jarislowsky, April 5, 2005

[3290] Jarislowsky would expect a new director (as Widdrington was) to know about the company's major transactions, although not immediately: "*When you just come on a Board you are not going to upset the apple cart, you're not going to make waves, you're going to sit there, you're going to observe the other directors, you expect the other directors to carry the ball till you are on stream and up to speed*"[3564].

[3291] Jarislowsky would expect that a director of a company such as Castor would know the company's main borrowers and projects for which loans were extended[3565].

[3292] With respect to the Morrison's report, Jarislowsky disagrees that the audited financial statements of Castor disclosed that Castor was a «*lender of last resort*» or that its activities were «*fundamentally high risk*».[3566] In fact, they disclose the exact opposite.

Rosen

[3293] Rosen expressed the opinion that audited financial statements did not provide assurance to investors.

> (...) there is a limited scope to attest audits and, on that particular basis, you then have to interpret the figures in light of the fact that they're primarily management's assertions, sometimes well audited, sometimes not.[3567]

[3294] Rosen confirmed that end users of financial statements should not solely rely on figures of said financial statements:

> Q. (...) is that end users got to go beyond what they see in the financial statements, correct, they have to ask questions, they have to get further information, they have to know the basis upon which the numbers are selected, is that correct?
>
> A- And that...
>
> Q- Is that correct?
>
> A- Correct, and that, what I have to correct about your comment is that the financial statements have notes and, in those notes, you were supposed to show what the accounting policies are and if one does a good job of reading the notes to try to pick up what the accounting policies are, that would go a long way before one man goes into the Internet and other sources.[3568]

[3564] Jarislowsky, April 5, 2005
[3565] Jarislowsky, April 5, 2005
[3566] PW-2405, p. 13
[3567] Rosen, February 26, 2009, p.106
[3568] Rosen, February 26, 2009, pp. 110-111

Defendants' experts

[3295] All the experts who were called by Defendants to testify at trial on the issue of reliance stated that making a sound business decision to invest in a company requires a substantial amount of information above and beyond what may be contained in the financial statements, especially if they are dated as in this case[3569].

Morrison

[3296] Morrison did not hesitate to characterize Widdrington as a sophisticated investor[3570] : while Widdrington was not a financial executive, he obviously had a strong command of financial statements, business valuations and due diligence[3571].

[3297] Morrison described Widdrington and his team of advisors as follows:

> unusually strong situation that Mr. Widdrington not only had his personal ability demonstrated track record, but in addition to that he had resources which were available to him and which clearly he used and relied on and in total made it an extremely strong situation[3572]
>
> You would rarely get the combination of greater advice or rapport, if I can use that word, amongst the team that would provide better input than Mr. Widdrington was quite fortunate enough to have.[3573]
>
> Well, the totality was extremely high. And this was, you know, certainly much higher than normal, even for a sophisticated investor it would be, you know, frankly hard to exceed the quality of investment advice that was available here[3574]

[3569] Lajoie, October 17, 2006; Morrison, October 4, 2006
[3570] Morrison, October 3, 2006, pp.156-164
[3571] Morrison, October 3, 2006, p. 158
[3572] Morrison, October 3, 2006, pp.163-164
[3573] Morrison, October 3, 2006, p.164
[3574] Morrison, October 3, 2006, p. 164

[3298] Morrison opined that :

- Widdrington, unfortunately, got inaccurate and out-of-date information from CIBC- the Royal Bank in fact had not been a significant or important lender to Castor for quite a few years in 1987 and, in fact, never really became a major lender to Castor.[3575]

- Widdrington regarded Stolzenberg vey highly, took many steps to introduce him to business relations and was eager to join him on Castor's board of directors[3576]. Widdrington had "*almost blind faith in Stolzenberg*".[3577]

- Widdrington's decision to invest in Castor was very important to him since the $1.1 million investment, required to become a Director in October 1989, represented about 20% of his total portfolio[3578] and that, therefore, the situation should have required a very thorough and careful evaluation before any investment commitment was made[3579].

- the information available to Widdrington was highly inadequate to make a sound decision on whether to invest in the package of debentures, preferred shares and common stock which he was offered[3580] - before he gave the go ahead, Widdrington did not have the shareholders' agreement and the mortgage portfolio analysis on hand.[3581]

[3299] Morrison recognized that the audited financial statements did, in fact, provide a degree of comfort as to the future. He acknowledged that Castor's extraordinary trend on retained earnings, as reflected in such statements for the period extending from 1978 to 1990, not only revealed a history of net profits accumulated, but indicated that the company would normally dispose of a buffer to weather more difficult times in the future.[3582]

[3300] Morrison acknowledged that there was a difference between the due diligence exercise required from someone buying a whole company and the due diligence required from someone making an investment as one of numerous shareholders in a company[3583].

[3301] Morrison was forced to recognize that it would make no sense for the Court to impose different standards of due diligence if the Court was to form an opinion on two

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[3575] Morison, October 3, 2006, p. 204; Morrison, October 4, 2006, pp. 8 and following
[3576] Morrison, October 3, 2006, p. 205 and following ; Morrison, October 4, 2006, pp.13-15
[3577] Morrison, October 3, 2006, p. 210, 217, 243
[3578] Morrison, October 3, 2006, p. 220
[3579] Morrison, October 3, 2006, p. 222
[3580] Morrison, October 3, 2006, p. 222 and following
[3581] Morrison, October 3, 2006, p. 231 and 238
[3582] Morrison, October 11, 2006, pp. 7-9 and 12
[3583] Morrison, October 3, 2006, p.73

plaintiffs who invested in Castor, one who made a $1.1 million investment that represented 1% of his net investment portfolio and one who made a $1.1 million investment that represented 20% of his net investment portfolio.[3584]

[3302] According to Morrison, if market conditions deteriorated, if Castor's growth slowed down, or if it developed financial problems, it might become difficult, if not impossible, for a shareholder to sell his shares[3585].

Lajoie

[3303] Lajoie was asked to answer the two following questions[3586]:

- What critical and essential information should a prudent investor and his professional advisor examine before making an investment decision?
- For each investment he made in Castor, was the information used by Widdrington sufficient to make a sound decision?

[3304] Lajoie opined that taking a sound business decision to invest in a corporation requires a substantial amount of information and a careful assessment thereof, and that the information required goes way beyond the simple financial information.

[3305] Lajoie pointed out that financial statements do not reveal some of the most critical factors that impact businesses[3587], such as management competence and continuity market trends. He mentioned that since these non-financial factors, determine the future structure and viability of a company more often than not, potential investors must carefully study them during their due diligence exercise.

[3306] Lajoie said that the burden of getting the required information to make a sound decision rests on the investor when he contemplates investing in a private corporation. Should he have difficulty in obtaining such information, or should he only get partial answers to his questions, the investor should wonder about the seriousness of the company and question his decision to invest in it.

[3307] Lajoie opined that the best document concerning information on a business was the Business Plan[3588], a document prepared by management periodically addressing the objectives of the corporation on a medium and a long-term basis together with the means taken and to be taken to achieve these objectives, and which is generally approved by the Board of directors.

[3584] Morrison, October 11, 2006, pp.148-150
[3585] Morrison, October 4, 2006, pp.65-79
[3586] D-867-1, p. 1
[3587] Lajoie, October 16, 2006, p.179
[3588] Lajoie, October 16, 2006, pp. 233 and following

[3308] Lajoie admitted that it could be comforting to know that the corporation had a solid background. He added that a prudent investor should nevertheless keep in mind that what he was buying was the future potential income or growth the investment had to offer. Therefore, the information to be obtained must also include information on the future financial health of the corporation.

[3309] Lajoie noted that Castor's growth was "remarquable, according to its audited consolidated financial statements"[3589].

[3310] Lajoie listed different types of information an investor should get and analyze before making his final decision, including past financial information, projected information and legal and corporate information.

[3311] Lajoie opined that, in 1989, Prikopa made a very good analysis[3590] and that he had correctly pointed out the level of risk of the business in which Castor was involved, i.e. the risky loan market. Prikopa had raised important issues such as:

- Sensitivity to financial market conditions.
- Quality of the loans portfolio taking into account the nature of the business of Castor.
- Trust in management.
- Lack of marketability of the Castor shares.
- Potential mismatch of the loan maturities and the debt maturities and potential difficulty to re-invest the money at profitable rates.

[3312] Lajoie shared Prikopa's comment "*How well you know the management and how the company conducts its business – the material or financial statements don't tell about that*"

[3313] Reviewing the information obtained and looked at by Widdrington and his advisors for the 1989 investment, Lajoie concluded that it was too basic and incomplete to arrive at a reasonable decision[3591] mainly because, in his opinion, none of the questions asked and answered, and none of the documents received and reviewed dealt with the future of the business[3592].

[3589] Lajoie, October 18, 2006, p.13
[3590] Lajoie, October 17, 2006, pp.39 and following
[3591] Lajoie, October 17, 2006, pp.81 and following
[3592] Lajoie, October 17, 2006, pp.120 and following

[3314] Lajoie opined that Widdrington did not take sufficiently into account various red flags that preceded his 1991 investment,[3593] which should have prompted his decision not to invest.

[3315] Lajoie acknowledged that Lowenstein and Jarislowsky were two experienced investors. [3594]

[3316] Lajoie said he shared the following comment made by Higgins, a C&L partner: "*an audit is essentially a search by the accountant for supporting documentation to confirm or corroborate the representations of the client*"[3595].

[3317] Lajoie admitted that audited financial statements were an important investment tool,[3596] and that the identity and reputation of the auditor, which he compared to a trade mark, were relevant factors. [3597]

[3318] Lajoie said anyone had to take for granted that the consolidated audited financial statements of Castor reflected the actual financial situation of Castor, as of their respective date, since it could not be otherwise. [3598]

[3319] Lajoie agreed that independence of the auditor was essential. [3599]

[3320] Lajoie acknowledged that when an investor had an unqualified audit opinion of a lender on hand, the investor could take for granted that, as of the date of said audited consolidated financial statements, the auditor had looked at the existence of the loans and at the borrowers' capacity to reimburse them. Lajoie acknowledged also that the auditor had to use the lowest of cost or net realizable value to assess the loans' worth, as assets[3600].

[3321] Lajoie recognized that the charts prepared from information appearing in the consolidated audited financial statements of Castor[3601] were showing very good, very interesting, highly impressive results[3602].

[3322] Obviously, had Lajoie been the investor, the fact that Castor was a private company, and the issue of exit ability, would have been deterrent[3603].

[3593] Lajoie, October 17, 2006, pp. 136 and following and pp. 250 and following
[3594] Lajoie, November 19, 2009, p. 32; Lajoie, November 20, 2009, p.37
[3595] Lajoie, November 19, 2009, pp. 36-43
[3596] Lajoie, November 19, 2009, p. 48
[3597] Lajoie, November 19, 2009, pp. 45-47
[3598] Lajoie, November 19, 2009, pp. 53 and following, p.64
[3599] Lajoie, November 19, 2009, pp. 63-64
[3600] Lajoie, November 19, 2009, p. 82
[3601] PW-2888 to PW-2892
[3602] Lajoie, November 19, 2009, pp. 128-132
[3603] Lajoie, November 19, 2009, pp.152 and 201 and following

Conclusions

[3323] When a witness is able to assist the Court in understanding the facts to which he is testifying, is consistent in his answers and does not contradict himself on significant issues or significant aspects of the litigation, and when the evidence as a whole corroborates his version of the facts, chances are the Court will attach credibility and reliability to his or her sayings. This neither means that a testimony will be discarded if the Court finds contradictions, nor that credibility and reliability will be granted in the absence of same.

[3324] Insofar as the circumstances of Plaintiff's decision to invest in Castor are concerned, Widdrington's testimony coupled with the testimony of Prikopa and Taylor is consistent with, and corroborated by, other evidence in the record. Notwithstanding some internal contradictions within Widdrington's testimony at discovery and trial, which are relatively minor, the Court finds the testimonies of Widdrington, Prikopa and Taylor credible and reliable.

[3325] As Lowenstein and Morrison said[3604], a high standard of prudence and care should be imposed upon a well-educated individual with a great deal of prior investment and business experience.

[3326] Defendants point to Widdrington's position as a director of Trinity, and suggest that, in that capacity, he should have been put on notice of Castor's undisclosed transactions with related parties and Castor's non-performing loan portfolio. In the circumstances established in evidence, using the standards of corporate governance that were generally followed in the 80s and without relying on hindsight, the Court does not share Defendants point of view.

[3327] Widdrington's role in Trinity was very limited. As an outside director, he was not involved in, or questioned on, the funding of Trinity's investment activities or any of its financial matters. Moreover, Widdrington testified that he was not aware of any affiliation or other form of relationship between Trinity's majority shareholder, namely First Holdings Cyprus Ltd., and the Castor group of companies. In fact, all that Widdrington knew was that Stolzenberg had injected 90% of the money in Trinity through one of his companies, but he did not recall First Holdings.[3605] Widdrington also testified he didn't have any specific knowledge of loans extended by Castor or its subsidiaries to Trinity for most of his tenure as a director of Trinity.[3606]

[3328] Prior to making his decision to invest in 1989, Widdrington was advised by three knowledgeable people and sophisticated readers of financial information (Prikopa, Taylor and Wood) who all considered the results to be excellent and enviable.

[3604] Lowenstein, March 23, 2005; Morrison, October 3, 2006
[3605] Widdrington, December 14, 2004
[3606] Widdrington, December 14, 2004

[3329] Prikopa and Taylor's testimony are clear, fully supported by the contemporaneous documents prepared at the time of the subject investments. Widdrington's testimony is coherent, corroborated by the testimony of Prikopa and Taylor, as well as by the documentation filed in the record.

[3330] Widdrington was fundamentally misled by the opinions contained in the consolidated audited financial statements, the valuation letters, and induced to make investments that he clearly would not have made without such statements or had he known the real gist of Castor.

[3331] Widdrington made equity and debt investments based on valuation letters that were provided to him prior to his investment in December 1989 and in October 1991. Each investment included units composed of common shares, preferred shares and debentures of Castor. The valuation letters specifically referenced these components of the fund raising activities of Castor.

[3332] Widdrington was entitled to accept and rely on such opinions for the purposes of his investments in 1989 and 1991 and the determination of the price that he was prepared to pay in connection therewith.

[3333] Widdrington would simply not have made investments in Castor absent the unqualified opinions by one of the world's largest and most prestigious accounting firms. If Castor's true financial position had been disclosed in the audited financial statements for the years ended 1988, 1989 and 1990, as well as in the share valuation letters, Widdrington would never have made any of his investments.

[3334] Plaintiff's experts on reliance, Lowenstein and Jarislowsky, were exceptionally qualified to opine on Widdrington's investments in the equity of Castor.

[3335] Had C&L done what they had to do, Castor would not have been able to present audited financial statements showing results even close to those appearing in C&L's audited reports and financial statements. Had C&L qualified its audit opinions and disclosed the extent of capitalization of interest Castor recognised as earnings, Widdrington would not have invested.

[3336] Widdrington relied on the knowledge and advice of those who had more experience than he had; i.e., Wood, Taylor and Prikopa. He was an experienced businessman based on his functions at Labatt and other companies, but certainly not a sophisticated investor in a company such as Castor. He was entitled to rely on the presumed knowledge, expertise and professionalism of C&L, who had acted as Castor's auditors since inception, and who had been valuing Castor's shares since 1980.

[3337] Prior to making his investments in Castor, Widdrington sought and obtained advice from three individuals with considerable experience in financial matters, thus acting prudently and reasonably, and exercising a proper measure of due diligence.

[3338] The various points underlined by Wood, Prikopa and Taylor, demonstrate that relevant matters were duly considered, prior to Widdrington making his investments. All of this in no way detracts from the proof that the two most important factors considered by Widdrington and his advisors were the following: the financial position of Castor, as reflected in the audited financial statements over a period of several years, and the fair market value of Castor's shares, as determined and opined upon by C&L. These factors easily outweigh any of the issues raised by his advisors.

[3339] Morrison acknowledged the very substantial and high-quality advice which Widdrington sought and obtained.[3607] Lowenstein testified that, as compared to the average typical high net worth investor, Widdrington's access to such expertise was both fortunate and unusual.[3608] This opinion was echoed by Jarislowsky.[3609]

[3340] Given the information that was provided year after year in the audited consolidated financial statements, it was reasonable for Widdrington to rely on same for his investments in Castor.

[3341] Experts for both the Plaintiff and the Defendants concurred that the audited consolidated financial statements disclosed results that were nothing less than spectacular.[3610] After reviewing the statements for December 31, 1988[3611] and for the five years 1984 to 1988 inclusive,[3612] as well as the interim unaudited statements for the nine months ended September 30, 1989,[3613] Prikopa stated in his memorandum to Widdrington that he considered Castor to be a profitable and high growth investment business.[3614] Lowenstein pointed out that the fact that the auditors did not consider losses as material was a strong indication of the financial health, business viability and future prospects of Castor.[3615]

[3342] Defendants are imposing a heavier burden on Widdrington than upon themselves as auditors and, further, are suggesting that Widdrington should have had the work of verification of Castor's financial position re-done; i.e. verify the audit work performed by C&L, supported by their unqualified audit opinion. This type of pretension was rejected by the Court in the case of *Morency v. Lafleur*.[3616]

[3607] Morrison, October 11, 2006, pp. 75-76
[3608] Lowenstein, March 21, 2005, pp. 73-74
[3609] Jarislowsky, April 4, 2005, pp. 15-16
[3610] Lowenstein, March 21, 2005, pp. 134-136; Morrison, on October 5, 2006, pp. 112-113; Morrison, October 11, 2006, pp. 15-16
[3611] PW-10-1
[3612] PW-10-2
[3613] PW-10
[3614] PW-43-1
[3615] PW-2404, p. 4
[3616] *Morency v. Lafleur*, [2002] CanLII 7992 (QC C.S), at paras. 25-26

[3343] Widdrington committed no fault, either in the exercise of his duties as a director of Castor, or in the due diligence exercised by him prior to making his respective investments in Castor.

[3344] Widdrington discharges his duty of care as director, given all the relevant circumstances.

> "The duty of care requires prudence and diligence. The duty of skill also requires prudence; but the two duties overlap to a certain extent. However, the type of prudence required for the duties of care and skill are different; the duty of care requires prudence based on common sense, whereas the duty of skill requires prudence based on experience. The duty of diligence, on the other hand, requires the director to keep himself informed as to the policies, business and affairs of the company. He must be aware of the functions and acts of the officers and **have a general knowledge of the manner in which** the business is conducted, the source of its revenue and the employment of its resources"[3617].
>
> In determining whether directors have acted in a manner that breached the duty of care, it is worth repeating that **perfection is not demanded**. Courts are ill-suited and should be reluctant to second-guess the application of business expertise to the considerations that are involved in corporate decision making, but they are capable, **on the facts of any case**, of determining whether an appropriate degree of prudence and diligence was brought to bear in reaching what is claimed to be a reasonable **business decision at the time it was made**.[3618] (our emphasis)

[3617] Wainberg and Wainberg. *Duties and responsibilities of Directors in Canada*, CCH Canadian Limited, 6th ed., 1987, p.18

[3618] *Magasins à rayons Peoples c. Wise* [2004] 3 R.C.S.461, p. 493, [2004] CSC 68, AZ-50277289, J.E. 2004-2016

The liability issue

[3345] The liability issue, assessing whether C&L shall be held liable for damages allegedly sustained by Widdrington, necessitates determining the applicable law and its content and, thereafter, its application to the specific facts of the Widdrington file (i.e. the findings on negligence, reliance and damages).

[3346] The obligation to determine the applicable law results from combination of the following facts:

- Castor is a corporation incorporated under a New Brunswick law.
- The audits of 1988, 1989 and 1990 were related to Castor which had its principal place of business in Montreal, Québec, but also subsidiaries in various foreign countries.
- C&L issued the consolidated audited financial statements of 1988, 1989 and 1990 after having performed audit work in Montreal (relating to CHL and the consolidation), and Zug and Schaan (relating to the various subsidiaries of Castor).
- Stand-alone audits of certain subsidiaries of Castor were done under the responsibility of various C&L firms (namely Ireland and Cyprus).
- C&L issued valuations letters.
- C&L issued Certificates for Legal for Life Opinions.
- In the relevant years, and when he instituted his action against C&L, Widdrington was a resident of the Province of Ontario. Plaintiffs in the other court claims are resident from various countries (mainly North America and Europe).

The applicable law

[3347] Plaintiff and Defendants agree that the issue of private international law at stake has to be resolved by application of conflict of law rules of the Civil Code of Lower Canada ("**CCLC**") [3619], articles 6 to 8, since the relevant facts took place prior to the entry into force of the Civil Code of Québec.

> 6. (...)
>
> The laws of Lower Canada relative to persons, apply to all persons being therein, even to those not domiciled there; subject, as to the latter, to the exception mentioned at the end of the present article.
>
> An inhabitant of Lower Canada, so long as he retains his domicile therein is governed, even when absent, by its laws respecting the status and capacity of persons; but these laws do not apply to persons domiciled out of Lower Canada, who, as to their status and capacity, remain subject to the laws of their country.
>
> 8. Deeds are construed according to the laws of the country where they were passed, unless there is some law to the contrary, or the parties have agreed otherwise, or by the nature of the deed or from other circumstances, it appears that the intention of the parties was to be governed by the law of another place; in any of which cases, effect is given to such law, or such intention expressed or presumed.

[3348] The required analysis is a 3 step process:

- Step # 1: Characterization of the question or questions.
- Step # 2: Identification of the appropriate conflict of law rules to apply.
- Step # 3: Identification of the legal system that governs the question or questions.

[3349] In order to apply the appropriate conflict of law rules to them, the legal nature of the questions that require adjudication must be ascertained.

[3350] The application of the conflict of law rules to the legal questions will lead to the identification of the legal system that governs the questions.

[3619] *Gauthier c. Bergeron*, [1973] C.A. 77, p.79; Claude Emanuelli, *Droit international privé québécois*, Montréal, Wilson & Lafleur, 2006, par. 412, par. 429, par. 437; Jeffrey Talpis et Jean-Gabriel Castel, *Le Code civil du Québec- Interprétation des règles de droit international privé*, dans *La Réforme du Code civil*, t.3, Québec, Presses de l'Université Laval, 1993, 801, par.95; Gérald Goldstein et Ethel Groffier, *Droit international privé*, t.1, *Théorie générale*, Cowansville, Yvon Blais, 1998, pp.195-197

[3351] The application of the proper law to the facts leads to definite answers to the questions that require adjudication.

Positions in a nutshell

Plaintiff's position

[3352] Plaintiff argues that:

- The question that requires adjudication is a matter of professional liability, a matter of delictual liability.
- C&L's professional liability is to be governed by the Quebec law where C&L operated and committed the various faults giving rise to the claims, "*lex loci delicti*". Knowing its consolidated audited financial statements, valuation letters and Certificates for Legal for Life Opinions were used and to be used, and relied upon, by decision-makers, lenders and investors, C&L failed to perform proper audits and other work, and C&L issued faulty audited consolidated financial statements (in 1988, 1989 and 1990), share valuation letters and Certificates for Legal for Life Opinions.
- It is neither a matter of status or capacity, nor a matter of contract.
- If the Court was to conclude that it is a matter of contract, Quebec law would still apply since evidence reveals that C&L' s contracts with Castor were concluded in Montreal, Quebec[3620].

Defendants' position

[3353] Defendants argue that:

- The question that requires adjudication is a matter of status or capacity, or a matter of contract.
- Castor auditors' liability, like that of any other person holding an office in a corporation, is to be governed by the "*lex societatis*": hence, New Brunswick law, since Castor was incorporated under the NBBCA.
- Moreover, since the law governing a contract, the "*lex contractus*", also governs the extra-contractual liability resulting from its faulty performance[3621], this also

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[3620] D-4

[3621] As now codified in article. 3127 of the Civil Code of Québec (« **CCQ** »); V. Heuzé, «La loi applicable aux actions directes dans les groupes de contrats» 1996 R.C. D.I.P. 243, at p. 261 ff

leads to the application of New Brunswick law, as the audit contract entered into between Castor and C&L is governed by New Brunswick law[3622].

- Subsidiary, the question that requires adjudication is a matter of delictual liability. If an auditor's liability is to be governed by the law of tort, the "*lex loci delicti*", then Ontario law applies to the Widdrington case. Ontario is the *locus delicti* as it is the place of the fault, the place where Widdrington received the documentation and allegedly relied on it[3623] and, more importantly, the place of the prejudice, a purely economic prejudice.

Evidence

[3354] Even though Castor was a New Brunswick corporation, its principal place of business was located at 1801 McGill College Avenue, suite 1450, Montreal, from where its activities were managed and directed.

[3355] For the relevant years, 1988, 1989 and 1990, C&L was appointed auditor of Castor at the annual general meeting of shareholders[3624]. However, their remuneration as such was to be fixed by the Board of directors, as it appears from the shareholders resolutions[3625], and the scope of their services was, from time to time, a matter of discussions and agreements as it appears from a letter dated January 14, 1988, from Wightman to Stolzenberg[3626].

> The foregoing relates only to our statutory responsibilities and we are **always prepared to extend the scope** or our examination if you so desire. (...)
>
> **In addition to** conducting audits, we also offer services in many other areas, (...)
>
> *(Emphasis added)*

[3356] As a matter of fact, C&L rendered a wide range of professional services to Castor[3627].

[3622] Article 8 of the Civil Code of Lower Canada ("**CCLC**") and D-4

[3623] *B.C. v. Imperial Tobacco Canada Ltd.*, [2006] BCCA 398, par. 62, 67-68 (leave to appeal denied, April 5, [2007], SCC no. 31715 ; *Roeder v. Chamberlain*, [2008] B.C.J. no. 893 (BCSC), par. 37-43; *Leclerc v. Rouer*, J.E. 2006- 1796, par. 18-21 (C.Q.)

[3624] PW-2400-100, PW-2400-103, PW-2400-114 or D-6

[3625] PW-2400-100, bates 017742 (1988); PW-2400-103, bates 017829 (1989); PW-2400-114, bates 017988 (1990)

[3626] D-4

[3627] See for example the following invoices for professional services: PW-2511, PW-2519, PW-2540, PW-2541, PW-2670, PW-3100, PW-3104, PW-3105, PW-3106 and PW-3107

[3357] The audit field work was performed in Montreal by the Montreal audit team or in Zug and Schaan by the European audit team. Except for Hunt, who was called in at the last minute to help out in the 1990 audit[3628], all members of those teams were employees based in C&L's Montreal office[3629].

[3358] The European team reported to Jean-Guy Martin, a partner of C&L based in Montreal who himself reported to Wightman, the engagement partner, also a partner of C&L based in Montreal.

[3359] The consolidation took place in Montreal as well as the second partner review[3630], which was performed by Allan Cunningham[3631] in 1988, and by Michael Hayes in 1989 and 1990, both audit partners of C&L based in Montreal[3632].

[3360] As the last audit step, Wightman held final wrap-up meetings with Stolzenberg, at Castor's offices in Montreal.

[3361] The audit reports and the audited financial statements were indisputably issued in Montreal, on C&L's letter paper. C&L's Montreal office address was printed on its letterhead.[3633] Neither the financial statements, nor the audit reports in litigation mentioned that Castor was a New Brunswick corporation[3634].

[3362] C&L's purpose in performing Castor's audits was not only to assist Castor's shareholders, as a group, in their task of overseeing management. There were multiple purposes for doing those audits.

[3363] The audits were performed in the following circumstances:

- C&L knew that it would, itself, rely on its audit work products to perform other tasks and issue other opinions (valuation letters and Certificates for Legal for Life Opinions)[3635].
    - In its first valuation letter issued on March 19, 1980, C&L wrote:

> You have asked us as professional accountants experienced in business and securities valuations for our opinion as to the fair market value at (...)
>
> <u>Scope of Investigation</u>

[3628] Hunt, March 28, 1996, pp. 4-11
[3629] PW-2619
[3630] TPS-A-209
[3631] Cunningham, December 13, 1996, pp. 7-8
[3632] Hayes, October 31, 1995, pp. 8 to 16
[3633] PW-5 tab 10, 11 and 12
[3634] PW-5 tab 10, 11 and 12
[3635] PW-6-1 and PW-7

> In arriving at our opinion, we have reviewed and relied upon the consolidated financial statements of Castor for the two years ended December 31, 1979. We have also reviewed our working paper files prepared in connection with the 1979 audit[3636]

- In subsequent valuation letters, namely in those that were issued between January 1, 1988 and October 22, 1991, C&L wrote that the purpose was to update previous letters relating to valuations of shares of Castor prepared at various dates.[3637]

- Based upon its audit work for each of the five previous years, C&L certified various items, as independent auditors of Castor, in Certificates for Legal for Life Opinions, namely those issued on March 6, 1989, February 16, 1990 and February 15, 1991[3638].

- C&L knew that the audited financial statements, or their by-products, would be distributed to third parties and relied upon for the purposes of allowing and making investment decisions.

  - After revision by C&L, at the request of Wightman, 1 500 copies of a brochure which included information on the financial statements were printed annually. [3639]

  - Brochures were written or translated in various languages.[3640]

  - In a letter dated March 8, 1991 to Stolzenberg, Wightman enclosed 100 copies of the C&L valuation letter[3641] whereas there are less than 14 directors at Castor[3642].

  - In July 1991, Wightman met with M. Gilligan and M. Martin from Bayerische Bank who wanted to speak to someone knowledgeable who had the ability to confirm the financial well-being of Castor. With them, Wightman went through the various steps of C&L's auditing process.[3643]

[3636] PW-6-1 (tab 1)
[3637] PW-6-1 (tab 17 to 24 inclusive)
[3638] Part of PW-2473 (see also PW-7)
[3639] Wightman, March 11, 2010, pp. 36-39, 69-71; PW-2372-18 (for 1988); PW-2372-19 (for 1989) and PW-2372-14 (for 1990)
[3640] D-187, PW-2474-2
[3641] PW-2679 or PW-2315
[3642] PW-2400-114 to PW-2400-120
[3643] Martin, November 5, 2008 and November 6, 2008; PW-72

- C&L knew that Castor's financing, through lenders or investors, was dependent on its audited financial statements, valuation letters and certificates for Legal for Life Opinions[3644].

    - In the absence of the Legal for Life Opinions prepared from time to time by McCarthy Tétrault for Castor, opinions largely resting upon C&L's Certificates,[3645] the various companies listed in such opinions might not have been able to invest in Castor's shares, common or preferred, or promissory notes[3646].

    - In a letter dated September 23, 1987, Wightman wrote to Stolzenberg:

        > *As you are aware, for a number of years, Castor has been issuing and redeeming shares on the basis of periodic valuation reports prepared by us.*
        >
        > *Because shareholders have come and gone over the years based on the valuations and if you intend to raise additional capital in the future base on these valuations....*[3647]

    - In a draft letter to Stolzenberg dated December 2, 1987, prepared by Wightman, which is part of C&L's working papers and which addresses the topic of calculations of capitalized values of common shares based on yields and price/earnings multiples, Wightman explained:

        > *Furthermore these calculations are not meant to necessarily establish fair market values for these shares which we calculate and report on separately from time to time for purposes of potential increases in capital of (CHL)*[3648]

[3364] C&L knew that the financial statements of Castor upon which they were reporting could affect the economic interests of the lenders and investors as well as those of shareholders and potential shareholders of Castor.

[3365] The fact that many different people (e.g., lenders, investors, etc.) would rely on their audit reports was not only reasonably foreseeable but was well known to C&L, and accepted by C&L.

[3644] See for example: Simon, June 16, 2009, 69 to 81
[3645] PW-2473
[3646] Simon, June 16, 2009, pp. 75-81; PW-2473
[3647] PW-665-2, at page 3
[3648] PW-1053-50B-1, sequential page 166

Characterization of the question or questions

[3366] Characterizing implies identifying the legal category into which the case falls, taking account of its particular facts, under the Quebec civil law[3649].

> (...) le choix du système légal que le tribunal doit appliquer au litige. À son tour, ce choix dépend de la qualification du problème juridique. Il est de toute première importance de retenir, à ce moment, que seules les lois du Québec doivent alors recevoir considération. (...) Comme l'écrivait avec raison le professeur Paul Crépeau :
>
> > Les règles de conflits sont des règles propres à chaque système; elles ne doivent, elles ne peuvent être interprétées, comme d'ailleurs les règles internes, que par les modes d'interprétation du système juridique qui les a conçues[3650].

[3367] Professor Groffier describes the qualification exercise as follows:

> C'est l'étape de l'identification du problème.
>
> (...) On peut dire, très généralement, qu'il s'agit d' »une opération intellectuelle indépendante du conflit de lois et qui est, en réalité, l'un des facteurs fondamentaux du raisonnement juridique ». Le juge doit y recourir constamment, puisque « qualifier, c'est attribuer l'existence juridique à un être, à une chose, à un fait en le rangeant dans une catégorie légale. ». (...)
>
> L'objet de la qualification sera le plus souvent non pas le fait en lui-même mais bien le rapport juridique dans lequel il s'inscrit[3651].

[3368] Professor Emanuelli writes:

> Le choix de la règle de conflit pertinente dépend de la qualification de la question qui est à l'origine du conflit[3652].

[3369] The relevant questions therefore are:

- What is the crux of the litigation?
- What are the issues opposing the litigants?

[3649] *Gauthier* c. *Bergeron* [1973] C.A. 77, AZ-73011017; Claude Emanuelli, *Droit international privé québécois*, 2 ed. edition, Wilson & Lafleur, 2006, p.207

[3650] *Gauthier c. Bergeron* [1973] C.A. 77, p.79

[3651] Ethel Groffier, *Précis de droit international privé québécois*, 4ième édition, Éditions Yvon Blais Inc.pp.41-42

[3652] Claude Emanuelli, *Droit international privé québécois*, 2e ed. , Wilson & Lafleur, 2006, p.209

[3370] In paragraph 118 of his re-re amended declaration, Widdrington alleges:

> As professional accountants, Defendants owed a duty to Plaintiff to conduct their audits, and all other professional services rendered to Castor in relation to the reliability of the financial statements and the valuation of Castor, in accordance with the Canadian Generally Accepted Accounting Principles ("GAAP"), the Canadian Generally Accepted Auditing Standards ("GAAS"), the Canadian Institute of Chartered Accountants Handbook ("CICA") and the Code of Ethics of the Canadian Institute of Chartered Business Valuators ("CICBV") namely but without limitation:..."

[3371] Widdrington is claiming damages from C&L as a result of losses he sustained and which he attributes to multiple C&L wrongdoings – negligent audit work, negligent valuation work, erroneous audit opinions, erroneous valuation opinions and erroneous Certificates for Legal for Life Opinions. Widdrington relied on C&L's work in its entirety to invest in Castor and to act in matters of dividends issuance.

[3372] Plaintiffs in the other cases present similar claims.

[3373] In paragraph 118 of their re-re-amended particularized plea, Defendants allege:

> They deny paragraph 118 of the Plaintiffs Declaration in so far as they owed no duty whatsoever to Plaintiff and further add that, in any event, based upon the information available to them at the time they performed their work, which they had no valid reason to disbelieve or doubt in any way, all of their services in connection with Castor's financial affairs were performed in accordance with the standards of their profession and the conclusions they arrived at were reasonable under the circumstances;

[3374] The gist of the matter is the liability of Defendants towards those who alleged they have suffered some economic damage in consequence of C&L's negligence.

[3375] In Quebec civil law, any matter of liability of a wrongdoer towards those who have suffered some economic damage in consequence of his or her negligence is clearly characterized as a matter of civil liability. It is not a matter of status or capacity[3653], even though the status or capacity of the wrongdoer might be an issue of the matter.

[3376] Even though status and capacity are determined by the law under which a corporation has been incorporated, activities of a corporation are subject to the law where such activities took place.

[3653] Jeffrey A. Talpis, *Aspects juridiques de l'activité des sociétés et corporations étrangères au Québec*, [1976] *C.P. du N.*, para. 76, 77, 78 and 89

[3377] In their treatise "*La responsabilité civile*", Baudoin and Deslauriers write:

> À l'égard de son client, la responsabilité du comptable est soumise aux règles générales du droit des obligations (art. 1371 et s. C.c.) et donc, en fonction de la qualification exacte de l'engagement (mandat, contrat de service, contrat mixte sui generis), aux règles propres à ces différents contrats. (...) À l'égard des tiers, le recours tire son fondement des règles de la responsabilité extracontractuelle, notamment de l'article 1457 C.c..[3654]

[3378] In essence, the questions that require adjudication are liability issues in relation to work done, audit and valuation, and opinions issued by accountants, namely in the performance of their duties as auditors to Castor.

Identification of the appropriate conflict of law rules

[3379] The general Québec conflict of law rules to apply to liability issues are :

- For delictual liability - the "*lex loci delicti rule*", according to section 6(3) CCLC.
- For contractual liability - the "*lex contractus rule*", according to section 8 CCLC.

[3380] There was no contract between Widdrington and C&L. Therefore the matter is delictual. The same conclusion applies to most other claims, if not all of them.

Lex loci delicti

[3381] The general Québec conflict of law rule to apply to quasi-delictual liability issues is the *lex loci delicti* rule.

[3382] The *lex loci delicti* rule means the place where the alleged wrongdoings (reproached acts) took place[3655], the place where the wrongful activity occurred[3656].

[3654] Jean-Louis Baudoin and Patrice Deslauriers, *La responsabilité civile*, Volume II- Responsabilité professionnelle, 7e ed. Éditions Yvon Blais Inc. p.176

[3655] Ethel Groffier, *Précis de droit international privé*, 4e ed., Éditions Yvon Blais, 1990, para. 225 at page 217; Paul-André Crépeau, *De la responsabilité civile extracontractuelle en droit international privé québécois,* 1961, 39 R. du B Can, pp. 3-29; Jean Pineau and Monique Ouellette-Lauzon, *Théorie de la responsabilité civile*, Éditions Themis; *Tolofson c. Jensen*, [1994] 3 R.C.S. 1022, para.43,45 and 94; *Lister c. McAnulty*, [1944] S.C.R. 317

[3656] Jean-Gabriel Castel and Janet Walker, *Canadian conflict of laws*, volume 1, 6th edition, Lexis Nexis, at page 35-18

[3383] No doubt employees and partners of C&L who participated in the audits or rendered other professional services to Castor, all practising professionals in the province of Quebec, adjusted their conduct and estimated what obligations they might incur should they cause prejudice as a result of deviation from the Quebec laws.

[3384] The *lex loci delicti rule* responds to a number of sound practical considerations as the Supreme Court wrote in *Tolofson* c. *Jensen*:

> The rule has the advantage of certainty, ease of application and predictability. Moreover, it would seem to meet normal expectations. **Ordinarily people expect their activities to be governed by the law of the place where they happen to be** and expect that concomitant legal benefits and responsibilities will be defined accordingly[3657]. (emphasis added)

[3385] As the evidence summed-up under the subheading "evidence" of the present section of this judgment establish,[3658] the wrongdoings (the reproached acts : the negligent issuance of audit reports, consolidated audited financial statements, valuation letters and Certificates for Legal for Life Opinions) took place in Montreal, at C&L's Montreal office where the wrongful activity (issuance of various misstated and misleading work products) occurred.

[3386] Quebec law applies.

Auditors' Professional liability and The Quebec laws

Applicable rules

[3387] Since all the relevant events took place before January 1, 1994, the Civil Code of Lower Canada applies according to article 85 of the *Act respecting the implementation of the reform of the Civil Code*.[3659]

> **85.** The conditions of civil liability are governed by the legislation in force at the time of the fault or act which causes the injury.

[3388] General rules of civil liability read as follows:

> **1053**. Every person capable of discerning right from wrong is responsible for the damage caused by his fault to another, whether by positive act, imprudence, neglect or want of skill.

[3657] [1994] 3 R.C.S. 1022, para. 44

[3658] Facts mentioned in the other parts of the present judgment are also relevant (they all point to the same conclusion)

[3659]

> **1073.** The damages due to the creditor are in general the amount of the loss that he has sustained and of the profit of which he has been deprived; subject to the exceptions and modifications contained in the following articles of this section.

[3389] Therefore, to succeed, a plaintiff needs only prove a fault, damage, and the causal connection between the fault and the damage.[3660]

[3390] The professional liability must be determined based on the conduct of a similar professional, acting reasonably, the whole as determined by the Supreme Court of Canada in the case of *Roberge*:[3661]

> «[TRANSLATION] A professional will therefore not incur liability unless he or she acts in a manner inconsistent with that of a reasonable professional.»

[3391] A plaintiff must demonstrate that the auditors' fault is the logical, direct and immediate cause of the damages claimed.[3662]

[3392] With respect to causation, Professor Jean-Louis Baudouin assesses the general position in Quebec concerning causation in *La responsabilité civile délictuelle,* as follows:[3663]:

> [TRANSLATION] The only real constant in all the decisions is the rule that the damage must have been the logical, direct and immediate consequence of the fault. This rule, stated many times by the courts, indicates a desire to limit the scope of causation and accept as causal only the event or events having a close logical and intellectual connection with the damage complained of by the victim. »

[3393] The auditor's negligence will not be considered the cause of the loss if a plaintiff cannot prove actual reliance on the professional opinions: for example, when the decision to invest was made before the professional opinions were provided to him,[3664] the investments were made before the professional opinions were issued,[3665] and when the plaintiff does not prove that proper disclosure by the professionals would have changed his or her decision to invest.[3666]

[3660] (1990), R.R.A. 303.
[3661] *Roberge c. Bolduc* [1991] 1 R.C.S. 374 at 395, AZ-91111033, J.E. 91-412; *Caisse Populaire de Charlesbourg v. Michaud*, [1990] R.R.A. 531 (Q.C.A), AZ-90011568, J.E. 90-814.
[3662] Jean-Louis Baudouin and Patrice DesLauriers, *La responsabilité civile, vol. II – responsabilité professionnelle, 7th ed., (*Cowansville, Qc: Yvon Blais, 2007) paras. 2-186.
[3663] (3rd ed. 1990), at No. 353, pp. 192-93; *Roberge c. Bolduc*, [1991] 1 R.C.S. 374, [1991] CanLii 83 (S.C.C.) at page 85.
[3664] *Allaire c. Girard & Associés (Girard et Cie comptables agréés),* [2005] QCCA 713 (CanLII), at para 53-54.
[3665] *Rouleau c. Placements Etteloc inc.,* [2006] QCCS 5319 (CanLII) at para. 288.
[3666] *Allaire c. Girard & Associés (Girard et Cie comptables agréés),* [2005] QCCA 713 (Can LII), at para. 56.

[3394] Accountants and auditors are liable towards those who, with their knowledge or consent, make use of their work products, as the Quebec Court of Appeal said in 1990 in *Caisse populaire de Charlesbourg c. Michaud*[3667], in 2005, in *Allaire v. Girard & Associés*[3668], and recently, in 2009, in *Agri-capital Drummond inc.* v. *Mallette.* [3669]

[3395] In *Michaud*[3670], the Quebec Court of Appeal ruled that when auditors render professional opinions, they assume responsibility for the consequences of their representations, regardless of the intended purpose of the document. According to authors Baudouin and Jobin, audited financial statements are not the type of professional opinions that are kept in the client's drawer. Therefore, the auditor must carry out his obligations with care and diligence in order to be considered to have acted reasonably towards third parties who rely on them.[3671]

[3396] Defendants suggest that *Hercules*[3672] has been imported into Quebec law as a result of a comment made by the Quebec Court of Appeal in its 2005 decision of *Savard.*[3673]

[3397] To the extent that Defendants suggest that such an "*importation*" would change or add to the rules of civil liability provided for by article 1053 *C.C.B.C.*, the Court disagrees.

[3398] In Savard, the appellants were trying to hold two lawyers, who did not represent them, responsible for their loss due to a transaction in which they were all involved. The first judge found that the lawyers' liability had not been engaged, although the court clearly acknowledged that lawyers could be held accountable to third parties for their actions:

> «Il ne fait aucune doute qu'un avis juridique erroné ou la communication de fausses informations dans le prospectus peut engager la responsabilité de l'avocat»[3674].

[3399] The Quebec Court of Appeal agreed that lawyers could be held liable toward third parties, based on professional faults committed in the execution of their mandates,

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[3667] *Caisse populaire de Charlesbourg c. Michaud*, [1990] R.R.A. 531 (Q.C.A.).
[3668] (2005) Q.C.C.A. 713; See also : Baudouin, La responsabilité civile, 7e édition, 2-182 à 2-190; *Besner c. Friedman & Friedman*, [2004] R.R.A. 1013 (j. Lacoursière, C.S.); *BDC c. Pfeiffer*, [2009] R.R.A. 848 (Juge Payette, C.S.).
[3669] [2009] QCCA 1589 at paragraphs 28-30.
[3670] *Caisse Populaire de Charlesbourg c. Michaud*, [1990] J.Q. no. 673, 30 Q.A.C. 23, [1990] R.R.A. 531 at p. 8
[3671] Jean-Louis Baudoin et Pierre-Gabriel Jobin, *Les obligations*, 6e édition par P.-G. Jobin avec la collaboration de N. Vézina, 2005 at para 507.

[3672] *Hercules Managements Ltd c. Ernst and Young*, [1997] 2 R.C.S. 165
[3673] *Savard c. 2329-1297 Québec inc. (Hôtel Lord Berri inc.)*, [2005] QCCA 705 (CanLII)
[3674] *Savard c. 2329-1297 Québec Inc.*, [2003] CanLII 4455 (QC C.S.) at para. 245

although, like the first judge, it concluded that the reviewed case was not a situation where the lawyers' extra-contractual liability was engaged. In reaching this conclusion, the Court drew an analogy with the case of auditor's liability and referred to *Hercules*[3675] and *Haig*[3676] for the proposition that auditors can be held liable to third party users whom they know, or ought to know, might use audited financial statements.[3677]

> [95] (...) la responsabilité d'un comptable est retenue lorsque le lien de causalité entre l'acte fautif commis à l'occasion de la préparation des états financiers de son client et le dommage subi par un tiers découle de la connexité créée par la connaissance par ce professionnel du rôle ou de l'usage de ses états financiers par cette autre personne qui n'est pas son client. Le strict lien contractuel client-professionnel est ainsi dépassé par la constitution d'un rapport nouveau découlant de la diffusion des états financiers, créant ainsi une obligation de diligence pour le professionnel en faveur du tiers non client.

[3400] In *Savard*, the Quebec Court of Appeal had to deal with extra-contractual liability of lawyers, not auditors, and, besides, the Court specifically wrote:

> [96] **Cette approche** peut sans doute **être d'un certain secours** à l'occasion de l'examen de la situation de l'avocat. Il ne faut toutefois pas perdre de vue **le contexte particulier dans lequel évolue l'avocat** en raison de l'exclusivité de ses services et de la confidentialité du contenu de ses communications. Dès lors, en règle générale, il ne se tisse pas de lien entre un avocat et un tiers.
>
> [97] (...) L'avocat, comme d'ailleurs tout professionnel, n'est pas responsable de la perte économique subie par tous ceux qui gravitent autour de lui à quelque titre ou quelque occasion que ce soit. Toute autre approche aurait pour effet de lui imposer « a liability in an indeterminate amount for an indeterminate time to an indeterminate class », pour reprendre la phrase célèbre du juge Cardozo dans Ultramares Corp. c. Touche. (our emphasis)

[3401] The audit opinion differs from a legal opinion provided to a specific client for a specified purpose, as was the situation in the *Savard* case.

[3402] Baudouin has explained that where a document clearly states the purpose for which it was prepared, a third party will have difficulty in arguing that it could be used for another purpose[3678], and the Court agrees. This does not conflict with *Michaud*, nor does it place any limitation on audited financial statements in the absence of a documented restriction which appears therein.

[3675] *Hercules Managements Ltd c. Ernst and Young*, [1997] 2 R.C.S. 165
[3676] *Haig* v. *Bamford*, [1977] 1 S.C.R. 466
[3677] *Savard c. 2329-1297 Québec inc. (Hôtel Lord Berri inc.),* [2005] QCCA 705 (CanLII) para. 95

[3678] Baudouin, *La responsabilité civile*, 7e édition, 2-189

[3403] Jean-Louis Baudouin is critical of the suggested interpretation of *Savard* made by the Defendants. In the most recent edition of his treatise on Quebec civil and professional liability[3679], he wrote that the comments made in Savard do not change the longstanding position in Quebec that common law concepts are not applicable in Quebec.

[3404] Baudoin's position was approved by the Quebec Court of Appeal in a 2009 decision [3680] and the Supreme Court rejected leave to appeal this decision.[3681] Based on Baudouin's analysis of *Savard* , Justice Pierre Dalphond stated the following:

> [30] En somme, la responsabilité des comptables et vérificateurs externes peut être engagée contractuellement envers les clients pour lesquels ils ont préparé des états financiers et extra contractuellement envers ceux dont ils savent qu'ils pourront faire usage desdits états, comme les actionnaires (La responsabilité civile, 7e éd., vol. II, Cowansville, Édition Yvon Blais de Baudouin et Deslauriers, paragr. 2-168 et suivants). Les auteurs Baudouin et Deslauriers écrivent aux paragr. 2- 186 à 2-188:
>
> > 2-186 – Droit civil – Inévitablement, la question se pose de savoir si les solutions dégagées par la Cour suprême en common law sont directement transportables en droit civil. Un **obiter** de la Cour d'appel semble le laisser entendre. À notre avis, la réponse est négative, même si ces enseignements sont évidemment intéressants sur le plan du droit comparé. Les conclusions auxquelles arrive la Cour reposent en effet sur une qualification et une catégorisation des liens de droit et des comportements propres au système de common law, mais étrangères au droit civil. Ainsi, en droit civil, il n'est ni utile, ni nécessaire de référer aux concepts de « duty of care », de « negligent misrepresentation », de « detrimental reliance », de « implied condition of merchantability », mais, plus simplement, aux concepts traditionnels de faute, de dommage et de lien causal. De plus, la traditionnelle méfiance de la common law à l'égard du « pure economic loss », chef de dommage largement reconnu au Québec, incite à une prudence accrue.
> >
> > 2-187 – Interprétation large – **Le droit civil adopte donc une position différente**, moins restrictive et, ce faisant, offre une protection accrue aux tiers. Certaines décisions, dont le raisonnement peut toutefois être rapproché de celui de common law, fondent leur analyse sur la preuve de la connaissance qu'avait le comptable de l'utilisation potentielle par les tiers des états financiers. D'autres vont plus loin et se démarquent nettement de la common law, en considérant que le recours est indépendant de la destination initiale des rapports, l'accordant ainsi à

[3679] Baudouin, *La responsabilité civile*, 7e édition, Tome 1 et Tome 2

[3680] *Agri-capital Drummond inc.* v. *Mallette,* [2009] QCCA 1589 at para. 30, AZ-50572993, J.E. 2009-1668, [2009] R.R.A. 935

[3681] *Mallette, s.e.n.c.r.l., Gratien Nolet et al. c. Agri-Capital Drummond Inc.,* [2010] CanLII 6341 (C.S.C.)

> tous les lecteurs potentiels des états financiers. Cette responsabilité est le tribut à payer pour le professionnalisme de ce métier, le caractère technique et complexe de ses analyses et la confiance du public dans la qualité des actes posés.
>
> 2-188 – Illustrations jurisprudentielles – La jurisprudence offre certaines illustrations. Ainsi, des prêteurs, des actionnaires et des investisseurs éventuels ont obtenu gain de cause contre des comptables en vertu du régime extracontractuel.[3682] (our emphasis)

[3405] As a review of the Quebec jurisprudence shows that professionals who issue an opinion for a specific purpose are not generally held liable towards a third party when such a third party was not an intended recipient of the opinion and relied on the opinion for a purpose that the professional could not foresee and which is different than the purpose for which the opinion was prepared[3683]. This is not our case.

[3406] Using precedents from Supreme Court of Canada decisions in matters other than those arising from Québec, as well as precedents from outside Québec, always requires caution and foresight. The Québec Court of Appeal and the Supreme Court have issued that reminder many times.[3684]

[3407] Again, under the Quebec liability rules, to succeed a plaintiff need only establish a fault, a damage, and the causal connection between such fault and such damage.[3685]

[3408] A defendant's liability can be limited if he or she proves that a fault by the plaintiff is also the logical, direct, and immediate cause of the plaintiff's loss.[3686] In such a case, the court apportions liability based on an "*assessment of the relative gravity of each fault*", the analysis of which is based on "*instinct and common sense.*"[3687]

[3682] *Agri-capital Drummond inc. v. Mallette*, [2009] QCCA 1589 at para. 30, AZ-50572993, J.E. 2009-1668, [2009] R.R.A. 935, leave to appeal at the Supreme Court of Canada dismissed: *Mallette, s.e.n.c.r.l., Gratien Nolet et al. c. Agri-Capital Drummond Inc.*, [2010] CanLII 6341 (C.S.C.)

[3683] *Robinson c. Barbe*, [2000] CanLII 11355 (QC.C.A.); *Banque canadienne impériale de commerce, c. General Appraisal of Canada Limited*, [1993] J.Q. no 1042 (C.A.); *Caisse populaire des fonctionnaires c. Plante* [1990] R.R.A.250 (C.A.); *Placements Miracle Inc. c. Larose*, [1980] C.A., 287;

[3684] *Poulin v. Prat* (C.A., 1994-02-22), AZ-94011268, J.E. 94-450, [1994] 61 Q.A.C. 231, [1994] R.D.J. 301 (C.A.); *Glegg c. Smith & Nephew Inc.*, AZ-50314388, [2005] CSC 31, J.E. 2005-994, [2005] 1 R.C.S. 724; *Bibaud c. Québec (Régie de l'assurance maladie)*, AZ-50256555, [2004] CSC 35, J.E. 2004-1247, [2004] 2 R.C.S. 3; *Prud'homme c. Prud'homme*, [2002] 4 R.C.S. 663; *Lac d'amiante du Québec Ltée c. 2858-0702 Québec inc.*, AZ-50100126, [2001] CSC 51, J.E. 2001-1735, [2001] 2 R.C.S. 743

[3685] *Allaire c. Girard & Associés (Girard et Cie comptables agréés)*, [2005] QCCA 713 (CanLII), para 32

[3686] *Cie. d'assurance Standard Life v. McMaster Meighen*, 2005 CanLII 25720 (QC C.S.), at para. 169, affirmed by Court of Appeal, *Cie. d'assurance Standard Life v. McMaster Meighen*, [2007] QCCA 1273, AZ-50451579, J.E. 2007-1897.

[3687] *Cie. d'assurance Standard Life v. McMaster Meighen*, 2005 CanLII 25720 (QC C.S.), at para. 182, affirmed by Court of Appeal, *Cie. d'assurance Standard Life v. McMaster Meighen*, [2007] QCCA 1273, AZ-50451579, J.E. 2007-1897.

[3409] The duties of skill and diligence owed by directors, who are deemed to be mandataries, are set out in article 1710 of the *Civil Code of Lower Canada*, which reads as follows:

> **1710.** The mandatary is bound to exercise, in the execution of the mandate, reasonable skill and all the care of a prudent administrator.

[3410] Sections of the *New Brunswick Business Corporations Act*,[3688] under which Castor was incorporated, set out that :

> **80(3)** A director is not liable under section 76 or 79 if he reasonably relies in good faith upon
>
> (a) financial statements of the corporation represented to him by an officer of the corporation or in a written report of the auditor, if any, of the corporation fairly to reflect the financial condition of the corporation; or
>
> (b) a report of a lawyer, accountant, engineer, appraiser or other person whose profession lends credibility to a statement made by him.»

[3411] The relevant provisions of the Ontario *Business Corporations Act*,[3689] enacted in 1990, are virtually identical to the foregoing statutory provisions.

[3412] Section 123.84 of the Quebec *Companies Act*[3690] sets out a presumption to the effect that the duty of diligence and care of directors was met by relying on expert reports in good faith.

> **123.84.** A director is presumed to have acted with appropriate skill and all the care of a prudent administrator if he relies on the opinion or report of an expert to take a decision.

[3413] According to M[e] Paul Martel, even without such statutory provisions, it would be extremely surprising for a director to be deemed to have failed in his duties of diligence and prudence if he were to demonstrate that he had relied on the report of an expert, or on financial statements presented as accurate, in making a decision. He would in fact have fulfilled his duty by seeking information before acting.[3691]

[3414] According to M[e] Paul Martel, directors are not attributed a duty of control over the officers of the company as such; it is only when they have reason for suspicion that they

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[3688] S.N.B. 1981, c. B-9.1
[3689] R.S.O. 1990, c. B.16, s.134, 135
[3690] S.Q. 1980, c. 28, s. 14
[3691] Paul Martel, "*The Duties of Care, Diligence and Skill Owned by Directors of Federal Business Corporations – Impact of the Civil Code of Quebec*" (2007-2008) 42 R.J.T. 233-305 at 184

are asked to investigate and, where appropriate, to intervene.[3692] If they do not do so, they are then committing an error. In *Blair v. Consolidated Enfield Corp.*,[3693] the Supreme Court of Canada reiterated the principle that directors are justified in trusting the work of a corporation's representatives.[3694]

Application of rules to facts

[3415] Defendants' negligence was the cause of Widdrington's damages because the Court finds that:

- Widdrington would not have invested in Castor without having reviewed satisfying audited financial statements and unqualified audit reports.
- Widdrington did not know that Castor's true financial position was materially different than that which C&L disclosed in their professional opinions and there is no reason for such knowledge to be imputed to Widdrington.
- Had C&L complied with GAAP and GAAS, audited financial statements, unqualified audit reports, valuation letters and Certificate for legal for Life Opinion would never have been issued showing anything close to those in litigation.
- Had the audited financial statements and valuation letters revealed the financial situation of Castor, including proper disclosure of Castor's financial position as they should have, Widdrington would not have invested and therefore would not have suffered a loss, even if there had been a "*stampede effect*".

[3416] Defendants had the burden to prove that Plaintiff would have lost his investments even without their fault.[3695] They did not discharge said burden.

[3417] In *Hodgkinson v. Simms*,[3696] in the context of an action for breach of fiduciary duty and under common law rules, the Supreme Court of Canada stated the following:

> «[76] What is more, the submission runs up against the long-standing equitable principle that where the plaintiff has made out a case of non-disclosure and the loss occasioned thereby is established, **the onus is on the defendant to prove that the innocent victim would have suffered the same loss regardless of**

[3692] Paul Martel, "The Duties of Care, Diligence and Skill Owned by Directors of Federal Business Corporations – Impact of the Civil Code of Quebec" (2007-2008) 42 R.J.T. 233-305 at 154
[3693] [1995] 4 S.C.R. 5, affirmed (1993), 106 D.L.R. (4th) 193 (Ont. C.A.)
[3694] *Blair v. Consolidated Enfield Corp.*, [1995] 4 S.C.R. 5 at para. LXIX
[3695] See, for example *Bussières* c. *Compagnie d'assurance Jevco,* [2002] CanLII 24454 (QC C.A.) at paras 9-10; See also *Montpetit v. Léger,* [2002] AZ-00021982 (C.S).
[3696] *Hodgkinson v. Simms,* [1994] 3 S.C.R. 377 (SCC), at para. 72 and 92, AZ-94111096, J.E. 94-1560

> **the breach**; see [references omitted]. This Court recently affirmed the same principle with respect to damages at common law in the context of negligent misrepresentation; see [references omitted]. I will return to the common law cases in greater detail later; it suffices now to say that courts exercising both common law and equitable jurisdiction have approached this issue in the same manner. [...]
>
> [92] From a policy perspective it is simply unjust to place the risk of market fluctuations on a plaintiff who would not have entered into a given transaction but for the defendant's wrongful conduct. (our emphasis)

[3418] Even though they were made in a common law context, these remarks also apply in the Quebec civil context.

[3419] Defendants submitted the following: "*Widdrington is thus in the exact position described by Baudouin and Deslauriers*[3697] *and by the Court of Appeal in Savard*[3698]*: he invested in Castor allegedly on the basis of an audit report prepared for others and for a different purpose. (...) The same reasoning is applicable to the valuation letters and the legal-for-life certificates".* The Court disagrees with that proposition.

[3420] Based on the evidence, the Court finds that Widdrington invested in Castor on the basis of audit reports, valuation letters and Certificate for Legal for Life Opinion that C&L prepared namely for investment purposes, knowing that such opinions were used and would be used for investment purposes and agreeing that it be the case.

[3421] Defendants imply that because of the content of Castor Shareholders' Agreement, Widdrington was prevented from mitigating his damages. The Court rejects that proposition.

- Widdrington's investments in Castor, both in 1989 and 1991, were made primarily on the faith of the accuracy and truth of the financial position of Castor, as reflected in the unqualified audited financial statements over the years as well as the correctness of C&L's opinion as to the fair market value of Castor's shares, as set out in the share valuation letters.

- Had the audited financial statements not been misstated, and had C&L's opinion as the fair market value of Castor's shares been correct, no provisions in the Shareholders' Agreement would have precluded Widdrington from disposing of his shares in Castor, pursuant to its terms. As the evidence shows, many shareholders did over the years.

[3697] Jean-Louis Baudouin and Patrice Des Lauriers, *La responsabilité civile*, vol. II – responsabilité professionnelle, 7th ed., (Cowansville, Qc: Yvon Blais, 2007 paras.2-182 to 2-190

[3698] *Savard c. 2329-1297 Quebec inc.* [2005] RJ.Q. 1997 (C.A.) EYB 2005-93444 (motion for permission to appeal at the Supreme Court of Canada dismissed)

[3422] Defendants point to Widdrington's position as a director of Trinity, and suggest that, in that capacity, he should have been put on notice of Castor's undisclosed transactions with related parties and the non-performance of Castor's loan portfolio.

[3423] Defendants also suggest that insofar as Widdrington knew that the loans extended by Castor to Trinity were "bad loans", he must have known that there might be other bad loans in the Castor portfolio which were not reported in Castor's financial statements.

[3424] While Widdrington acknowledged that by the Board meeting of June 26, 1990 he was aware that Trinity was not doing well financially,[3699] this does not mean that he ever considered Trinity to be a bad loan. On the contrary, Widdrington testified that he was not so much concerned about the financial aspects of Trinity but rather the operational aspects of the company.[3700] He believed that if there were any concerns about the quality of this loan, if this was an issue, it would have been discussed with the auditors of Castor, and if it was a "bad loan", there would have been a bad loan provision. At the time, in May 1990, to put matters into perspective, Castor had assets of approximately $1.6 billion.[3701]

[3425] It is true to say that from the beginning of his involvement in Trinity, Widdrington consistently voiced his concern that the company was getting involved into too many businesses and in businesses that it should not have been in. However, to put matters into perspective again, one needs to add that, at all relevant times, Widdrington believed Trinity could be righted reasonably quickly.[3702]

[3426] Castor's Board included international and experienced directors with diverse talents.[3703] Widdrington regarded this as an opportunity for him to make a positive contribution in the future.[3704] Prikopa described the way a director acquires his knowledge as a learning process.[3705] Jarislowsky explained that it is a common situation that the directors who compose the board of any given company have different and complementary strengths, and that it is normal for directors to lean on each other according to their respective specialties.[3706]

[3427] Widdrington explained that the role of a director in general, and his role as director of Castor in particular, consisted in ensuring that the company had direction, a game plan, and the right people in place to carry it forward, and that this did not require directors to know a great deal about the specifics of the business.[3707] He testified that

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[3699] Widdrington, December 15, 2004
[3700] Widdrington, December 15, 2004
[3701] Widdrington, December 15, 2004
[3702] Widdrington, December 15, 2004
[3703] PW-43-1.
[3704] Widdrington, November 30, 2004
[3705] Prikopa, January 17, 2005
[3706] Jarislowsky, April 5, 2005
[3707] Widdrington, November 30, 2004

he did not view his role as director as requiring him to examine the nuts and bolts of the business. It was up to the auditors to examine the financial details, and the auditors would bring any areas of concern to the attention of the directors.[3708]

[3428] Through their argument, Defendants are imposing a heavier burden on Widdrington than upon themselves as auditors. If fact, what they are suggesting is that Widdrington should have questioned and verified the audit work performed by C&L, supported by C&L's unqualified audit opinion. The Court cannot accept such a proposition.

[3429] Plaintiff committed no fault, either in the exercise of his duties as a director of Castor, or in the due diligence exercised by him prior to making his respective investments in Castor.

[3430] It was Defendants' burden to prove a fault on the part of Plaintiff, which was the logical, direct and immediate cause of damages suffered by him, a burden which Defendants have failed to satisfy. Contributory negligence applies when the Court finds that two faults have caused the damage.[3709] This is not the case here.

[3431] Defendants are liable and shall be condemned to indemnify the Plaintiff for the damages he has sustained.

[3708] Widdrington, December 1, 2004

[3709] See, for example *Business Development Bank of Canada c. Pfeiffer,* [2009] QCCS 2310 (CanLII), at para. 93.

Common law

[3432] As previously said, the Quebec civil law rules apply to this litigation and therefore, to decide the merits of the case, it is not necessary to discuss the content and the application of the common law rules.

[3433] In the unique and special circumstances of the Castor file however, and given the enormous resources that have been dedicated to this litigation, financial and others, the Court feels that it is her duty nevertheless to summarize the evidence adduced before her on that topic and to communicate what her findings would have been had she concluded that she had to apply the common law rules – the Court feels she owes it to the parties, to counsel, to the judicial community at large and to the judicial system.

Judicial notice

[3434] Under article 2809 of the Civil code of Québec, and provided it has been pleaded, the Court may take judicial notice of the law of Ontario and New Brunswick. Proof of such law by expert evidence is also allowed.

> **2809.** Judicial notice may be taken of the law of other provinces or territories of Canada and of that of a foreign state, provided it has been pleaded. The court may also require that proof be made of such law; this may be done, among other means, by expert testimony or by the production of a certificate drawn up by a jurisconsult.
>
> Where such law has not been pleaded or its content has not been established, the court applies the law in force in Québec.

[3435] The law of other provinces of Canada, New Brunswick or Ontario, is pleaded since the Defendants asserted that the case had to be decided on the basis of the common law principles, according to the Quebec conflict of law rules, in their re-amended defense of 1998.

[3436] Defendants and Plaintiff have elected to present expert evidence on the principles at common law: Defendants have called John Campion ("**Campion**") and Plaintiff has called Earl A. Cherniak ("**Cherniak**"). Both submitted written reports in advance[3710] and testified *viva voce* before the Court[3711].

[3710] Reports of Cherniak : PW-3099 and PW-3099A ; Reports of Campion : D-660 and D-660-1

[3711] Cherniak, February 24, 2010; Campion, August 31, 2009 and September 1, 2009

Expert evidence

Who's who

Campion

[3437] Campion received his Bachelor of Arts degree from the University of Western Ontario in 1967 and his law degree from the University of Toronto Law School in 1972[3712].

[3438] Campion articled at the law firm then known as Fasken Calvin, now known as Fasken Martineau. In 1974, he was called to the Bar of Ontario and to the Bar of the Northwest Territories, of which he has been a member since[3713].

[3439] Campion became a partner at Fasken Martineau, the legal firm where he worked his entire career, always as a litigator, and where he was still practicing when he testified before this Court.

[3440] Throughout his career, Campion has been involved in commercial litigation, including many professional liability cases.

[3441] With Dianna Dimmer, Campion is the co-author of *Professional Liability in Canada* published at Carswell, a treaty on professional liability, which includes a chapter on auditors' liability[3714].

[3442] From 1995 to 2001, Campion was a member of the board, and head of the audit committee of the Canadian Broadcasting Corporation.

[3443] In the late 90s, Campion acted as an expert before the Senate of Canada Banking Committee dealing with auditors' liability.

[3444] Campion wrote articles and lectured at professional meetings on negligent misrepresentation and the analysis of the principles attached thereto.

Cherniak

[3445] Cherniak received his Bachelor of Arts degree from the University of Western Ontario and his law degree from Osgoode Hall Law School.

[3712] D-660-1A (curriculum vitae)
[3713] Campion, August 31, 2009, p.23
[3714] D-660-3

[3446] In law school, Cherniak received the gold medal in his final year, and had honours in all years.

[3447] In 1960, Cherniak was called to the Bar of Ontario, of which he has been a member since.[3715]

[3448] In the mid 60s, Cherniak became a partner at Lerners LLP, a legal firm where he worked his entire career, always as a litigator, and where he was still practicing when he testified before this Court.

[3449] Cherniak has been involved in cases involving professional negligence his entire career.

- He handled numerous medical negligence cases, doing a lot of work for plaintiffs in that field in the early days of his career.

- He handled professional liability cases for or against lawyers, sometimes defending lawyers and sometimes suing lawyers or law firms.

- With respect to accountant professional liability cases, he acted in two principal cases – one case involving KPMG that was settled just before trial, where he acted for KPMG, and a second case, a class action against professionals of multiple disciplines (namely lawyers and accountants) including Deloitte, where he acted for the Plaintiff and where a settlement for 85 million dollars was reached further to a three week settlement conference presided by Justice Winkler of the Ontario Superior Court. He never had an auditor's negligence case at trial[3716].

[3450] Cherniak has appeared in several hundred cases before the Ontario Court of Appeal and approximately 35 to 40 times before the Supreme Court of Canada, without taking account of leave applications[3717].

[3451] Cherniak has written over a hundred papers on a variety of topics, namely:

- "*Policy and Predictability Pure Economic Loss in the Supreme Court of Canada*"

- "*Two Steps Forward or One Step Back: Ends of the Crossroads in Canada*", a paper cited twice by the Supreme Court of Canada in the Hercules decision.

[3452] Since 1982, Cherniak is a Fellow of the American College of Trial Lawyers.

[3715] PW-3098 (curriculum vitae)
[3716] Cherniak, February 24, 2010, p. 29
[3717] Cherniak, February 24, 2010, p. 21

[3453] Since 2006, he is a Fellow of the Chartered Institute of Arbitrators.

[3454] Between 1961 and 1979, Cherniak taught at the University of Western Ontario Law School.

[3455] Cherniak was elected a bencher of the Law Society of Upper Canada and sat on the governing body of the Law Society for eight years, from 1999 to 2007. During those years, Cherniak acted as chair and vice-chair of the proceedings authorization committee, a committee involved in the discipline process of the members of the Law Society.

Experts' opinions

Campion

[3456] At common law, Campion opined that a plaintiff needs to establish five general requirements for a misrepresentation claim to be successful[3718] :

- There must be a duty of care based on a "special relationship" between the plaintiff and the defendant.
- The representation must be untrue, inaccurate, or misleading.
- The defendant must have acted negligently in making said misrepresentation.
- The plaintiff must have relied, in a reasonable manner, on said negligent misrepresentation.
- The reliance must have been detrimental to the plaintiff in the sense that damages resulted.

[3457] Campion opined that, for the purposes of auditor's liability cases, the first requirement "*the duty of care based on a "special relationship" between the plaintiff and the defendant*" has been canvassed by the Supreme Court of Canada in the Hercules case, based on the two steps of the commonly known "*Anns test*"[3719]. He added that, since 1997, such canvass was repeatedly used by the Ontario courts in deciding misrepresentation claim cases.[3720]

[3718] *Queen v. Cognos*, [1993], 1, S.C.R., 87, at p. 110, AZ-93111008, J.E. 93-270, D.T.E. 93T-198

[3719] *Anns v. Merton London Borough Council*, [1978], A.C.728; *Kamloops (City) v. Nielsen*, [1984], 2 S.C.R. 2, AZ-84111034, J.E. 84-603

[3720] *Waxman V. Waxman* [2004], 44 B.L.R. (3d) 166, at pages 308-311 (Ont. C.A.); *D'Amore Construction (Windsor) Ltd. v. Lawyer's Professional Indemnity Co.* [2005], 249 D.L.R. (4th) 467, at page 474 (Ont. Div. Ct.): *Windsor Equities Ltd. v. Sentinel Hill Sales Corp.*, [2005] O.J. No. 1516 (S.C.J.) at paragraph 16; *Ontario Public Service Employees Union v. Ontario,* [2005], 13 C.P.C. (6th) 178, at

[3458] In most auditors' negligence cases, said Campion, concern over indeterminate liability under the second component of the *Anns test* would serve to negate the *prima facie* duty of care. Such duty of care would only survive in exceptional cases where the concerns about indeterminate liability would not arise.

[3459] To determine in any given case whether such exceptional circumstances existed, Campion suggested a court would have regard to whether the defendant auditor had specific knowledge of the plaintiff, or a narrow class of plaintiffs, and to whether the auditor work product had been used for the specific purpose or transaction for which it had been prepared. If both criteria were to be satisfied, Campion opined that the potential liability could not be regarded as indeterminate. In such a case, he concluded the duty of care would not be negated[3721].

[3460] Campion further opined that, of necessity, a "class of plaintiffs" had to be a narrow class or a limited one[3722]. He suggested that it could not be all shareholders or all lenders of a company.[3723] He added that in an auditor's negligence claim, the notion of a "limited class" did not turn on the number of members within the class but depended rather on whether the members were known to the defendant and had used the auditor work product for the specific purpose(s) for which it had been produced.[3724]

[3461] Campion wrote that the second requirement "*the representation must be untrue, inaccurate or misleading*" was largely a question of fact, which in most cases did not raise any significant legal issues.[3725]

[3462] To satisfy the third requirement, "*the defendant must have acted negligently in making said misrepresentation*", Campion said the plaintiff had not only to establish that the representation was untrue but also that the untruth was the result of a lack of reasonable care and skill which other competent auditors would have exercised in identical circumstances.[3726]

[3463] Campion opined that, at common law, the standard practices of a profession- namely GAAP and GAAS in the case of auditors- were entitled to very deferential

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pages 186-188 (Ont.S.C.J.); *Mantella v. Mantella* [2006], 267 D.L.R. (4th) 532, at pages 544-545 (Ont. S.C.J.); *Murphy v. BDO Dunwoody LLP* [2006], 32 C.P.C. (6th) 358, at pages 362-363 (Ont.S.C.J.); *Dood v. RBC Dominion Securities Inc.* [2006] O.J. No. 4259 (S.C.J.) at paragraphs 22-22; *1597203 Ontario Ltd. v. Ontario* , [2007] O.J. No. 2349 (S.C.J.) at paragraph 74; and *McCarthy Corporation PLC v. KPMG LLP*, [2007] O.J. No.32 (S.C.J.) at paragraphs 53-55

[3721] D-660, at paragraphs 13-14

[3722] *RoyNat inc. v. Dunwoody & Co.* [1993], 18 C.C.L.T. (2d) 43 (B.C.S.C.) at paragraph 22; *Haig v. Bamford*, [1977] 1 S.C.R. 466, AZ-77111040

[3723] D-660 (additional report), at paragraph 11

[3724] D-660 additional report, at paragraph 15

[3725] D-660, at paragraph 6

[3726] D-660, at paragraph 17; *Guardian Insurance Co. v. Sharp*, [1941] 2 D.L.R. 417 at 430 (S.C.C.); *Re Kingston Cotton Mill Company (no.2)*, [1896] 2 Ch. 279 at pages 288-290 (C.A.); *Re London & General Bank (no.2)*, [1894] 2 Ch. 673 at page 683 (C.A.)

treatment by the courts so that, save in exceptional circumstances where the standard practice was obviously deficient, a professional who had acted in conformity with the standards of his profession would not be found negligent. On that topic, Campion referred to the reasons written by Justice Sopinka in the Supreme Court unanimous decision *Ter Neuzen v. Korn.*[3727]

[3464] On the fourth requirement, "*the plaintiff must have relied, in a reasonable manner, on said negligent misrepresentation*", Campion opined that the weight of authority supported the view that reliance might be inferred from circumstantial evidence. He cited two cases into which the following had been affirmed: "*the question of reliance is a question of fact to be inferred from all of the circumstances of the case and all of the evidence adduced at trial*".[3728]

[3465] Campion wrote "*The courts are encouraged to be sceptical of claims of reliance upon a misrepresentation based upon the existence of a loss which has been sustained*". However, in his cross-examination, he acknowledged that he had no authorities to support the "*encouragement to be sceptical*" element of his proposition.[3729] Finally, Campion admitted that the burden of proof of the reliance element of a misrepresentation claim was exactly the same as that of other elements, the cross-examination on his "*sceptical proposition*" ending on the following question and answer:

> Q. - The point is I suggest to you the burden of proof or reliance is the same as negligence, the same as damages, the same as any other element of the claim; correct?
>
> A- It is.[3730]

[3466] On the fifth requirement, "*the reliance must have been detrimental to the plaintiff in the sense that damages resulted*", Campion opined that the basic principle animating the assessment of damages in tort was that a plaintiff was to be put in the position that it would have been in if the wrong had not been committed.[3731] Assuming a judge was to conclude there had been a negligent misrepresentation but not an intentional wrongful conduct (like fraudulent misrepresentation), he added that only the reasonably foreseeable losses could be recovered.[3732] Finally, he opined that there might be contributory negligence, in which case apportionment of liability was expressly provided for in the Negligence Act.[3733]

[3727] [1995], 3 S.C.R. 674, at page 701
[3728] *L.K. oil & Gas Ltd. v. Canalands Energy Corp.* (1989), 60 D.L.R. (4th) 490, at page 500 (Alta C.A.); *TWT Enterprises Ltd. v. Westgreen Developments (North) Ltd.*, [1992] 5 W.W.R. 341 (Alta. C.A.)
[3729] Campion, September 1, 2009, pp.34-41
[3730] Campion, September 1, 2009, p.41
[3731] *Rainbow Industrial Caterers Ltd. v. Canadian National Railway Co.* [1991] 84 D.L.R. (4th) 291 (S.C.C.)
[3732] *B.G. Checo International Ltd. v. British Columbia Hydro and Power Authority* [1993], 99 D.L.R. (4th) 577, at pages 593-594 (S.C.C.)
[3733] R.S.O. 1990, c. N.1, s.3

[3467] During his cross-examination, Campion was asked to comment on the two following extracts of paragraph 32 of the Hercules decision[3734]:

> **Extract # 1 relating to foreseeability of reliance**
>
> In modern commercial society, the fact that audit reports will be relied on by many different people (e.g., shareholders, creditors, potential takeover bidders, investors, etc.) for a wide variety of purposes will almost always be reasonably foreseeable to auditors themselves. (...)
>
> **Extract # 2 relating to ascertaining a prima facie duty of care**
>
> In light of these considerations, the reasonable foreseeability/reasonable reliance test for ascertaining a prima facie duty of care may well be satisfied in many (even if not all) negligent misstatement suits against auditors and, consequently, the problem of indeterminate liability will often arise.

[3468] About extract # 1, commenting on the proposition that in our modern society it would always be reasonably foreseeable to auditors that a variety of people would rely on their work, Campion said the proposition was rather a factual conclusion than a legal proposition:

> I can tell you what the law of Ontario and Canada in a common law jurisdiction is and this comment forms part of Justice La Forest's opinion and review, but I cannot say authoritatively that I have the expertise to agree with the proposition. I can simply say, "That's what the court said", and it's on that basis he went on then to make his analysis and that is not so much a legal as a factual conclusion. And I don't know what evidence was before the court to assist it in making that decision.
>
> So for me to agree with the proposition, which is a not so much a legal one but a factual one, based possibly on findings of evidence in the court, I can't give you an authoritative opinion one way or the other.
>
> it's a factual conclusion as opposed to something which forms part of the law. And it is a factual conclusion which the court found favour with when coming to its conclusions. I do not believe that it is a legal conclusion itself and therefore I cannot say that it forms part of the law of Ontario. You cannot go into any particular case and say, "That is a given conclusion which would be binding", because someone may lead evidence to the contrary and I simply... I'm not in a position as coming here to give expert testimonial on the law to give you an answer. In fact, I would say that since it is a finding of fact which could be debated in other ways in other evidence, in other cases, it is not something that would be binding as a matter of law.[3735].

[3734] [1997] 2 S.C.R. 165

[3735] Campion, September 1, 2009, pp.29-31

[3469] About extract # 2, commenting on the proposition that the reasonable foreseeability/reasonable reliance test for ascertaining a *prima facie* duty of care may well be satisfied in many, even if not all, negligent misstatement suits against auditors, Campion said he believed, again, it was an observation rather than the expression of a principle of law:

> I do not believe it is a legal conclusion in whole; it is in part. Based on the legal principles that it is not... It's a mixed question of fact and law and the application of it. So take the... in light of these considerations, the reasonable foreseeability and reliance tests may well be satisfied.
>
> The court is making an observation either upon its own understanding or on evidence which have been led, details which I have not read. And so he... the Court is not giving one and absolute finding in any event, but even assuming that the parenthetical even if not all negligent misstatement suits against auditors it leaves open the possibility that somebody with different evidence or with a different perspective may not agree.[3736]

[3470] Summing up on both extracts, Campion concluded:

> I will give you this far though with respect of both of these comments. They set a framework that would cause anybody who wish to disagree with it to lead evidence to the contrary. I assume without knowing that the judge is making comment without evidence and it has a ring and aura of practical application of general knowledge that the judge is apparently applying and understanding. And if I were going to disagree with it as a manner of law in Ontario, I would have to persuade a court through evidence one way or the other whether these were accurate or not. But they are comments around which... because Hercules is such a significant case for the purposes of auditor liability one would give great care and concern to the statements if you were going to prove that they were not so.[3737]

[3471] During his cross-examination, Campion agreed that it was fair to say that auditors could agree that their audited financial statements be used for other purposes than the statutory audit purpose, before rendering their audit opinion or after rendering their audit opinion. In some exceptional circumstances, which obviously would have to be proved, he acknowledged a plaintiff could show that his case was falling under the exception mentioned by Justice La Forest at paragraph 36 of the Hercules case.[3738]

> 36 As I have thus far attempted to demonstrate, the possible repercussions of exposing auditors to indeterminate liability are significant. In applying the two-stage Anns/Kamloops test to negligent misrepresentation actions against auditors, therefore, policy considerations reflecting those repercussions should be taken into account. **In the general run of auditors' cases, concerns over**

[3736] Campion, September 1, 2009, p.31-32
[3737] Campion, September 1, 2009, pp.33-34
[3738] Campion, September 1, 2009, pp.53-54

> **indeterminate liability will serve to negate a prima facie duty of care**. But while such concerns may exist in most such cases, there may be particular situations where they do not. In other words, **the specific factual matrix of a given case may render it an "exception" to the general class of cases** in that while (as in most auditors' liability cases) considerations of proximity under the first branch of the Anns/Kamloops test might militate in favour of finding that a duty of care inheres, the typical concerns surrounding indeterminate liability do not arise.[3739] (our emphasis)

[3472] Finally, Campion opined a plaintiff could have a cause of action against an auditor, at common law, provided such a plaintiff discharged his burden of proof to establish the five requirements of his negligent misrepresentation claim.[3740]

Cherniak

[3473] Cherniak, who testified after Campion and who had the opportunity to read Campion's testimony in advance[3741], confirmed that he had no disagreement with Campion's testimony on the following subjects:

- The sources of the common law.
- The general description of the development of the Canadian common law with respect to economic loss or negligent misstatement.
- The five requirements under the case *Queen vs. Cognos Inc.* in a misrepresentation claim.

[3474] Cherniak said that the principal issue was the issue of indeterminacy in relation to the duty of care requirement.

[3475] He recognized that this issue was often stated in the words of Justice Cardozo in the *Ultramares* case[3742], where the latter warned against liability being held for an indeterminate amount, to an indeterminate class and for an indeterminate period of time, but he disagreed with the following assertion of Campion: "*The plaintiff's reliance must be the end and aim of the transaction in which the statement was made, the proximity must be so close as to approach that of "contractual privity"*".[3743]

[3476] Cherniak opined that it is not necessary that a plaintiff's reliance be the "*end and aim of the transaction*". He said it is only necessary to have used the work product for the same purpose for which it was prepared or if the work product was prepared for

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[3739] [1997] 2 S.C.R. 165
[3740] Campion, September 1, 2009, pp. 61-66 and PW-3064
[3741] Cherniak, February 24, 2010, p.35
[3742] *Ultramares Corp, v, Touche* [1931], 255 N.Y. 170, 174 N.E. 441, 74 A.I.R. 1139 (U.S. N.Y. Ct. App.)
[3743] Cherniak, February 24, 2010, p. 40-41

several purposes, for one of those purposes. Cherniak added that there was nothing in jurisprudence to support that a plaintiff's reliance must be the "*end and aim of the transaction*".[3744]

[3477] Cherniak affirmed that if the sentence "*The proximity must be so close as to approach that of "contractual privity*", was the law of the United States, it was surely not with the law of Canada. Cherniak said the same applied to the *Glanzer* case[3745] of the 1920s (United States case also).

[3478] Cherniak testified that two criteria had to be analysed at the first stage of the Anns' test: reasonable foreseeability and proximity.

[3479] To establish a duty of care at common law, he explained that the following three elements had to be shown:

- The plaintiff is complaining of a harm that was reasonably foreseeable.
- The relationship of the plaintiff with the defendant is of sufficient proximity such that it is just and fair to hold the defendant subject to a duty of care.
- There are no residual policy reasons, concerned with the effect of recognizing a duty of care on other legal obligations, the legal system and the society more generally, for declining to impose such a duty.

[3480] Under the law of Ontario, at common law, he said a duty of care may lie on the part of an auditor where the plaintiff was known to the auditor (or the class of such plaintiffs was known to the auditor) and where the auditor's statement was used for the purpose for which it was made, those circumstances being questions of fact in any given case.

[3481] He cited cases from Ontario post Hercules, where the courts found a duty of care between auditors and plaintiffs where there was no contractual relationship or where the courts recognized that possibility[3746].

[3482] He opined that the purpose (or purposes) of the auditor work product(s) was the key element in the determination of an auditor's duty of care and that the identification of any such purpose was a question of fact in any given case. He wrote:

> In my opinion, **a court in Ontario** considering the purpose of audit reports and audited financial statements **will always consider the factual matrix of the case to determine what purpose or purposes were intended for** the audit

[3744] Cherniak, February 24, 2010, pp.40-42
[3745] Cherniak, February 24, 2010, p. 43
[3746] *McKenzie Financial Corp. V. McRae* [1998], 81 O.T.C. 321 (Gen. Div.); *Canadian Imperial Bank of Commerce v. Deloitte & Touche* [2003] Carswell Ont 1814; *CC&L Dedicated Enterprise Fund (Trustee of) v.Fisherman* [2001] 18 B.L.R. (3d),260 (Ont.S.C.J.)

> reports and the financial statements. The answer to that factual question, in turn, will affect the determination of the duty of care.[3747] (our emphasis)

[3483] Cherniak wrote "*whether it is reasonable to rely on audit reports or audited financial statements is a different question than whether such reports or statements can give rise to liability. The first is a factual question that, in my opinion, Ontario courts would answer by having regard to the commercial context of the case. The second is a question of law that requires applying legal standards to the facts as found*"[3748]. The Court agrees.

Analysis

[3484] If she had come to the conclusion that the common law rules applied to this litigation, the Court would have reviewed the evidence, and Widdrington's claim, through the five requirements applicable to a misrepresentation claim, as described by Campion and agreed to by Cherniak.

[3485] Having said earlier that she would have come to the same conclusion as the one she has reached under the Civil Code of Québec, and to explain summarily such a conclusion, the Court now sums up her analysis through these five requirements.

First requirement –the duty of care

[3486] As the Supreme Court wrote in *Hercules Managements Ltd. v. Ernst & Young ("***Hercules***"),*[3749] the existence of a duty of care in tort is to be determined through an application of the two-part test enunciated in *Anns v. Merton London Borough Council*[3750]*, [1978] A.C. 728 (H.L.), at pp. 751-52:*

> **First** one has to ask whether, as between the alleged wrongdoer and the person who has suffered damage there is a sufficient relationship of proximity or neighbourhood such that, in the reasonable contemplation of the former, carelessness on his part may be likely to cause damage to the latter -- in which case a prima facie duty of care arises. **Secondly**, if the first question is answered affirmatively, it is necessary to consider whether there are any considerations which ought to negative, or to reduce or limit the scope of the duty or the class of person to whom it is owed or the damages to which a breach of it may give rise[3751]. (our emphasis)

[3747] PW-3099A, at paragraph 32
[3748] PW-3099A, at paragraph 35
[3749] [1997] 2 S.C.R. 165
[3750] [1978] A.C. 728 (H.L.), at pp. 751-52
[3751] [1997] 2 S.C.R. 165, paragraph 19

[3487] This basic approach has repeatedly been accepted and endorsed by the Supreme Court of Canada[3752]. In his 2007 report, Cherniak opines that the reformulation of the test into three parts from two did not change the test in its substance[3753]. Campion shares this conclusion, and the Court agrees.

First part of the test : relationship of proximity

[3488] The first part of the test demands an inquiry into the relationship between Widdrington and C&L - In the reasonable contemplation of C&L, could carelessness on their part cause damage to Widdrington?

[3489] The Court has to investigate whether C&L and Widdrington can be said to be in a relationship of proximity or neighbourhood.

[3490] As Justice La Forest said in Hercules, writing for the Court: "*the term "proximity" itself is nothing more than a label expressing a result, judgment or conclusion; it does not, in and of itself, provide a principled basis on which to make a legal determination*"[3754].

[3491] A relation of proximity or neighbourhood exists if the circumstances of the relationship between a plaintiff and a defendant are of such a nature that the defendant may be said to be under an obligation to be mindful of the plaintiff's legitimate interests in conducting his or her affairs. There is a relation of proximity or neighbourhood when two criteria relating to reliance may be said to exist on the facts:

- the defendant ought reasonably to foresee that the plaintiff will rely on his or her representation; and
- reliance by the plaintiff would, in the particular circumstances of the case, be reasonable.

[3492] "*In modern commercial society, the fact that audit reports will be relied on by many different people (e.g., shareholders, creditors, potential takeover bidders, investors, etc.) for a wide variety of purposes will almost always be reasonably foreseeable to auditors themselves*", as Justice La Forest wrote in Hercules.[3755]

[3752] *Kamloops (City of) v. Nielsen*, [1984] 2 S.C.R. 2; *B.D.C. Ltd. v. Hofstrand Farms Ltd.*, [1986] 1 S.C.R. 228; *Canadian National Railway Co. v. Norsk Pacific Steamship Co.*, [1992] 1 S.C.R. 1021; *London Drugs Ltd. v. Kuehne & Nagel International Ltd.*, [1992] 3 S.C.R. 299; *Winnipeg Condominium Corporation No. 36 v. Bird Construction Co.*, [1995] 1 S.C.R. 85.

[3753] PW-3099A, at paragraph 18

[3754] [1997] 2 S.C.R. 165, at paragraph 23

[3755] [1997] 2 S.C.R. 165, at paragraph 32

[3493] Above and beyond this remark of Justice La Forest, and to determine what is or is not foreseeable in any given situation, the facts of the case are highly relevant.[3756]

[3494] In this case, and through their audit partner Wightman, C&L had knowledge of Castor's business and of the limited "investment club group of persons" that interacted with Castor.

[3495] In this case, and as explained under the heading "independence" of the present judgment, Wightman was a promoter of Castor's affairs.

[3496] In this case, and as the Court previously enunciated, the purposes of C&L's work products were multiple.

[3497] The audits of Castor performed by C&L had more than one purpose. Above and beyond any statutory audit requirements, in doing their annual audit of Castor, C&L were pursuing the following tasks:

- To produce a tool that would be relied upon to assess the fair market value of Castor's shares and to issue valuation letters serving to attract and convince new investors to join the "investment club" of Castor or to retain the actual members of said "investment club".

- To produce a tool to be relied upon for the issuance of an annual Certificate for Legal for Life Opinion and to attract investors and to convince investors of Castor's creditworthiness.

[3498] The issuance of the valuation letters also had more than one purpose. Even though those letters might have had some connection with the shareholders' agreement, they were primarily issued as a professional opinion on the fair market value of Castor's shares for treasury issuance purposes, to be used by those who were approached to invest in Castor's shares.

[3499] One of the objectives pursued through the issuance of Legal for Life Opinions, as mentioned by Simon during his testimony, was to establish Castor's creditworthiness in the eyes of the potential investors.

[3500] In those circumstances, C&L ought reasonably to have foreseen reliance by third parties on their opinions and representations (audit reports, valuation letters and Certificates for Legal for Life Opinion).

[3501] In fact, Widdrington reasonably relied on C&L's work products (audit reports, consolidated audited financial statements, valuation letters and Certificates for Legal for Life Opinions) as the Court explained earlier in the present judgment, under the heading "reliance".

[3756] [1997] 2 S.C.R. 165, at para graph 28

[3502] There is no doubt that a relation of proximity or neighbourhood existed between Widdrington and C&L.

Second part of the test : policy considerations

[3503] In the second part of the test, the Court has to ask herself whether, in the particular circumstances of this case, there are considerations which ought to negate or limit the scope of C&L's duty of care and the class of persons to whom it is owed or the damages to which a breach of such duty may give rise.

[3504] The fundamental policy consideration that must be addressed centres around the possibility that C&L might be exposed to "*liability in an indeterminate amount for an indeterminate time to an indeterminate class*". Concerns over indeterminate liability generally serve to negate a *prima facie* duty of care in auditors' liability cases.

[3505] An important case, cited by both experts, is *CC & L Dedicated Enterprise Fund (Trustee of) v. Fisherman*[3757], in which a class action was authorized based on a finding that a duty of care was owed by the auditors not only to the investors who initially purchased shares in the initial public offering, but also to the secondary-market purchasers for whom reliance was also reasonably foreseeable to Defendants. As Campion agreed, this case shows that a potential class of plaintiffs cannot be considered indeterminate simply because it is large.[3758] In that case, even though the class of plaintiff was large and comprised members not specifically known to the defendants, the class was nonetheless sufficiently delimited because the auditors knew this group would rely on their opinions.

[3506] Justice La Forest mentioned in the Hercules decision, *"while such concerns may exist in most such cases, there may be particular situations where they do not. In other words, **the specific factual matrix of a given case** may render it an "exception" to the general class of cases in that while (as in most auditors' liability cases) considerations of proximity under the first branch of the Anns/Kamloops test might militate in favour of finding that a duty of care inheres, the typical concerns surrounding indeterminate liability do not arise"*[3759] (our emphasis).

[3507] On the facts of the Hercules case, Justice La Forest:

- Described the purpose as "*precisely, to assist the collectivity of shareholders of the audited companies in their task of overseeing management*"[3760]

[3757] [2001] 18 B.L.R. (3d) Ont. S.C.J. (Mondor)
[3758] D-660A, paragraph 13
[3759] [1997] 2 S.C.R. 165, at paragraph 36
[3760] [1997] 2 S.C.R. 165, at paragraphs 49 and 53

- Rejected the submission that, in addition to the statutorily mandated purpose, the audits had been prepared for the purpose of providing the appellants with information on the basis of which they could make personal investment decisions[3761].

- Assessed that, in fact, the audit reports had not been prepared in order to assist the appellants in making personal investment decisions or, indeed, for any purpose other than the standard statutory one[3762].

- Established that it followed "*that the only purpose for which the 1980-82 reports could have been used in such a manner as to give rise to a duty of care on the part of the respondents is as a guide for the shareholders, as a group, in supervising or overseeing management*"[3763].

- And concluded that "*even though the respondents owed the appellants (qua individual claimants) a prima facie duty of care both with respect to the 1982-83 investments made in NGA and NGH by Hercules and Mr. Freed and with respect to the losses they incurred through the devaluation of their existing shareholdings, such prima facie duties are negated by policy considerations which are* ***not obviated by the facts of the case***"[3764] (our emphasis).

[3508] Justice La Forest concluded accordingly because, as he said, based on the facts of the Hercules case "*to come to the opposite conclusion on these facts would be to expose auditors to the possibility of indeterminate liability, since such a finding would imply that auditors owe a duty of care to any known class of potential plaintiffs regardless of the purpose to which they put the auditors' reports. This would amount to an unacceptably broad expansion of the bounds of liability drawn by this Court in Haig, supra.*"[3765]

[3509] As was explained by Cherniak,[3766] and agreed to by Campion,[3767] financial statements can be prepared for more than one purpose.

[3510] Castor required audited financial statements in order to obtain and maintain the financing required to meet its current obligations and to enable its business to expand. Defendants were well aware of this purpose, and issued its unqualified opinions with full knowledge of the various ways in which they were being used in pursuit of this purpose, including:

[3761] [1997] 2 S.C.R. 165, at paragraphs 50, 52 and 54
[3762] [1997] 2 S.C.R. 165, at paragraph 50
[3763] [1997] 2 S.C.R. 165, at paragraph 51
[3764] [1997] 2 S.C.R. 165, at paragraph 64
[3765] [1997] 2 S.C.R. 165, at paragraph 64
[3766] Cherniak, February 24, 2010, pp. 78-79.
[3767] Campion, September 1, 2009, pp. 52-53

- *Providing the audited financial statements to lending institutions pursuant to covenants in loan agreements*. Being Castor's auditor since its inception, and reviewing its loan documentation, C&L knew that Castor had to provide audited financial statements to its lenders as a condition of its financing agreements and also knew the identity of such lenders, as appears from the lists of liabilities in the AWPs and confirmations. In fact, C&L acknowledged as much in a letter to Revenue Canada,[3768] in which they represented that CHI's lenders relied on Castor's audited financial statements as the basis for their financing decision and made representations that the improved liquidity on such statements due to the $100M debenture transaction made it easier for Castor to obtain financing from lenders. C&L also communicated directly with Castor's lenders[3769] to explain the financial statements, thereby providing them with further comfort to extend credit and continue lending. For example, in 1991, Wightman met with Norman Martin of BV Bank and reviewed the audited financial statements in detail with this lender, which contributed to their decision to continue to extend credit to Castor.[3770]

- *Distributing the audited financial statements to current and potential shareholders and depositors in order to solicit investments*.[3771] Wightman knew that this information was distributed by way of Castor's brochure, which he reviewed to ensure the accuracy of the financial information contained therein.[3772] He also kept his own stack of these materials[3773], and admitted to having sent them to potential depositors on occasion[3774] as well as to having requested that such information be sent to potential depositors.[3775]

- *Using the audited financial statements as a basis for determining the fair market value of Castor's shares, which in turn, were provided to current and potential shareholders to set the price for the issuance and redemption of shares*.[3776] Defendants intended their opinion in these letters to be relied upon : they qualify an opinion given in another letter as being unreliable by referring to the share valuation letters, as an example of a reliable opinion.[3777] Even though Wightman denied knowing that the letters were being used to solicit investments, he could not provide an alternative explanation as to why Castor was provided with

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[3768] PW-60; PW-1492-3A, p. 3
[3769] Wightman, March 11, 2010, pp. 72-75; PW-3107, PW-2372-28, PW-2496
[3770] PW-72; Martin, November 5, 2008, pp. 33-34
[3771] Wightman, October 20, 1995, pp. 114-115
[3772] Wightman, March 11, 2010, pp. 36-38
[3773] Although Wightman does not outright admit this, the fact that he explained this status to a party that did not require this status to invest indicated that he knew it was being used to indicate a safe investment from a profitable company.
[3774] Wightman, February 10, 2010, p. 131
[3775] Wightman, June 20, 1996, p. 58; Simon, May 1, 2009, pp. 154-155; PW-2372-32-1; PW-2372-32-2
[3776] PW-665-2; PW-1053-50A, sequential pp. 23, 25-26 (Shows National Trust purchasing shares at the price of the most current valuation letter)
[3777] PW-1053-50B-1, seq. p. 166

multiple copies of the valuation letters, when there were always less than 14 directors.[3778] C&L knew that Castor intended to increase its capital base and to attract more European individual depositors as opposed to banks: those facts were noted by C&L in their audit working papers.[3779]

- *Using the audited financial statements as a basis for the issuance of legal-for-life opinions*, which in turn, were used to solicit specific investments from pensions, trusts, and insurance companies[3780] as well as a general marketing tool to show Castor as a safe investment to current and potential shareholders, investors, lenders and depositors.[3781]

[3511] Each case must be looked at on its facts to determine whether indeterminacy is truly a concern in the situation.

[3512] In this second part of the test, the Court must enquire, when deciding whether or not policy considerations ought to negate or limit C&L's *prima facie* duty towards Widdrington, if C&L had knowledge of the identity of Widdrington (or of the class of plaintiffs) and what use was made of the work products at issue.

[3513] The facts of the case are the cornerstone of such an enquiry. As explained by Cherniak, «*there is no substitute for a close examination of the facts to determine auditor's liability in general and whether indeterminacy considerations do arise and whether they are negatived.*»[3782]

[3514] If the facts reveal that indeterminacy is not an issue, such as when the plaintiff (or class of plaintiffs) is known to the defendant and the statement is relied upon for the purpose for which they were prepared, there is no reason not to hold an auditor liable for the reasonably foreseeable consequences of a third party's reasonable reliance on his negligently executed work.

[3515] Based on the facts of the Castor file, the Court concludes that the Castor case is an "*exception*" to the general class of auditors' liability cases in that she finds, as Justice La Forest wrote, that "*the typical concerns surrounding indeterminate liability do not arise*".

[3516] Knowledge of the plaintiff (or of a limited class of plaintiffs) and use of a work product for a purpose for which it was prepared are significant factors serving to obviate concerns over indeterminate liability.

[3778] PW-2315
[3779] PW-2677
[3780] Wightman, October 20, 1995, pp. 160-161
[3781] Simon, June 16, 2009, pp. 75-76
[3782] Cherniak, February 24, 2010, pp. 68-69

> the presence of such factors in a given situation will mean that worries stemming from indeterminacy should not arise, since the scope of potential liability is sufficiently delimited. In other words, in cases where the defendant knows the identity of the plaintiff (or of a class of plaintiffs) and where the defendant's statements are used for the specific purpose or transaction for which they were made, policy considerations surrounding indeterminate liability will not be of any concern since the scope of liability can readily be circumscribed. Consequently, such considerations will not override a positive finding on the first branch of the Anns/Kamloops test and a duty of care may quite properly be found to exist.[3783]
>
> It should be equally clear, however, that in certain cases, this problem does not arise because the scope of potential liability can adequately be circumscribed on the facts.[3784]

[3517] Defendants knew that a distinct group was relying on their professional opinions. In the words of Wightman, Castor was «*a private investment club*», comprised of closely connected high net worth shareholders and lenders.[3785] Being a member of this investment club, Widdrington was clearly part of the class for whose benefit C&L knew that the audited financial statements,[3786] the share valuation letters[3787] and indirectly, the legal for life opinions[3788] were prepared. Wightman's acknowledgment of this limited group shows that the class to which C&L owed a duty, and who was reasonably in their contemplation in the execution of their mandate, is not indeterminate.

[3518] As a consequence of his significant involvement with Castor, Wightman was aware of the identity of the investment club members. As was explained by Ron Smith, Wightman was viewed as a key ally in Castor's promotion among the members of this club with whom he interacted at the cocktails and dinners organized in conjunction with the shareholders' and directors' meeting,[3789] and with whom he discussed the company's financial position.[3790]

[3519] Wightman's participation in the promotion of C&L's professional opinion among these class members further militates against a finding of indeterminacy. Wightman viewed the investment club to be such a tight-knit group that he even justified the decision to use a SCNIA, rather than a GAAP mandated SCFP in the audited financial statements: in his view, if any shareholder or lender in the club wanted to see the SCFP, he or she would have phoned and the change would have been made:

[3783] [1997] 2 S.C.R. 165, at paragraph 37
[3784] [1997] 2 S.C.R. 165, at paragraph 44
[3785] Wightman, February 8, 2010, p. 173; February 11, 2010, p. 205; October 11, 1995, pp. 60-61. References to the investment club can be found in the working paper, e.g. PW-1053-50B-2, seq. p. 585
[3786] Wightman, October 20, 1995, pp. 114-115
[3787] See question 65; See also PW-665-2 (p. 3, "Other considerations"); Wightman, August 13, 1996, pp. 88-89
[3788] See question 56; PW-1053-6, seq. p. 103
[3789] R. Smith, May 14, 2008, pp. 110-111; PW-2434, PW-2435, PW-2436
[3790] R. Smith, May 14, 2008, p. 111

> "CASTOR was such a closely held and closely followed company that I felt that if any of the major investors or lenders could have asked CASTOR for that Statement and CASTOR might have in fact changed their presentation accordingly if they felt that somebody was interested." [3791]

[3520] This justification is an express acknowledgement of the limited class that, to C&L's knowledge, was receiving and was relying on Castor's financial statements, which included both the lenders and investors.

[3521] The distribution to, and the reliance on the audited financial statements by shareholders, investors and lenders for various financing purposes, was common knowledge to the audit staff, including Wightman,[3792] Grzelak[3793] and Hunt,[3794] who noted such a purpose in the Audit Planning Memo for 1990, on the first day working on the audit.[3795]

[3522] Wightman also knew that Castor's brochures, which included the five-year summary of the audited financial statements and referenced Castor's legal for life status, were being used by lenders and investors contemplating doing business with Castor.[3796] In fact, he kept such brochures in his office[3797] and on occasion, distributed them to third parties contemplating doing business with Castor.[3798]

[3523] Unlike the financial statements in *Hercules*, the Castor financial statements were not prepared for a statutory audit since Castor was not obliged by statute to produce audited financial statements.

[3524] Castor's financial statements were prepared by C&L for other purposes which C&L was aware of and approved of. The financial statements were used in share valuation letters and Legal for Life Certificates, they were included in information brochures, they were distributed to actual and potential investors and creditors (some of whom were directly solicited by Wightman himself), they were used in tax planning and structuring including the incorporation of C.H. (Ireland) Inc. by Wightman, and they served in communications with investors and lenders. Wightman considered Castor to be an investment club and the audited financial statements were distributed to and relied upon by the members and the potential members of the club.

[3791] Wightman, September 13, 1996, pp. 47-48
[3792] PW-2695, wherein Wightman recommends that Castor follow a new presentation, because «*Castor's statements are widely distributed*»
[3793] Grzelak, October 22, 1996, pp. 196-201
[3794] Hunt, March 28, 1996, pp. 86-91
[3795] PW-1053-16, seq. p. 265
[3796] PW-1057-1, PW-1057-2, PW-1057-3; Wightman, March 11, 2010, pp. 36-38; Wightman, September 13, 1996, pp. 109-110
[3797] Wightman, March 11, 2010, p. 38
[3798] Wightman, February 10, 2010, p. 131

[3525] C&L knew that the share valuation letters were being used by current and potential investors to justify the share price for the frequent capital subscription requests, and that «*shareholders were coming and going*» based on the prices set in the valuation letters.

[3526] C&L was aware of the impact of the Legal for Life designation, which enabled Castor to attract investments from insurance companies and pension funds requiring such a status, as well as in general, by providing comfort to investors as to the safety of the investment.

[3527] C&L knew of an identifiable class of plaintiffs and of the various uses those plaintiffs would make of their work products (audit reports, consolidated audited financial statements, valuation letters and Certificates for Legal for Life Opinions).

[3528] Only one conclusion can be reached: by their course of conduct, C&L consented, if not expressly at least implicitly, to the use of their work products for those purposes.

[3529] Moreover, through the content of the various valuation letters that they issued, C&L associated themselves with Castor's information, without expressing any limitations or reserves, while if they wanted to exclude or limit their liability, they had to according to the professional standards that were applicable to them as accountants and auditors.

[3530] Concerns over indeterminate liability have sometimes been overstated.[3799] In fact, in the Castor environment, C&L never was exposed to *liability in an indeterminate amount for an indeterminate time to an indeterminate class.* Through their audit partner Wightman, who was actively involved in the development of Castor's business since Castor's inception and until its demise, they were always in a position to foresee what they were getting themselves into, whether they acted upon it or not.

[3531] On the facts of this case, as described throughout the present judgment, the Court finds that deterrence of negligent conduct is an important policy consideration with respect to auditors' liability that needs to be taken into consideration.[3800].

[3799] [1997] 2 S.C.R. 165, at para.33
[3800] [1997] 2 S.C.R. 165, at para.35

Second requirement –untrue, inaccurate, or misleading representation

[3532] This requirement raises issues of fact that have been dealt with under the headings of the present judgment to which the Court refers, having nothing else to add.

Third requirement - defendant must have acted negligently in making said misrepresentation

[3533] Again, this requirement raises issues of fact that have been dealt with under the headings of the present judgment to which the Court refers, having nothing else to add.

Fourth requirement - plaintiff must have relied, in a reasonable manner, on said negligent misrepresentation

[3534] Under the heading "Reliance" of the present judgment, the Court explained why she finds it was reasonable for Widdrington to rely on the Defendants' work products.

[3535] In light of Campion's cited authorities that "*the question of reliance is a question of fact to be inferred from all of the circumstances of the case and all of the evidence adduced at trial*"[3801], these explanations of the Court are the answer to the fourth requirement.

Fifth requirement- the reliance must have been detrimental to the plaintiff in the sense that damages resulted

[3536] This requirement raises issues of fact that have been dealt with under the heading "The damages issue" of the present judgment to which the Court refers.

[3537] According to the evidence that was adduced by Cherniak and Campion before the Court regarding damages issues at common law, there is nothing contradictory to or substantially different from the legal principles she did apply under the Civil Code of Québec.

[3801] L.K. oil & Gas Ltd. v. Canalands Energy Corp. [1989], 60 D.L.R. (4th) 490, at page 500 (Alta C.A.); TWT Enterprises Ltd. v. Westgreen Developments (North) Ltd., [1992] 5 W.W.R. 341 (Alta. C.A.)

[3538] For example, there is no issue of contributory negligence which could possibly impact differently on the Plaintiff's capacity to recover.

- In *Ingles v. Tutkaluk Construction Ltd.*, the Supreme Court of Canada stated the principle of joint and several liability at common law as follows:

> «The purpose of a regime which imposes joint and several liability on multiple defendants is to ensure that plaintiffs receive actual compensation for their loss. Given the wording of the Ontario Negligence Act, I can see no reason to deny this benefit to a plaintiff who contributes to his or her loss. His or her responsibility for the loss is accounted for in the apportionment of fault. There is no reason to account for it again by denying him or her the benefit of a scheme of joint and several liability when the wording of the legislation does not intend it to be so.[3802]

- In the case of *Campbell v. Calgary Power Ltd.*,[3803] section 2(2) of the Alberta *Contributory Negligence Act*,[3804], which is identical to section 2(2) of the New Brunswick statute in all material aspects, was held to expressly preserve the traditional joint and several liability.

- A similar conclusion was reached by the Saskatchewan Court of Queen's Bench in *Housen v. Nikolaisen*,[3805] where legislation virtually identical to that of New Brunswick, Ontario and Alberta, was interpreted.

[3802] *Ingles v. Tutkaluk Construction Ltd.*, [2000] SCC 12 (CanLII),at paragraph 59.
[3803] *Campbell v. Calgary Power Ltd.*, [1988] A.J. No. 855 (Alta. C.A.), at 9
[3804] R.S.A. 1980, c. C-23
[3805] *Housen v. Nikolaisen* [1997] S.J. No. 759, at para. 108, reversed on appeal, restored by the Supreme Court of Canada, *Housen v. Nikolaisen*, [2002] 2 S.C.R. 235, AZ-50118043, J.E. 2002-617

The damages issue

Plaintiff's claim

[3539] Widdrington's claim for damages totalling $2,672,960 breaks down as follows[3806]:

- $1,422,960 representing the full refund of his total investments in Castor;
- $1,250,000 representing the costs for the settlement out of court of the petition and legal action pursuant to a transaction agreement entered into on March 11, 1998, between Widdrington and the Trustee to Castor's bankruptcy.

[3540] The amount of $1,422,960 claimed by Widdrington for his investments in Castor are the result of three successive transactions that Widdrington made between October 1988 and October 1991:

- A deposit of $200,000 in October 1988, which amounted to $231,800.82 when it was rolled over to finance his first investment;
- An additional $898,599.18, paid in December 1989 in order to complete the financing of the first investment - the purchase of four (4) units in Castor for an aggregate price of $1,130,400;
- The purchase of an additional unit in the amount of $292,560, in October 1991.

Positions in a nutshell

Plaintiff

[3541] Plaintiff argues that he should be granted all the damages claimed, namely because:

- He would never have been involved with Castor, and would never have been in the position to approve dividends, but for his reliance on the negligently issued audited financial statements.

[3806] Paragraphs 2 and 171 of the statement of claim

- Had the audited financial statements and valuation letters revealed the true financial situation of Castor, he would not have invested and therefore would not have suffered the loss of the invested amounts.

- The amounts he paid to the Trustee to settle the claims are the direct and immediate consequence of Defendants' fault. He trusted that the audited financial statements fairly presented Castor's true financial position, and he was confident that Castor was in a position to pay the $15,522,942 in dividends declared in the 12 months preceding its bankruptcy, when, unbeknownst to him, Castor was hopelessly insolvent.

- His damages should not be reduced by any supposed benefits he obtained as a result of his investment in Castor.

    - Director fees, which are compensation for work, and trips to Europe for board meetings, cannot be characterized as "profits".

    - The dividends and interest earned on the investments cannot be characterized as profits. Had Widdrington not invested in Castor, he could have invested in another venture.

    - It would be unfair to allow Defendants to obtain a reduction for such gains because Plaintiff lost his entire investment due to Defendants' negligence, and was deprived of the earnings benefit of his investment. But for Defendants' negligence, his investment should have continued to generate revenue but, due to the fact that it has been lost completely, is no longer generating revenue.

[3542] As far as the reimbursement of the settlement that he reached with the Trustee, Plaintiff further argues the following:

- Defendants benefited from this settlement, as Plaintiff's claim under this head of damages would have been for the entire amount of any judgment against him had he not settled.

- Even though his approval of the dividends was based on the audited financial statements, and therefore the fault of Defendants, it was far from certain at the time that a contestation would be successful as the *Bankruptcy and Insolvency Act* did not explicitly provide a defence based on the reasonable belief of the company's ability to pay.[3807]

[3807] *Castor Holdings (Syndic de)*, [2008] QCCS 3437 (CanLII) at 57-67.

- If the claim against him had been successful, Plaintiff feared that he would have been required to satisfy the entire judgment, as he was one of three Canadian defendants (the others are Europeans) and the only one with assets in Canada.

- The fact that in 2008 the other directors were found solidarily liable to repay the dividends after an arduous and expensive litigation further supports the reasonableness of the settlement.[3808]

[3543] Plaintiff submits that the following issues, also raised by the Defendants, are irrelevant in light of the facts of the case, and ill-founded.

- The "stampede effect":

  - had the audited financial statements and valuation letters revealed the true financial situation of Castor, Widdrington would not have invested and therefore would not have suffered a loss, even if there had been a "stampede effect" in 1988[3809], or

  - if the audited financial statements and the share valuation letters prepared by C&L (PW-5 and PW-6) had reflected, for real, the financial position of Castor, Castor would have been a highly solvent and viable company, able to survive a downturn in the economy, as it had apparently done in the early 80s.

- The "stampede effect": No proof was made by Defendants to support their assertion that there would have been a stampede effect.

- The shareholders' agreement: Had the audited financial statements not been misstated, and had C&L's opinion as the fair market value of Castor's shares been correct, there are no provisions in the Shareholders' Agreement that would have precluded Widdrington from disposing of his shares in Castor, pursuant to its terms.

- The "tax treatment": Defendants should not be able to benefit from the potential savings generated from losses which are borne by the Crown by way of tax savings. If the Court was to come to a different conclusion, Defendants who had the burden of proof did not discharge it.

- The "alleged faults of others": Liability of the Defendants cannot be reduced in any way due to unproven allegations they made against third parties that are

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[3808] *Castor Holdings (Syndic de)*, [2008] QCCS 3437 (CanLII), at para 1-2 and 146.
[3809] *Hodgkinson v. Simms* [1994] 3 S.C.R. 377 (SCC), at para. 72 and 92.

not parties to the litigation. Defendants were free to commence a separate action against anyone who they felt might also be responsible, and claim indemnification from them accordingly. However, this was completely irrelevant to the Widdrington action.

[3544] Plaintiff argues:

- Widdrington committed no fault, either in the exercise of his duties as director of Castor, or in the due diligence he exercised prior to making his respective investments in Castor.

- Defendants had the burden to prove a fault on his part, which was the logical, direct and immediate cause of the damages suffered. They failed to discharge such burden.

- Contributory negligence can only apply when a court finds that two faults have caused the damage[3810] : it cannot be the case in the present file.

[3545] Plaintiff submits there is no issue of contributory negligence which could possibly impact on his capacity to recover, whether the applicable law is the Quebec law or the common law applicable in New Brunswick or Ontario. Plaintiff cites the provisions of the New Brunswick law, the provisions of the Ontario law and he argues that the principles established by Quebec doctrine and jurisprudence are similar.

- The relevant provisions of the *New Brunswick Contributory Negligence Act*.[3811]

> 1(1) Where by the fault of two or more persons damage or loss is caused to one or more of them, the liability to make good the damage or loss is in proportion to the degree in which each person was at fault but if, having regard to all the circumstances of the case, it is not possible to establish different degrees of fault, the liability shall be apportioned equally. [...]
>
> 2(2) Except as provided in sections 3 and 4, where two or more persons are found at fault they are jointly and severally liable to the person suffering the damage or loss, but as between themselves, in the absence of any contract express or implied, they are liable to make contributions to and indemnify each other in the degree in which they are respectively found to have been at fault. [3812]

[3810] See, for example *Business Development Bank of Canada c. Pfeiffer,* [2009] QCCS 2310 (CanLII), at para. 93.

[3811] .S.N.B. 1973, c. C-19, articles 1(1) and 2(2)

[3812] D-666; Subsequent amendments to this Act up to this day are as follows: 1991, c.27, s.11: « Subsection 2(2) of the Contributory Negligence Act, chapter C-19 of the Revised Statutes, 1973, is amended by striking out "sections 3 and 4" and substituting "section 4". »; 1995, c.40, s.3(1) : « Subsection 2(2) of the Contributory Negligence Act, chapter C-19 of the Revised Statutes, 1973, is

- The relevant provisions of the *Ontario Negligence Act*.[3813]

> 1. Where damages have been caused or contributed to by the fault or neglect of two or more persons, the court shall determine the degree in which each of such persons is at fault or negligent, and, where two or more persons are found at fault or negligent, they are jointly and severally liable to the person suffering loss or damage for such fault or negligence, but as between themselves, in the absence of any contract express or implied, each is liable to make contribution and indemnify each other in the degree in which they are respectively found to be at fault or negligent.
>
> 3. In any action for damages that is founded upon the fault or negligence of the defendant if fault or negligence is found on the part of the plaintiff that contributed to the damages, the court shall apportion the damages in proportion to the degree of fault or negligence found against the parties respectively.[3814]

[3546] Plaintiff argues the Defendants should be held jointly and severally liable. In his written submissions of July 8, 2010, Plaintiff argued and wrote:

> Liability between the partners of C&L is joint and several because, according to art. 1106 *Civil Code of Lower Canada* (C.c.), this is the rule for extra-contractual liability between two or more persons. Several cases have held that the professional liability of partners working together in auditing firms results in liability on a joint and several basis, including *Verrier c. Malka.*[3815] Art. 1854 C.c., which provides that partners are not jointly and severally liable for the debts of the partnership, does not interfere with the application of 1106 C.c. in this action. This is because the provision leads to joint liability for the partnership's contractual obligations only.[3816] A partnership's professional responsibility is, rather, governed by the rules of mandate,[3817] according to which mandators (all of the partners) are liable for the damages caused by the fault of their mandataries (the individual partners) based on 1054 C.c.[3818] Accordingly, article 1106 C.c. applies to result in joint and several liability.
>
> In 1925, the Supreme Court of Canada applied article 1854 C.c. to prevent a plaintiff from recovering the totality of a debt resulting from one partner's failure to

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amended by striking out "Except-as provided in section 4, where two or more persons" and substituting "Where two or more persons". s. 3(2): « Section 4 of the Act is repealed.»

[3813] R.S.O. 1990, c. N.1, articles 1 and 3

[3814] R.S.O. 1980, c. 315, s. 4.

[3815] AZ-50401934 (S.C.), aff'd, 1998 CanLII 12884 (Qc. C.A). See also *Sumabus inc. c. Daoust*, [1994] J.Q. no. 2667 at para. 42.

[3816] Discussing article 2219 C.C.Q. (which replaced article 1854 C.c.), the Court explained in *Bélisle-Heurtel c. Tardif*, REJB 2000-20086 at para. 182 that joint liability «*ne s'applique qu'en matière contractuelle*».

[3817] According to article 1856 C.c., liabilities which are not regulated by any article under the title *Of Partnerships*, are governed by the rules *Of Mandate*. Since professional liability is not so covered, these rules apply.

[3818] Article 1731 C.c.

> pay the plaintiff's debt pursuant to a mandate.[3819] This decision, however, should not prevent this Court from holding Defendants jointly and severally liable in the present case. Firstly, the case is distinguishable on account of the fact that the plaintiff's action was based on a failure to pay pursuant to a specific mandate, which could be considered a debt of the partnership for which art. 1854 C.c. applied. Conversely, there is no contract on which to base this argument in the Widdrington action. Rather, Plaintiff's claim is exclusively based on an extra-contractual fault for which solidarity amongst all responsible parties is presumed by law. Defendants derived credibility from using C&L's name in carrying out their professional practice together; third parties relying on the strength of that name are therefore entitled to claim from any of them for the losses incurred as a result of their reliance. Secondly, civilian scholars have taken the position that this case was wrongly decided because even though there was a contract, the claim related to a breach of a professional obligation.[3820] Indeed, subsequent cases have presumed, without any discussion on the issue, that the professional fault of a partner results in joint and several liability between all partners.[3821] This approach is also consistent with that followed in the rest of Canada, where partners are joint and severally liable for extra-contractual faults committed by their partners in the normal course of business of a partnership by virtue of various Partnership Acts. For example, in Ontario's *Partnership Act*[3822], section 11 stipulates that that the partnership is liable, to the same extent as the partner committing the fault, for losses resulting from "*any wrongful act or omission of a partner acting in the ordinary course of the business of the firm, or with the authority of the co-partners.*" While section 13 thereof stipulates that partners are jointly liable for the obligations contracted by the partnership (as in Quebec), it also stipulates (as do the Quebec rules of mandate and extra-contractual liability), that they are severally liable for the obligations of the partnership incurred under section 11.

[3547] Plaintiff concludes that the Defendants shall be condemned to pay, jointly and severally, the amount claimed.

Defendants

[3548] For one or many of the following reasons, the Defendants submit that no damages can be or should be awarded to Plaintiff.

[3819] *Perodeau c. Hamill*, [1925] S.C.R. 289.
[3820] Hervé Roch and Rodolphe Paré, *Traité de Droit Civil du Québec* (Montréal: Wilson Lafleur, 1942) at 402.
[3821] See e.g. *Laidley c. Kovalik*, 1994 CanLII 5878 at 2 (Qc. C.A.); *Verrier c. Malka*, AZ-50401934 (S.C.), aff'd, 1998 CanLII 12884 (Qc. C.A) and *Sumabus inc. c. Daoust*, [1994] J.Q. no. 2667 at para. 42.
[3822] R.S.O. 1990, c. P.5, section 11.

Claim of $1,422,960

[3549] Defendants submit that Widdrington's claim of $1,422,960 should be dismissed for the following additional reasons:

- None of those 3 investments of October 1988, December 1989 and October 1991 can be attributed to Widdrington's reliance upon the auditor's reports on the financial statements of Castor, the valuation letters signed by C&L or the Legal for Life Certificates issued to McCarthy Tétrault with respect to its Legal for Life Opinions. The overwhelming evidence clearly shows that the determinative factor that led to Widdrington's three investments was his absolute faith and blind trust in Stolzenberg.

- The main and immediate cause of the creditors' losses was the collapse of Castor in 1992 due to the meltdown of the commercial real estate values commencing in the early 90s.

- Given the terms and conditions of Castor's shareholders' agreement[3823], Widdrington knew or should have known that there was no free market for Castor's shares and that he could not dispose of his shares at will without the consent of his fellow directors and shareholders. If it was difficult for Widdrington to get out of his investments in the best of circumstances, it would be even more so if Castor's financial condition deteriorated. The lack of exit ability was a risk that Widdrington knew and accepted from the outset.

- Widdrington has not discharged his burden to prove that if the audited consolidated financial statements for the relevant year-ends had been issued with hundreds of millions in losses he alleges they should have shown, he would have been able to recover part or all of his 1989 and 1991 investments. In fact, had the audited consolidated financial statements been issued and published with the figures proposed by Widdrington, the most probable outcome would have been a run on all Castor's assets (the stampede effect) by all the secured and unsecured creditors, which would have left the company bankrupt with hundreds of millions of debt outstanding, debt to which Widdrington's investments were subordinated.

- Finally, the "benefit rule" should apply and the amounts received by Widdrington while he was a shareholder and a director of Castor should be deducted from any indemnity. Therefore, benefits aggregating $179,436.10 should be deducted from any damages the Court would allow to Widdrington (further to his investments in Castor) because it would be highly irregular and unfair if Widdrington was allowed to get the full refund of his investments while keeping the benefits thereof at the same time.

[3823] PW-2832

Claim of $1,250,000

[3550] Defendants submit that Widdrington's claim of $1,250,000 representing the refund of what Widdrington paid to the Trustee to settle out of Court the latter's petition, seeking reimbursement of the September 1991 dividends [3824] and the action for negligence instituted against Castor's directors,[3825] should be dismissed for the following additional reasons:

- Widdrington's claim for the refund of the amounts he agreed to pay to the Trustee pursuant to the settlement agreement[3826] has nothing to do with his alleged reliance on C&L's representations for purposes of his investments in Castor. His personal reasons for justifying this settlement have nothing to do with C&L's alleged negligence in the representations they issued with respect to Castor.

- These legal proceedings were instituted against Widdrington essentially by reason of Widdrington's failure to properly discharge his duties and responsibilities as a director of Castor.

    - Either Widdrington had a due diligence defence available of good faith reliance on C&L and, if that defence was well-founded, his payment to the Trustee was gratuitous and he cannot be indemnified; or,

    - The due diligence defence was not well-founded, and then Widdrington has only himself to blame;

    - In either circumstance, there is no basis for a claim against C&L.

- Widdrington failed to discharge his legal duties as a director. His failure, as well as the failure of the other directors to discharge their duties, allowed Stolzenberg to manage Castor without board supervision. This failure precludes Widdrington from claiming that he relied in a reasonable manner on C&L with respect to financial information for which Castor's directors were primarily responsible.

- Widdrington failed to adduce proof justifying the reasonableness of the amount of the settlement reached with the Trustee.

[3824] PW-1
[3825] PW-8A
[3826] PW-39

The existence of a claim by the Trustee in bankruptcy

• The Trustee in bankruptcy of Castor instituted an action against C&L, on behalf of Castor, claiming $40 million of damages[3827]. The Trustee's action precedes and pre-empts those of ordinary creditors. If the Trustee's action was successful, Widdrington would receive an amount that cannot be ascertained at present. Therefore, and since Widdrington's damages cannot be definitively determined before the Trustee's action is decided, Widdrington's claim should be dismissed.

No joint and several liability for the C&L partners

[3551] In their written submissions of July 8, 2010, Defendants write and argue:

> If the Court determines that C&L is liable to the Plaintiff, the issue of the liability of C&L individual partners would arise. C&L is an Ontario partnership. However, since there are no allegations with respect to the rules governing the liability of individual partners as per Ontario law, the Court must apply Quebec law (art. 2809(2) C.C.Q).
>
> The liability of partners for the acts performed before January 1st, 1994 is governed by the CCLC[3828]. Under the CCLC, a partnership of professionals was a civil partnership since the activity of professionals was not considered to be of a commercial nature[3829]. According to art. 1854 CCLC, the partners of a civil partnership are not solidarily liable for the debts of the partnership, they are rather liable to the creditor in equal share, even though their shares in the partnership may be unequal. In the case of *Pérodeau* v. *Hamill* (1925) S.C.R. 289, it was thus decided by the Supreme Court that the liability of partners of a civil partnership was *conjointe* and not solidarily. As a consequence, the individual partners of C&L would only be liable *conjointement*, each for an equal amount, for any liability that could be found against C&L in the present case.

[3552] In their written submissions of August 5, 2010, Defendants add:

> Plaintiffs have never alleged the application of the Ontario Partnership Act to govern the issue of the liability of C&L's individual partners, if any. In light of this, Quebec law applies in that respect, not because Quebec law is applicable as such, but because no party has alleged the application of another law (cf. art. 2809 CCQ). The Supreme Court decision in Pérodeau v. Hamill (cf. DPA, p. 263) authoritatively determines that the professional liability of the partners of a civil partnership is conjointe in equal shares, as per art. 1854 CCLC. Art. 1106 CCLC has no application in such a case since it only applies where the defendants

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[3827] See file 500-05-003843-933: a pending claim before our Court

[3828] *An Act respecting the implementation of the reform of the Civil Code*, 1992, Q.L., c.57

[3829] *Pérodeau v. Hamill*, [1925] S.C.R., 289; *Bastien v. Beaulac*, J.E. 2000-1963; *Samson Bélair, v. Autobus Fortin*, AZ-87021265

> have each committed a fault,[3830] which is certainly not the case when partners of a firm are liable qua partners for the wrongful act of the firm or of another partner.

Evidence

[3553] Widdrington became a director of Castor in 1990.

[3554] Before he made his investment in October 1991, Widdrington participated to board of directors' meetings and shareholder's meetings:

- The shareholder's meeting that took place on April 8, 1990, in Zurich.
- The board meeting that took place on October 12, 1990, in Toronto.
- The board meeting of March 21, 1991, in Montreal at which time the declaration of dividends was unanimously approved by Castor's Board of Directors.
- The board meeting and the shareholders' meeting of May 7, 1991, in Zurich.
- The board meeting of October 24, 1991, in New York City.

[3555] A capital call of September 25, 1991 had targeted an amount of $25 million to be raised from existing directors and shareholders.

[3556] Stolzenberg's presentation at the board meeting held on October 24, 1991 is summed up, as follows, in Castor's minutes book:

> "The Chairman reported that as a result of the current environment in the banking industry Castor had recently experienced a reduction or cancellation of certain of its credit facilities (particularly with the Japanese and French banks) which, together with the necessity for the Corporation to refinance certain of its mortgage loans (where other financing was not available to borrowers), was causing a liquidity problem for Castor, which the Chairman was working hard to solve. He stated that certain shareholders were prepared to reinvest their dividends to alleviate this problem.
>
> The directors unanimously endorsed the Chairman's efforts to correct the situation, and the meeting agreed that it was in the best interests of the Corporation to raise additional capital and to secure medium term debt financing. The Chairman pointed out that the minimum target for raising funds should be $50,000,000 but ideally $100,000,000 to overcome the present situation and to look positively forward towards 1992. The Chairman also stated that further support of the present shareholders would be absolutely necessary. In that

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[3830] *Masoud v. Modern Motor Sales*, [1953] S.C.R. 149, at p. 165

connection the Chairman reported that he had already secured additional capital subscriptions from existing shareholders for $1.5 million".[3831]

[3557] Widdrington described the atmosphere of Castor's board meeting that took place on October 24, 1991, as follows:

"Q. How would you describe the atmosphere of that Board meeting?

A. It was considerably more sombre than previous meetings.

Q. Sombre in the sense that...

A. serious.

Q. Is that because of the – what would you ascribe this somberness to at this October twenty-fourth (24th) meeting?

A. Well, my guess is that it might have been the fact that the directors had been asked to put up more money.

Q. That wasn't the first time they were asked to do so, was it?

A. It was as far as I was concerned.

Q. Did you know at the time whether they had been previously asked to increase their shareholding?

A. I did not.

Q. Was the somberness also due to the state of the real estate market, in your view?

A. I'm not going to attempt to explain the fact that I felt the meeting was somber, outside of my own reaction.

Q. Was it your reaction that the request for increasing the shareholdings was a sign of problems for the company?

A. It was a sign of some sort of problem in the sense that a system that previously existed wasn't functioning quite as well as it has in the past.[3832]

[3558] As of October 24, 1991, Castor had only secured additional capital subscriptions from existing shareholders of $1.5 million.

[3831] PW-51

[3832] Widdrington, November 9, 1995, pp.164-165

[3559] Castor was very far from its target and Stolzenberg, its Chairman, had proposed that $50 to $100 million of capital was required to overcome the situation and to look positively at the forthcoming 1992 year.

[3560] In a memo to Widdrington dated October 26, 1991, Prikopa wrote:

> "Your investment in Castor is not easy to cash out if for some reason you wanted to get out cash out is possible but it is at the discretion of Castor, and if Castor got into trouble a sell would not be possible.[3833]"

[3561] Lowenstein testified that, perhaps, as a professional director or a professional that does a lot of due diligence, he might have wanted to say, "*well, how serious is this*?".[3834]

[3562] Morrison expressed the opinion that a prudent director should have obtained full details on Castor's problems[3835].

[3563] Lajoie expressed the opinion that Stolzenberg's letter dated September 25, 1991[3836], followed by the minutes of the October 24, 1991 board meeting[3837] amounted to "red flags" that Widdrington should have seriously considered before making his last investment.[3838]

[3564] When he received the minutes of the October 24, 1991 meeting (at the meeting that took place on December 16, 1991) and noticed that he was the only director who had provided funds as a result of the call for additional capital, Widdrington felt betrayed.[3839]

[3565] As a result of his investments and as a result of his directorship at Castor, Widdrington received $164,436.10 in dividends, interest payments and directors' fees between October 1989 and Castor's bankruptcy[3840].

[3566] In December 1989, Prikopa calculated that the benefits associated with Widdrington's investment in Castor included the value of two trips to Europe per year, estimated at $10,000[3841]. Since Widdrington attended three meetings in Zurich during his tenure as director – those of May 8, 1990, May 7, 1991 and February 13, 1992 – he would have received an "additional value" of $15,000 on account of these three trips to Europe.

[3833] PW-47
[3834] Lowenstein, March 24, 2005
[3835] Morrison, October 4, 2006, p. 200-230
[3836] PW-17
[3837] PW-51
[3838] Lajoie, October 18, 2006, 40-71
[3839] Widdrington, January 6, 2005
[3840] PW-2388
[3841] PW-43-2

[3567] No evidence was presented as to the tax treatment of any of the above: the $164,436.10 or the value of trips to Europe.

[3568] The legal proceedings instituted against Widdrington were settled out of Court through a transaction agreement of March 11, 1998[3842] between Widdrington and the Trustee. The amounts paid or to be paid by Widdrington, pursuant to this agreement purported to settle both the Trustee's petition for dividends[3843] and the Trustee's action for negligence,[3844] are:

- A first amount of $750,000 paid to the Trustee, which includes an amount of $150,000 payable to Langlois Gaudreau for their services to bring the Widdrington action to judgment.

- An amount of $650,000 less all legal fees and disbursements incurred to execute the judgment, to be paid from the damage award to be granted to Widdrington in the present file (court claim).

[3569] In May 1998, Widdrington testified that he settled the above-mentioned claims for personal reasons such as his age, the need to take care of his daughters and grand-children.[3845] At trial, Widdrington also explained that he was concerned with the additional exposure that he was facing with respect to the Trustee's $15 million claim for the refund of dividends, as he was one of only three Canadian directors on Castor's board.

[3570] On July 30, 2008, a judgment was rendered by Justice Louise Lemelin on the Trustee's petition seeking the reimbursement of the dividends paid to Castor's directors.[3846] In her judgment, Justice Lemelin namely wrote and concluded:

> [2] Il est admis que la requérante a conclu des ententes de règlement hors cour avec quatre intimés initialement poursuivis, soit avec MM. Luerssen (3 650 000 $), Raborn Jr. (200 000 $), Widdrington (750 000 $) et Dennis (1 250 000 $) pour une somme de 5 850 000 $. En début d'audience, la requérante réduit en conséquence sa réclamation à 9 672 942 $ contre les autres intimés.
>
> [3] L'intimé Marco Gambazzi conteste le bien-fondé de cette demande. Les quatre autres intimés, Wolfgang Stolzenberg, Wolfgang Leser, Peter Ochsner et Walther Stromeyer, n'ont produit aucune contestation et ne sont pas représentés lors de l'audience.
>
> (...)

[3842] PW-39
[3843] PW-1
[3844] PW-8A
[3845] Widdrington, May 22 1998, p.17; Widdrington, December 3, 2004
[3846] [2008] QCCS 3437

[25] Il est utile de réciter des admissions faites par la requérante et l'intimé Gambazzi, pour situer le contexte factuel :

> The audited consolidated financial statements of Castor Holdings Ltd. as at December 31, 1990 and the Auditor's report thereon dated February 15, 1991 (collectively filed as Exhibit D-1), both of which were provided to the Directors of Castor Holdings Ltd. at or in the days prior to the Meeting of Directors held on March 21, 1991, did not indicate:
>
> a) That Castor Holdings Ltd. was insolvent at that time; and/or,
>
> b) That the declaration and payment of a dividend by Castor Holdings Ltd. in the amount of $15,522,942.00 would render Castor Holdings Ltd. insolvent.
>
> While Respondent Gambazzi reserves his right to make proof and/or argue that he did not know of the insolvency of Castor Holdings Ltd. in September 1991, Respondent Gambazzi admits that Castor Holdings Ltd. was in fact insolvent in September 1991.

(...)

[43] Ce dossier origine de la même faillite, mais ne porte pas sur les mêmes questions. Le présent jugement n'a pas à décider de la responsabilité des comptables-vérificateurs. D'ailleurs, la requérante et Gambazzi ont signé des admissions pour dissiper tout doute et bien circonscrire le cadre du litige. Il est utile de les reproduire :

> 1. Both Petitioner and Respondent contend and believe that Coopers & Lybrand ("Coopers") was at fault in respect of Castor's financial statements, in general, and Castor's consolidated December 31, 1990 financial statements, in particular, as set forth in separate legal proceedings initiated by each of Petitioner and Respondent before the Quebec Superior Court (the "Coopers Proceedings"); and
>
> 2. Whether Coopers was or was at fault in respect of Castor's financial statements as set forth in paragraph 1 hereof and as alleged by each of Petitioner and Respondent in their respective Coopers Proceedings, is not an issue and is not to be decided in the Petition.

(...)

[56] Existe-t-il à l'époque pertinente une autre défense pour les intimés? La question ne se pose pas pour les intimés Stolzenberg, Leser, Ochsner et Stromeyer puisqu'ils n'ont pas contesté la requête ni proposé aucun moyen de défense, mais qu'en est-il pour Gambazzi?

[57] En 1996, la Loi sur la faillite et l'insolvabilité a modifié entre autres l'article 101 en introduisant une nouvelle condition pour engager la responsabilité

des administrateurs s'ils « n'avaient pas de motifs raisonnables de croire que la transaction était faite à un moment où [la compagnie] n'était pas insolvable ou ne la rendrait pas insolvable. »

(...)

[60] Les auteurs opinent que l'amendement qui nous intéresse est de droit nouveau. Me Dolan souligne qu'avant un seul moyen disculpatoire était possible pour les administrateurs (art. 101(3)). Il ajoute :

> Until recently, the BIA, unlike most comparable corporate legislation dealing with the declaration of dividends [...] did not contain a "due diligence" defence for believing that the corporation was not insolvent at the time in question.

[61] L'auteur Bennett y voit aussi une limitation de responsabilité des administrateurs, disposition législative nouvelle qu'il qualifie ainsi :

> To mitigate the potential liability of directors, Parliament amended section 101 of the Act to provide that the directors are not liable if they have reasonable grounds to believe that the transactions was occurring at the time the Corporation was solvent. In addition to the defence that the directors protested, the directors can argue that they exercised due diligence, acted in good faith [...].

[62] Selon les auteurs Martel , la modification de l'article 101 est venue corriger une injustice pour les administrateurs qui ne pouvaient bénéficier de la défense d'une croyance raisonnablement fondée sur des états financiers ou des rapports d'experts comme en matière corporative. Si on exclut la protestation, en fait les administrateurs avaient l'obligation de faire la preuve du fait objectif de la solvabilité de la compagnie.

[63] Les interprétations de la doctrine confirment également l'argument de texte qui manifestement accrédite l'ajout d'une condition pour tenir responsables les administrateurs lorsque le dividende est payé alors que la compagnie est insolvable et ouvre en contrepartie un nouveau moyen de défense à l'administrateur.

[64] Le tribunal note de plus que le législateur dans ses mesures transitoires prévoit que les modifications à l'article 101 « s'appliquent aux faillites et aux procédures visées par des procédures intentées après l'entrée en vigueur de 1997 ».

[65] En bref, les administrateurs de Castor au moment de la faillite pouvaient se disculper en prouvant leur protestation au paiement ou qu'au 31 septembre 1991, Castor était solvable, il n'existait alors aucune autre défense disponible.

(...)

[71] Le tribunal conclut que même si la défense de croyance raisonnable n'existait pas lorsque le dividende a été payé en 1991, il peut exercer judiciairement sa discrétion et ne pas rendre jugement en défaveur de M. Gambazzi. Ce dernier a le fardeau d'arguer pour quels motifs et d'en faire la preuve. Il faut ici distinguer. Le tribunal ne statue pas sur le moyen de défense accordé par le nouvel article 101, mais apprécie s'il doit exercer sa discrétion en se guidant des principes d'équité.

(...)

[87] M. Gambazzi est un juriste de formation, un homme familier avec le monde des affaires, qui a de plus l'expérience des conseils d'administration et des véhicules corporatifs. Sa signature complaisante témoigne d'imprudence et d'un manque de diligence qui doivent aussi être pris en compte.

[88] Cette participation de Gambazzi à diverses transactions nous amène à vérifier s'il peut avec succès soutenir que ses décisions étaient tributaires des états financiers et opinions accessibles lors de l'assemblée du 21 mars. Le tribunal ne croit pas que M. Gambazzi était dans la complète ignorance de la situation financière de Castor, un survol de certaines transactions éclaire.

[94] Ce qui est pertinent dans le cadre de notre discussion, ce n'est pas d'identifier les dettes et obligations réelles de Castor mais d'apprécier si la conduite de M. Gambazzi lui permet de bénéficier de la discrétion accordée par l'article 101(2).

(...)

[98] M. Gambazzi n'a pas informé Coopers & Lybrand ou le Conseil d'administration de ces prêts consentis à des compagnies dont il est administrateur. L'intimé ne peut toujours pas, lors de son témoignage en Cour, confirmer l'identité des véritables propriétaires de ces compagnies et, ce qui est plus important, de leur situation financière respective. Il ne sait pas non plus si les intérêts prévus ont été payés. Le syndic, pour sa part, dit que les créances à l'endroit de ces compagnies n'ont pu être exécutées.

[99] Le tribunal n'a pas à se prononcer sur le rôle qu'auraient pu jouer les vérificateurs Coopers & Lybrand; comme nous l'avons vu, leur responsabilité est recherchée entre autres par la requérante et l'intimé Gambazzi dans d'autres dossiers de Cour. L'étude de ces prêts n'est faite que pour illustrer que l'intimé savait que certaines entrées comptables n'étaient pas rigoureusement exactes et pouvaient avantager la présentation de la situation de Castor, comme ce fut le cas pour les transactions de FITAM.
(...)

[104] Le tribunal retient que l'intimé Gambazzi était informé que, de façon générale, Castor et/ou M. Stolzenberg se livrait à un exercice de « window dressing » que l'intimé définit en ces termes : (...)

(...)

[106] La preuve retrace une participation de M. Gambazzi dans le flot de transactions circulaires entourant l'émission de 100 millions d'obligations par Castor. Les états financiers constatent en 1989 et 1990 ce passif à long terme. La note 6 des états financiers explique qu'il s'agit de deux groupes d'obligations de 50 millions, échéant respectivement les 30 juin 1997 et 2002 avec possibilité pour Castor de rembourser à compter de 1992 et 1994.

(...)

POUR TOUS CES MOTIFS, LE TRIBUNAL :

[145] ACCUEILLE la réclamation de la requérante;

[146] CONDAMNE solidairement les intimés à payer à la requérante la somme de 8 759 490,00 $ avec intérêts à compter de la signification et l'indemnité additionnelle à compter du 1er juin 2001.

[147] LE TOUT, avec dépens contre les intimés.

Conclusions

General conclusions

[3571] The Court assesses the quantum of Widdrington's claim at the amount claimed of $ 2,672,960 for the following reasons.

[3572] Had the audited financial statements and the valuation letters revealed the true financial situation of Castor, Widdrington would not have invested in Castor. Therefore, he would not have suffered the loss.

[3573] The amount of $2,672,960 constitutes a damage which is the direct and immediate consequence of the Defendants' conduct.

[3574] Plaintiff committed no fault, either in the exercise of his duties as a director of Castor, or in the due diligence exercised by him prior to making his respective investments in Castor.

[3575] There was no contributory negligence on the part of Widdrington. As my colleague Justice Lowry said in *Kripps v. Touche Ross and Co.,* after the case had come back before the British Columbia Supreme Court to resolve the issues of contributory negligence and quantum of damages:

> [18] **The mere assumption of the risk does not**, as the investors contend, **amount to negligence**. (...) It may have been an unacceptable risk for the

> conservative investor but, in my view, it was not, as presented, an unreasonable risk for a prudent investor seeking a high rate of return.
>
> [19] That being so, **the auditors' plea of contributory negligence cannot succeed.**[3847] (our emphasis)

[3576] Moreover, in the circumstances of the present case, the Court finds it appropriate to apply the following remarks made by the Supreme Court of Canada in the case of *Hodgkinson* v. *Simms*:

> [76] What is more, the submission runs up against the long-standing equitable principle that where the **plaintiff has made out a case of non-disclosure** and the **loss occasioned thereby is established**, the **onus is on the defendant** to prove that the innocent victim would have suffered the same loss regardless of the breach; (...)
>
> [92] From a **policy perspective** it is **simply unjust** to **place the risk of market fluctuations on a plaintiff** who would not have entered into a given transaction but for the defendant's wrongful conduct.[3848] (our emphasis)

Specific conclusions

Claim of $1,422,960

[3577] The Plaintiff has discharged his burden of proof: Plaintiff has established fault, damages and causality.

[3578] There is no reason to deduct the amounts received by Widdrington while he was a shareholder and a director of Castor.

- The director fees and travel expenses allocation that Widdrington received were paid as compensation for work and assumed responsibilities.
- If Widdrington had not invested in Castor, he would have invested in another vehicle. Evidence shows that his return would have been equal, and may be even superior to the dividends he received on his Castor's investments on a short term basis.

[3579] The tax treatment of Plaintiff's loss has no relevance to the Court's determination of the quantum of his damages.

[3847] [1998] B.C.J. No. 1670, [1999] 3 W.W.R. 629, 56 B.C.L.R. (3d) 160, 41 B.L.R. (2d) 124,80 A.C.W.S. (3d) 1272

[3848] *Hodgkinson v. Simms* [1994] 3 S.C.R. 377 (SCC), at para. 72 and 92.

[3580] In *Girard & Cie c. Allaire*[3849], Justice Forget of the Québec Court of Appeal explained that defendants should not be able to benefit from the potential savings generated from losses which are borne by the Crown by way of tax savings:

> Il faut donc comprendre que les commanditaires, selon l'expert, auraient pu déduire les pertes annuelles entre 1985 et 1989. Même si tel était le cas, j'estime que l'appelante ne pourrait invoquer cette exemption fiscale à son profit. J'illustre mon raisonnement par un exemple simple. Si le vendeur d'un immeuble garantit les revenus de loyer et que les revenus n'atteignent pas le montant garanti, l'acheteur pourra certes demander une diminution du prix de vente - ou des dommages - sans que le vendeur puisse le contraindre à déduire les exemptions fiscales obtenues à la suite d'une exploitation déficitaire. Autrement, comme le note avec justesse le juge Barbe, on ferait supporter par l'État une partie des dommages causés à l'acheteur par la faute du vendeur.

[3581] In any event, if alleged tax benefits could be taken into account, absent of appropriate evidence into the court record, the argument must be dismissed. In *Girard & Cie c. Allaire*, the Court of Appeal further found that if it would require speculation, it could not be determined on the balance of probabilities as required and should be dismissed.

[3582] The shareholder's agreement argument is either irrelevant or ill-founded:

- Irrelevant: the Castor shareholders' agreement provisions would have been irrelevant if Widdrington had not invested in Castor.
- Ill-founded: had the audited financial statements not been misstated, and had C&L's opinion as the fair market value of Castor's shares been correct, there are no provisions in this shareholders' agreement that would have precluded Widdrington from disposing of his shares in Castor, pursuant to its terms.

Claim of $1,250,000

[3583] Widdrington would never have been involved with Castor, and would never have been in the position to approve the dividends, but for his reliance on the negligently issued audited financial statements, valuation letters and Certificates for Legal-for-Life Opinions.

[3584] Widdrington trusted that the audited financial statements fairly presented Castor's true financial position, and he reasonably relied on them being confident that Castor was in a position to pay dividends when, unbeknownst to him, Castor was hopelessly insolvent.

[3849] 1998 CanLII 12757 (QC C.A.)

[3585] While it might not have been the case for other directors of Castor who had a different and more extensive knowledge of Castor's affairs, the Court finds that Widdrington did discharge his duties as a director of Castor: Widdrington acted with care and due diligence in the circumstances.

[3586] However, and as Justice Louise Lemelin wrote and explained in her judgment rendered on July 30, 2008, the Bankruptcy and Insolvency Act at the time (1990-1991) did not provide a defence based on the reasonable belief of the company's ability to pay even though a director's approval of dividends was based on audited financial statements.

[3587] Facing a claim of more than $15 million and knowing he might be the only Canadian defendant having assets in Canada, Widdrington chose to finalize a settlement with the Trustee.

[3588] Defendants had the burden to prove that the settlement was unreasonable in order to disprove it as a head of damages. They failed to discharge that burden. As a matter of fact, the Court concludes that the settlement that intervenes was more than reasonable, in all circumstances.

[3589] Rather than risking the accumulation of his losses, Plaintiff reasonably decided to settle with the Trustee.[3850]

[3590] Whether Widdrington could have raised a valid defence is not relevant. It was Defendants' obligation to make proof that the settlement was unreasonable in order to disprove it as a head of damages. As Justice Gomery explained when he rejected a defendants' contestation to a plaintiff's payment of a tax reassessment on account of their negligence:

> Defendants argue that if he had contested the reassessment, he would eventually have succeeded in having it overturned. No expert opinion to that effect has been produced, the tax decision cited by Defendants refers to a different development, and no evaluation of the legal cost of lengthy litigation before the relevant tribunals has been made. In all of the circumstances the Court is not satisfied that Plaintiff was in error in accepting to pay the reassessment.[3851]

[3850] See 1479 CCQ.; *McGregor On Damage,* 16th ed. (London: Sweet & Maxwell, 1997) at 285-287, *Gallop v. Abdoulah*, (2008) SKCA 29 (CanLII), at 36; *Malpass v. Morrison,* [2004] O.J. No. 4596, aff'd by the Court of Appeal, *Malpass v. Morrison*, [2006] O.J. No. 719.

[3851] *Laidley c. Kovalik* [1992] R.R.A. 501, at 46 (C.S.), aff'd by the Court of Appeal *Laidley c. Kovalik*, 1994 CanLii 5878 (QC.C.A).

The Trustee's law suit

[3591] When Justice Carrière decided on February 20, 1998 to select the Widdrington case to proceed to trial, while the other Castor-related actions were suspended, he was fully aware of the action instituted by the Trustee. As a matter of fact, this action is one of the active files that appears on Annex A of the trial minutes of March 12, 2008 and to which the present judgment applies on all common issues.

[3592] That decision was not appealed and the issue is now res judicata.

[3593] As stated in *Bélanger* c. *Masson* :

> Il serait illogique que le juge siégeant dans l'affaire civile puisse déclarer irrecevable un recours dont la poursuite a été spécifiquement autorisée par un autre juge de la même Cour dans l'affaire de la faillite impliquant la défenderesse. Ainsi, **dans l'hypothèse où il y aurait effectivement une forme de litispendance, elle est autorisée spécifiquement par le jugement** du juge Verrier, jugement non porté en appel.[3852] (our emphasis)

[3594] Defendants cannot, 13 years later, successfully allege, as they do, that "*The Trustee's action precedes and pre-empts those of ordinary creditors. If the Trustee's action was successful, Widdrington would receive an amount that cannot be ascertained at present. Therefore, and since Widdrington's damages cannot be definitively determined before the Trustee's action is decided, Widdrington's claim should be dismissed.*"

[3595] The Trustee's claim falls under a different heading of damages than that of Plaintiff.

[3596] In any case, if the Trustee's claim was to encompass the Widdrington's claim, in whole or in part, Defendants would be allowed to argue the issue before the judge hearing and deciding the Trustee's claim and have it resolved.

Joint and several liability

[3597] There were no allegations with respect to the rules governing the liability of individual partners as per Ontario law. As per article 2809 of the Civil Code of Quebec, the Court must apply Quebec law.

[3598] Articles 1854 and 1856 of the *Civil Code of Lower Canada* read as follows:

> **1854**. Partners are not jointly and severally liable for the debts of the partnership. They are liable to the creditor in equal shares, although their shares in the partnership may be unequal.

[3852] [2007] QCCS 850 at para. 12, EYB 2007-115788 (S.C.).

> This article does not apply in commercial partnerships.
>
> **1856.** The liabilities of partners for the acts of each other are subject to the rules contained in the title *Of Mandate*, when not regulated by any article in this title.

[3599] Articles 1054, 1106 and 1731 of the *Civil Code of Lower Canada*, relevant to the issue, read as follows:

> **1054.** He is responsible not only for the damage caused by his own fault, but also for that caused by the fault of persons under his control and by things under his care; (...)
>
> The responsibility attaches in the above cases only when the person subject to it fails to establish that he was unable to prevent the act which has caused the damage.
>
> Masters and employers are responsible for the damage caused by their servants and workmen in the performance of the work for which they are employed.
>
> **1106**. The obligation arising from the common offence or quasi-offence of two or more persons is joint and several.
>
> **1731**. He (the mandatory) is liable for damages caused by the fault of the mandatary, according to the rules declared in article 1054.

[3600] Article 1854 of the Code applies to the partnership's contractual obligations only.[3853]

[3601] Defendants' liability towards Plaintiff is extra contractual. No specific article in the title eleventh of the Code "*Of Partnership*" regulates partnership's extra contractual liability. Therefore, according to article 1856 of the Code, partnership's professional responsibility towards third parties is governed by the rules of mandate.

[3602] Mandators (all of the partners) are liable for the damages caused by the fault of their mandataries (the individual partners) and of their employees (all the persons who worked on the audits) based on article1054 *C.c.*

[3603] Article 1106 *C.c.* applies: the Defendants are jointly and severally liable towards Plaintiff.[3854]

[3853] *Bélisle-Heurtel c. Tardif*, REJB 2000-20086 at para. 182

[3854] *Laidley c. Kovalik*, 1994 CanLII 5878 at 2 (Qc. C.A.); *Verrier c. Malka*, AZ-50401934 (S.C.), aff'd, 1998 CanLII 12884 (Qc. C.A) and *Sumabus inc. c. Daoust*, [1994] J.Q. no. 2667 at para. 42.; *Martel c. Hôtel-Dieu St-Vallier*, [1969] R.C.S. 745; Hervé Roch and Rodolphe Paré, *Traité de Droit Civil du Québec* (Montréal: Wilson Lafleur, 1942) at 402.

Costs

[3604] According to article 466 of the *Code of Civil Procedure*[3855], the Court must rule, in its discretion, on the costs of both the first and the second trial.

Positions in a nutshell

Plaintiff

[3605] Plaintiff urges the Court to render a complete order on court costs pursuant to articles 466 and 477 of the *Code of Civil Procedure*. Apart from taxation, to the extent that the Court determines that a special fee is indicated, the only matter which should be left to a later date shall be the fixing of the quantum of the special fee under section 15 of the tariff.[3856] The issue of the special fee should be dealt with in the judgment, while a subsequent hearing might take place to deal with the quantum of that special fee, if no agreement intervenes.[3857]

[3606] Plaintiff acknowledges that article 273.1 of the *Code of Civil Procedure* foresees the possibility, in exceptional cases or circumstances, to split the decision in an action. However, he argues this should not be done in his file. If judgment was rendered and the issue of costs or some portion of the issue of costs was left to a later date, one might argue that the Court is *functus officio* or one might argue rights to appeal should only be exercised after all issues are decided[3858], including all reliance and damages issues in all the pending cases: Plaintiff certainly wants to avoid such situations.

[3607] Plaintiff says Defendants should be condemned to pay all costs, including fees of all experts, the additional fee, a special fee, all stenographic and judicial fees relating to all examinations in discovery conducted in the Widdrington file, as well as in the Richter file and the files of the other Plaintiffs, where the testimony of various witnesses forms part of the Widdrington file, and all fees, costs and expenses relating to Rogatory Commission examinations.

[3608] Plaintiff argues the fact that arrangements were made to finance the pursuit of the litigation[3859] after the Widdrington case was chosen as "The case", changes nothing. The Court has not to and should not take that into account.

[3855] R.S.Q., c. C-25
[3856] R.R.Q. [1981], c. B-1, r.13
[3857] Representations, October 4, 2010, pp.1-26
[3858] Article 273.2 C.C.P.
[3859] PW-39

[3609] Plaintiff concludes all costs (experts' costs, transcription, etc.) were and had to be incurred to present the Widdrington case, namely as a result of the Defendants' positions and absence of cooperation. Defendants chose to act in such a way; they shall face the consequences of their own doings. Justice and equity require that all costs be part of the costs adjudicated to Widdrington, if the latter succeeds.

[3610] Plaintiff invites the Court to grant the following conclusions[3860]:

THE WHOLE WITH COSTS against the Defendants, including the costs relating to the original inquiry and hearing before the Honorable Justice Paul P. Carrière, which costs shall include the following:

1. a special fee pursuant to section 15 of the Tariff of Judicial Fees (the "Tariff");

2. the additional fee, pursuant to section 42 of the Tariff, based on the amount of the condemnation herein in favour of the Plaintiff, The Estate of the Late Peter N. Widdrington;

3. all costs of Plaintiff's experts; namely, Keith Vance (BDO Dunwoody LLP), Ken Froese (LECG), Lawrence S. Rosen (Rosen & Vettese Ltd.), Stephen A. Jarislowsky, Paul Lowenstein (Canadian Corporate Funding Ltd.), John Kingston (eMerging Capital Corp.) and Earl Cherniak (Lerners LLP), including costs for preparation of reports as well as preparation, assistance and attendance at either or both trials;

4. all costs of examinations on discovery conducted (i) in the present case, (ii), in the case of Richter and Associés Inc. vs. Elliot C. Wightman et als. (500-05-003843-933 (the "Richter Case") where such examinations form part of the present court record by Order of this Court dated January 7, 2008 (the "January 7 Order") and (iii) in any other cases against the Defendants, where the transcripts of which, in whole or in part, were filed into the present record with the authorization of this Court;

5. all costs of rogatory commission examinations conducted in the present case and in the Richter Case, where such latter examinations form part of the present court record pursuant to the January 7 Order;

6. all costs of judicial stamps for various proceedings and subpoenas;

7. all costs and expenses, including travel, lodging, meal and fees, of ordinary witnesses, in accordance with the Tariff;

8. all costs and expenses related to exhibits, in accordance with the Tariff;

[3860] Representations, October 4, 2010, pp. 22-26

9. all costs of translation in respect of the foregoing;

10. all costs of stenography in respect of the foregoing; and

11. all other costs in accordance with the Tariff not herein specifically referred to.

Defendants

[3611] Given that the present judgment has binding effects on all the pending lawsuits (as listed in Annex A of the minutes of trial of March 12, 2008), a unique situation, Defendants argue that the Court should postpone her decision on costs and that she has the power to do so since the Court has a discretion to "*order otherwise*" under section 477 of the *Code of Civil Procedure* and given the inherent powers of the Court. Defendants submit ordering otherwise could be deciding to postpone awarding costs[3861].

[3612] In order to achieve the above, Defendants invite the Court to proceed to a splitting of the action under article 273.1 *C.C.P.*[3862]

[3613] While the judgment rendered in the present file will end the debate on the common issues, Defendants say litigation is far from being finished since debates will continue on individual issues (reliance and damages), on a case by case basis, in the other files. Even if C&L was to be condemned to indemnify Widdrington, if Plaintiffs in the other cases do not discharge their burden of proof on reliance and damages, Defendants argue the court could conclude those cases should be dismissed.

[3614] Defendants plead a huge amount of time and money was invested to defend all claims given their collective financial impact. Had the Widdrington case been the only claim they had to face, Defendants might not have invested as much time and money.

[3615] Without the knowledge of the end results in all cases, Defendants invite the Court to postpone awarding costs.

[3616] Alternately, if the Court sees fit to adjudicate on costs, Defendants urge the Court to act prudently. Defendants suggest the Court should grant costs on a prorata basis: since Widdrington's claim represents 0.4 of 1% of the total amount claimed, Widdrington should be granted costs on that basis. If the other Plaintiffs succeed, the same mechanics will apply – if any of the other Plaintiffs do not succeed, justice will be done to the Defendants.

[3861] Representations, October 4, 2010, pp. 26-43
[3862] Representations, October 4, 2010, p. 43

Analysis and Conclusion

Applicable law

[3617] The Court was called upon to hear the Widdrington case re-entered on the roll pursuant to article 464 of the *Code of Civil Procedure*.

[3618] Given articles 466 and 477 of the *Code of Civil Procedure,* the Court shall rule on the costs of the first trial (trial that took place before Justice Paul Carrière between September 1998 and October 2006) and of the second trial (trial that took place before her between January 14, 2008 and October 4, 2010).

> **466. The judge called upon to continue a case** or matter assigned to him or **to hear a case or matter re-entered on the roll pursuant to articles 464 and 465 may,** with the consent of the parties, limit the proof to the transcription of the stenographic notes, provided that, where he considers the notes to be insufficient, he recalls a witness or requires any other proof.
>
> **He shall rule on the costs, including those relating to the original inquiry and hearing, according to circumstances**, and may, in addition, take any other measure he considers fair and appropriate. Where, for the purposes of the first paragraph, the stenographic notes must be transcribed, the transcription costs shall be paid by the Government unless the judge orders otherwise, in particular, when the recourse is manifestly unfounded or frivolous and excessive or dilatory. (our emphasis)
>
> **477. The losing party must pay all costs**, including the costs of the stenographer, **unless** by decision giving reasons the court reduces or compensates them, or orders otherwise.
>
> As well, the court may, by a decision giving reasons, reduce the costs relating to experts' appraisals requested by the parties, particularly if, in the opinion of the court, there was no need for the appraisal, the costs are unreasonable or a single expert's appraisal would have been sufficient. (...) (our emphasis)

[3619] As written in article 477, the losing party must pay all costs unless the court orders otherwise by decision giving reasons. Since ordering otherwise is an exception to a general rule, the burden rested on the Defendants to convince the Court that she should do so taking account all the circumstances of the case. Defendants have failed to discharge this burden.

[3620] As article 15 of the tariff provides, "*The Court may, upon request or ex officio, grant a special fee, in addition to all other fees, in an important case*".[3863]

Defendants' suggestion: postponement of ruling

[3621] As the Defendants suggested, the Court might have jurisdiction to postpone awarding costs.

[3622] At first glance, the following words of Justice André Forget, writing for the majority of the Court of Appeal in *Pearl c. Gentra*, supports Defendants' position that awarding costs could be done in a second step, even maybe without splitting the action under article 273.1 *C.C.P.*:

> On doit, dans un premier temps, examiner l'article 477 C.p.c.; cet article, quant aux dépens, permet au juge «d'en décider autrement».
>
> On connaît la pratique souvent suivie par les tribunaux qui consiste à faire dépendre l'adjudication des dépens d'une démarche future: «frais réservés» ou «frais à suivre».
>
> Dans le domaine des procédures frivoles ou manifestement mal fondées, ici en cause, le législateur a reconnu la possibilité de procéder en deux étapes. L'article 75.2 C.p.c., récemment adopté, permet au tribunal de «réserver, dans le délai et aux conditions qu'il détermine, le droit de s'adresser par requête au tribunal compétent pour réclamer le montant des dommages-intérêts».
>
> De même, en appel, l'article 524 C.p.c. permet à notre Cour, si un appel est déclaré dilatoire et abusif et si les dommages-intérêts ne sont pas liquidés ou admis, d'autoriser l'intimé à s'adresser à la Cour supérieure ou à la Cour du Québec pour les réclamer.
>
> Le premier juge ne s'apprête donc pas à réviser une décision préalablement rendue, mais plutôt à trancher une demande sur laquelle il n'a pas encore statué.
>
> Gentra recherchait une condamnation aux dépens contre Tisserand et une autre contre Pearl & Associés. Le juge de la Cour supérieure a disposé de la première demande et a reporté l'audition sur la deuxième. Je ne peux voir quelle règle fondamentale l'empêcherait de procéder ainsi. (...)
>
> **Le pouvoir d'en ordonner autrement (477 C.p.c.), en matière de dépens, me semble suffisant pour donner compétence au premier juge pour agir comme il l'a fait, surtout s'il estimait que l'intimée subirait une injustice grave en prolongeant l'audition sur la demande d'injonction permanente.**

[3863] *Banque canadienne impériale de Commerce c. Aztec Iron Corp.*, [1978] C.S. 266, [1978] R.P. 385, EYB 1978-145103, J.E. 78-94 (C.S.); Marc LÉGER, *Mémoire de frais, Législation annotée*, 3e Edition, Éditions Yvon Blais

> Avec respect pour l'opinion contraire, j'estime que le premier juge, **en prononçant** une condamnation aux dépens contre Tisserand **et en reportant** sa décision sur la demande visant Pearl & Associés, **a «décidé autrement»** conformément à l'article 477 C.p.c.
>
> Je n'ignore pas qu'une simple «réserve de droits» n'ajoute généralement rien aux droits de la partie, mais, en l'espèce, lorsqu'on prend connaissance des motifs du premier juge, on voit bien qu'il a refusé de se prononcer immédiatement sur une demande dont il était saisi et qu'il a reporté l'audition pour permettre à Pearl & Associés de se défendre adéquatement.
>
> La procédure suivie par le premier juge ne me paraît donc pas contrevenir aux règles du Code de procédure civile; toutefois, il existe, selon moi, une raison plus fondamentale pour justifier la compétence du premier juge à se saisir et à disposer de la requête qui lui est présentée, c'est son «pouvoir inhérent»[3864]. (our emphasis)

[3623] However, in the same case, Justice Robert Pidgeon (as he then was), dissenting, wrote:

> Je conçois que l'amplitude de la compétence inhérente de la Cour supérieure autorise certains redressements judiciaires mais cette compétence porte une limitation temporelle infranchissable: la prononciation du jugement met un terme au conflit et marque la fin du contrat judiciaire des parties qui inclut l'adjudication des dépens[3865].

[3624] Defendants also find support for their proposition that adjudicating on costs might be done in a second step in the following judgments of our court:

- *Centre de santé et de services sociaux de Sept-Îles c. P.T.*, [2008] QCCS, 5415;
- *N-Xpress Canada Inc. (Syndic de)* AZ-50309107, B.E. 2005BE-620

[3625] The issue and the Defendants' proposition that it could be done are interesting legal questions. They are to be left for another day.

[3626] More than ever and in the circumstances of the present case, splitting the action must be ruled out.

[3627] Plaintiff's point of view that adjudicating on costs is a matter of fairness, equity and justice must prevail.

[3864] *Pearl* c. *Gentra Canada Investments Inc.* AZ-98011477, J.E. 98-1260, [1998] R.L. 581, motion for leave to appeal at the Supreme Court dismissed (C.S. Can., 1999-02-18), 26807

[3865] *Pearl c. Gentra Canada Investments Inc.* AZ-98011477, J.E. 98-1260, [1998] R.L. 581, motion for leave to appeal at the Supreme Court dismissed (C.S. Can., 1999-02-18), 26807

Defendants' alternate proposition: a prorata ruling

[3628] The Court dismisses the Defendants suggestion that she should grant costs on a *prorata* basis.

[3629] To succeed, Plaintiff had to prove fault, damage and causality. The burden of proof rested on him as Defendants repeatedly reminded the Court and his counsel. The case was complex and establishing the relevant facts without resorting to numerous admissions was quite a challenge. Defendants elected to defy Plaintiff to do it, as it was their right[3866]; it is just fair that they live with the consequences of the choice they made now that Plaintiff has succeeded.

[3630] Plaintiff had no choice but to resort to expert testimonies in numerous and various fields of expertise. Plaintiff had to ask those experts to deal with the situation, without the benefit of a series of clear uncontested facts or admissions. As the Court writes at paragraph 21 of this judgment, "*Writing clear and complete but concise reasons represents a titanic challenge*". Each of the experts that appeared before the Court had to face a similar challenge, Plaintiff's experts as well as Defendants' experts.

[3631] With the benefit of hindsight, one could think or suggest that the case should have unwound differently.

[3632] However, relying on hindsight is discarded. This case started in 1994 and more than 50% of the first trial took place at times when our rules of civil procedure did not include the following specific provisions (which are now part of our Code since 2003) relating to trial management, to proportionality and to an active role of the judge to ensure proper management.

> **4.1** Subject to the rules of procedure and the time limits prescribed by this Code, the parties to a proceeding **have control of their case and must refrain from** acting with the intent of causing prejudice to another person or behaving in an excessive or unreasonable manner, contrary to the requirements of good faith.
>
> The **Court sees to the orderly progress** of the proceeding **and intervenes** to ensure proper management of the case.
>
> **4.2** In any proceeding, the parties **must ensure that** the proceedings they choose are **proportionate, in terms of the costs and time required**, to the nature and ultimate purpose of the action or application and to the complexity of the dispute; the same applies to proceedings authorized or ordered by the judge. (our emphasis)

[3866] In compliance with articles 6 and 7 of the *Quebec Civil code* and compliance with articles 4.1, 4.2 and 4.3 of the *Code of Civil Procedure*

[3633] The present judgment ends the debate on the common issues. Those issues were the ones for which most of the experts' costs were incurred. Again, in assessing the costs of expert evidence, the Court must be careful as the Court of Appeal said recently in *Michaud c. Équipements ESF inc.*[3867]

[3634] Neither the Plaintiff nor the Defendants have challenged the quantum of the professional services rendered by the experts that appeared before the Court even though all invoices were introduced in evidence. Comparing one invoice with the other, comparing Plaintiff experts' invoices with Defendants experts' invoices, confirms time spent and hourly rates are alike.

[3635] There is not a doubt that the reports and the testimonies of the Plaintiff's experts were useful. In fact, in the circumstances of the case, they were necessary. Therefore the Court finds that all experts' costs should be part of the costs adjudicated to Plaintiff.

[3636] This case is an important case: it satisfies many, if not all of the twenty-three criteria developed in the case of *Banque canadienne impériale de Commerce c. Aztec Iron Corp.*[3868]: Plaintiff is well founded to request a special fee under article 15 of the tariff. While acknowledging the right to a special fee will form part of the conclusions of this judgment, establishing the quantum will only be done at a later date and at the written request of the parties, if they cannot agree and as suggested.

[3637] Defendants say litigation is far from being finished since debates will continue on individual issues (reliance and damages), on a case by case basis, in the other files. They might be right. They might be wrong. They have to remember that litigating all the other files is only one of multiple options. Now that the litigants have on hand answers to all common issues, resolving the remaining conflicts otherwise is clearly an option (for example, resorting to alternative modes of conflict resolution).

[3638] Now that the answers to common issues are known, Defendants argue it could still happen that a court will dismiss a plaintiff's claim in the pending cases, if the plaintiff does not discharge his or her burden to prove damages or reliance, and they are right. However, it does not justify this Court to reduce the costs in the present file even though it might allow the Defendants to claim costs in any of the pending files, a question left for further adjudication by the judge who will be hearing the case.

Conclusion

[3639] The Court sees no reason why she should exercise her discretion in order to mitigate costs. Plaintiff's position prevails: the Court grants the conclusions he has suggested, which are reproduced hereinabove.

[3867] *Michaud c. Équipements ESF inc.* [2010] QCCA 2350, see namely paragraphs 98 and following - Justice France Thibault discussing adjudication on costs of experts and hindsight

[3868] [1978] C.S. 266, [1978] R.P. 385, EYB 1978-145103, J.E. 78-94 (C.S.);

FOR THESE REASONS, THE COURT:

On common issues

DECLARES that:

- the audited consolidated financial statements of Castor for 1988 are materially misstated and misleading;
- the audited consolidated financial statements of Castor for 1989 are materially misstated and misleading;
- the audited consolidated financial statements of Castor for 1990 are materially misstated and misleading;
- C&L failed to perform their professional services as auditors for 1988 in accordance with the generally accepted auditing standards ("GAAS");
- C&L failed to perform their professional services as auditors for 1989 in accordance with GAAS;
- C&L failed to perform their professional services as auditors for 1990 in accordance with GAAS;
- C&L issued various other faulty opinions relating to Castor's financial position during 1988 (valuation letters and certificate for Legal for Life Opinion);
- C&L issued various other faulty opinions relating to Castor's financial position during 1989 (valuation letters and certificate for Legal for Life Opinion);
- C&L issued various other faulty opinions relating to Castor's financial position during 1990 (valuation letters and certificate for Legal for Life Opinion) ;
- C&L issued various faulty opinions relating to Castor's financial position during 1991 (valuation letters and certificate for Legal for Life Opinion);
- The governing law is Quebec civil law;

Specifically on Plaintiff's claim

CONDEMNS the Defendants to pay jointly and severally to the Plaintiff the amount of two million six hundred and seventy-two thousand nine hundred and sixty dollars ($2,672,960.00) together with interest and the additional indemnity from the date of service of the statement of claim;

THE WHOLE WITH COSTS against the Defendants, including the costs relating to the original inquiry and hearing before the Honorable Justice Paul P. Carrière, which costs shall include the following:

- A special fee pursuant to section 15 of the Tariff of Judicial Fees (the "Tariff");
- The additional fee, pursuant to section 42 of the Tariff, based on the amount of the condemnation herein in favour of the Plaintiff, The Estate of the Late Peter N. Widdrington;
- All costs of Plaintiff's experts; namely, Keith Vance (BDO Dunwoody LLP), Ken Froese (LECG), Lawrence S. Rosen (Rosen & Vettese Ltd.), Stephen A. Jarislowsky, Paul Lowenstein (Canadian Corporate Funding Ltd.), John Kingston (eMerging Capital Corp.) and Earl Cherniak (Lerners LLP), including costs for preparation of reports as well as preparation, assistance and attendance at either or both trials;
- All costs of examinations on discovery conducted (i) in the present case, (ii), in the case of Richter and Associés Inc. vs. Elliot C. Wightman et als. (500-05-003843-933 (the "Richter Case") where such examinations form part of the present court record by Order of this Court dated January 7, 2008 (the "January 7 Order") and (iii) in any other cases against the Defendants, where the transcripts of which, in whole or in part, were filed into the present record with the authorization of this Court;
- All costs of rogatory commission examinations conducted in the present case and in the Richter Case, where such latter examinations form part of the present court record pursuant to the January 7 Order;
- All costs of judicial stamps for various proceedings and subpoenas;
- All costs and expenses, including travel, lodging, meal and fees, of ordinary witnesses, in accordance with the Tariff;
- All costs and expenses related to exhibits, in accordance with the Tariff;
- All costs of translation in respect of the foregoing;

- All costs of stenography in respect of the foregoing; and
- All other costs in accordance with the Tariff not herein specifically referred to.

Marie St-Pierre, S.C.J.

PLAINTIFF

Me Avram Fishman
Me Leonard W. Flanz
Me Mark Meland
Me Gilles Paquin
Me Margo Siminovitch
Me Tina Silverstein
Me Nicolas Brochu
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Me Véronique Ranger (pour Me Greenstein)
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Avocat conseil Chrysler
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Me Yvan Bolduc
Me Serge Gaudet
Me Tibor Holländer
Me Max R. Bernard
Me Guy Sarault
Me Marie-Josée Hogue
Me Sophie Gallizioli
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CANADA
PROVINCE OF QUEBEC
DISTRICT OF MONTREAL

NO: 500-05-001686-946

Estate of late Peter N. Widdrington
Plaintiff
c.
Elliot C. Wightman et al
Defendants

SCHEDULE 1

Alphabetical list of names, abbreviations

and main technical expressions

Schedule 1

Alphabetical list of names, abbreviations and main technical expressions

A

ACC	Airport Corporate Centre
Alksnis	Leonard Alksnis
AWPs	Audit working papers

B

Banziger	Edwin Banziger
Binch	James Binch
Blake	Harold James Blake
BMO	Bank of Montreal
BNP	Banque nationale de Paris

C

CA	Chartered accountant
Campion	John Campion
Camrost	Camrost Office Developments (Lakeshore) Limited
CBICA	Canadian and British Insurance Companies Act
CBV	Chartered business valuator
CCF	Crédit commercial de France
CCLC	Civil Code of Lower Canada

CDC	Canada Development Corporation
CFAG	Castor Finance AG
CFO	Chief financial officer
Cherniak	Earl A. Cherniak
CHIBV & CHINBV	CH International Netherlands BV
CHIF & CHIF NV	CH International Finance NV
CHII	CH Ireland Inc.
CHIO	CH International Overseas Ltd.
CHL	Castor Holding Limited
CIBC	Canadian Imperial Bank of Commerce
CICBV	Canadian Institute of Chartered Business Valuators
C&L	Coopers & Lybrand or Coopers
Chur	Chur Investments Limited
CICA	Canadian Institute of Chartered Accountants
CPA	Certified Public Accountant
CSH	Calgary Skyline Hotel or Calgary Skyline
Cunningham	William P. Cunningham

D

David Smith	David T. Smith
Dragonas	George Dragonas
DT Smith	DT Smith group of companies

E

Edper	Edper Investments Ltd.

F

FCBV	Fellow chartered business valuator
FICAN	First Interstate Bank of Canada
Fitzsimmons	Fred Fitzsimmons
Froese	Kenneth Froese

G

GA	General appraisal
GAAP	Generally accepted accounting principles
GAAS	Generally accepted auditing standards
Gambazzi	Marco Gambazzi
G\L	General ledger
Global	Global Management Limited
Goodman	Russell Goodman
Goulakos	Socrates Goulakos
Gourdeau	Bernard Gourdeau
Gross	Ernst Gross

H

Hajiroussos	Antonio Hajiroussos
Hercules	*Hercules Managements Ltd.* v. *Ernst & Young*

Hughes report	R. W. Hughes & Associates Inc.

J

Jarislowsky	Stephen A. Jarislowsky
JE#6	Journal entry number 6
JE#12	Journal entry number 12
Jet Lease	Jet Lease 900
Johnson	Clifford Johnson
Jurg Bänziger	Jurg Bänziger

K

Karl	Christa Karl
Kingston	John Kingston
KK	Konto kurrents
KVWIL	KVW Investment Limited

L

Labatt	John Labatt Limited
Lajoie	Alain Lajoie
Lakeland	Lakeland Inc.
Lambert	Lambert Securities Inc.
Lapointe	Alain Lapointe
Lee	Soo Kim Lee
LEQ	Loan evaluation questionnaires

Levi	Phillip Levi
Lincoln	Lincoln North & Company Ltd.
LIQ	Loan information questionnaires
LLP	Loan loss provision
Lowenstein	Paul J. Lowenstein
LTV	Loan to value ratio

M

Mackay	Barry Mackay
MAPs	Matters for attention of partners
MEC	Montreal Eaton Center
Mellon	Mellon Bank Canada
MLV	Maple Leaf Village
MLVII	Mapel Leaf Village Investments Inc.
Morrison	Donald C. Morrison
Moscowitz	James Moscowitz
Mullins	R. B. Mullins

O

O'Connor	Ingrid O'Connor
OSH	Ottawa Skyline Hotel

P

Petra	Petra Investments Limited
PKF	Pannell Kerr Forster
PKF Report (1988)	Pannell Kerr Forster Market Position Study
Prikopa	Heinz Prikopa
Prychidny	Walter Prychidny

R

Rancourt	Cynthia Rancourt
Renaud	Christine Renaud
Rogoff	Rogoff & Company
Ron Smith	Ronald Smith
Rosen	Lawrence S. Rosen
RPTs	Related party transactions

S

SAAE	Sufficient appropriate audit evidence
SCFP	Statement of changes in financial position
SCNIA	Statement of changes in Net Investment Assets
Selman	Donald Selman
Simon	Manfred Simon
Skyeboat	Skyeboat Investments Ltd.
Sloppin	Sloppin Investments Limited

Skyline 80	Skyline Hotels (1980)
Skyview	Skyview Hoteld Limited
Stolzenberg	Wolfgang Stolzenberg
Strassberg	Ira Strassberg

T

Taylor	George Taylor
TMF	Trust Management and Finance
The Triumph	The Toronto Skyline Triumph
Tooke	Ruth Tooke
Topven	Topven Holdings Ltd.
Topven 88	Topven Holdings (1988) Inc.
Trinity	Trinity Capital Corporation
TSH	Toronto Skyline Hotel
TWTC	Toronto World Trade Center
TWTCI	Toronto World Trade Centre Inc.
TWTCLP	Toronto World Trade Centre Limited Partnership
TWDC	Toronto Waterfront Development Corp.

V

Vance	Keith Vance
VTB	Vendor Take Back mortgage

W

WEM	West Edmonton Mall
Wersebe	Karsten Von Wersebe
Whiting	David Whiting
Widdrington	Peter N. Widdrington
Wightman	Elliot Wightman
Wood	Bill Wood
Wost group or WOST group	Wost group of companies

Y

YHAL	York-Hannover Amusement Ltd.
YHDHL	York-Hannover Developments Holdings Ltd.
YHDL	York-Hannover Developments Ltd.
YHHI	YHH Investments
YHHL	York-Hannover Holdings Ltd.
YHHL	York-Hannover Hotels Ltd.
YHHHL	York-Hannover Hotels Holdings Ltd.
YHLP	York-Hannover Leisure Properties Ltd.
YH Group	York Hannover companies
YH Hotels	York-Hannover Hotels

Z

Zampelas	Michael Zampelas

166505	166505 Canada Inc.
321351	321351 Alberta Ltd.
594369	594369 Ontario Inc.
606752	606752 Ontario Ltd.
607670	607670 Ontario Inc.
612044	612044 Ontario Ltd.
687292	687292 Ontario Ltd.
696604	696604 Ontario Ltd.
705743	705743 Ontario Ltd.
752608	752608 Ontario Limited
97872	97872 Canada Inc.

CANADA
PROVINCE OF QUEBEC
DISTRICT OF MONTREAL

NO: 500-05-001686-946

Estate of late Peter N. Widdrington
Plaintiff

c.

Elliot C. Wightman et al
Defendants

SCHEDULE 2

Detailed Table of Contents

THE LIABILITY ISSUE 677

CANADA
PROVINCE OF QUEBEC
DISTRICT OF MONTREAL

NO: 500-05-001686-946

Estate of late Peter N. Widdrington
Plaintiff
c.
Elliot C. Wightman et al
Defendants

SCHEDULE 3

Annex A:

Pending lawsuits

Trial minutes

March 12, 2008

Plaintiff	Court No	Amount of claim	Law firm / lawyer
ACTIVE FILES			
Estate of Peter N.T. Widdrington	500-05-001686-946	$ 2,672,960.00	FISHMAN FLANZ MELAND PAQUIN Mes Leonard Flanz, Avram Fisman, Mark Meland 1250 René-Lévesque Ouest Suite 4100 Montréal, Québec, H3B 4W8
Rabom, Smiley Jr.	500-05-001676-947	$ 1,252,944.00	LANGLOIS KRONSTRÖM DESJARDINS Me Raynold Langlois
Adelaide Capital Corporation	500-05-002033-940	$ 9,162,798.65	FISHMAN FLANZ MELAND PAQUIN Mes Leonard Flanz, Avram Fisman, Mark Meland
Arab Banking Corporation Daus & Co. GmbH	500-05-002564-936	$ 14,784,772.79	
AIB Capital Markets PLC	500-05-002564-936	$ 7,981,850.58	
Banco Aleman Platina SA	500-05-002564-936	$ 2,799,515.01	
Bankhaus Aufhauser (BHA) and Bayerische Landesbank Girozentrale (BLG)	500-05-002564-936	$ 18,774,862.16	
Bankhaus Lampe KG (formerly Bankhaus Hermann Lampe KG (BHL)	500-05-002564-936	$ 4,833,268.09	
Dexia Banque Internationale à Luxembourg SA (formerly Banque Internationale à Luxembourg SA)	500-05-002564-936	$ 9,257,482.20	
Bayerische Hypo und Vereinbank AG(formerly Bayerische Vereinsbank AG (BV)	500-05-002564-936	$ 5,654,372.66	
ING bank Deutschland AG (formerly ING BHF-BANK Aktiengesellschaft (BHF)	500-05-042847-986	$ 48,503,322.31	FISHMAN FLANZ MELAND PAQUIN Mes Leonard Flanz, Avram Fisman, Mark Meland
DZ Bank AG (Formerly DG Bank)	500-05-042848-984	$ 16,499,551.93	
Deutsche Postbank AG (formerly Deutsche Siedlungs- Und Landesuntenbank)	500-05-002564-936	$ 11,192,650.78	
Frankfurter Bankgesselschaft AG	500-05-002564-936	$ 4,584,735.83	
Hauck & Aufhauser Privatbankiers KGaA (formerly Georg Hauck & Sohn Bankiers KgaA)	500-05-002564-936	$ 4,454,924.84	
Ibero Platina Bank Aktiengeschellschaft	500-05-002564-936	$ 8,485,378.15	
Merck Finck & Co. Private Bankers	500-05-002564-936	$ 10,694,508.87	
Gontard & Metallbank AG (formerly Metallbank GmbH)	500-05-002564-936	$ 2,580,934.34	
Sal. Oppenheim Jr. & Cie CgaA	500-05-042849-982	$ 17,403,096.19	
B.C. Central Credit Union	500-05-014013-930	$ 16,729,355.11	FISHMAN FLANZ MELAND PAQUIN Mes Leonard Flanz, Avram Fisman, Mark Meland
Banca Commerciale Italiana of Canada	500-05-014491-938	$ 11,934,248.72	FISHMAN FLANZ MELAND PAQUIN Mes Leonard Flanz, Avram Fisman, Mark Meland
Bankgesellschaft Berlin AG	500-05-002292-942	$ 11,885,506.10	FISHMAN FLANZ MELAND PAQUIN Mes Leonard Flanz, Avram Fisman, Mark Meland
Banque Nationale de Paris (Canada)	500-05-016260-935	$ 8,723,513.62	FISHMAN FLANZ MELAND PAQUIN Mes Leonard Flanz, Avram Fisman, Mark Meland
Banque République Nationale de New York (Canada), Plaintiff in continuance of suit [previously Bank Hapoalim Canada]	500-05-014059-933	$ 6,908,480.81	FISHMAN FLANZ MELAND PAQUIN Mes Leonard Flanz, Avram Fisman, Mark Meland
Banque République Nationale de New York (Canada), Plaintiff in continuance of suit [previously Bank Leumi Le-Israel Canada]	500-05-013480-932	$ 4,148,258.45	FISHMAN FLANZ MELAND PAQUIN Mes Leonard Flanz, Avram Fisman, Mark Meland
Credit Union Central of Saskatchewan	500-05-013560-931	$ 3,681,205.48	FISHMAN FLANZ MELAND PAQUIN Mes Leonard Flanz, Avram Fisman, Mark Meland
RSM Richter Inc.	500-05-003843-933	$ 40,000,000.00	FISHMAN FLANZ MELAND PAQUIN Mes Leonard Flanz, Avram Fishman and Mark Meland
Bandigo Investments et al. [One claim]	500-05-016686-931	$ 829,750.53	ROBINSON SHEPPARD SHAPIRO Me Charles Flam Stock Exchange Tower 800 Place Victoria, Suite 4700 Montréal, Québec H4Z 1H6

Plaintiff	Court No	Amount of claim	Law firm / lawyer
Marvin Company Ltd.	500-05-016686-931	$ 849,909.25	ROBINSON SHEPPARD SHAPIRO Me Charles Flam
Monarch Investments SA	500-05-016686-931	$ 452,680.59	ROBINSON SHEPPARD SHAPIRO Me Charles Flam
Pentafin Ltd.	500-05-016686-931	$ 738,660.89	ROBINSON SHEPPARD SHAPIRO Me Charles Flam
Ticinfin Anstalt	500-05-016686-931	1,871,519.07	ROBINSON SHEPPARD SHAPIRO Me Charles Flam
Arthur Köser GmbH & Co. KG	500-05-007307-943	$ 2,899,529.79	ROBINSON SHEPPARD SHAPIRO Me Charles Flam
Christensenn, Uwe	500-05-002844-932	$ 8,293,651.88	ROBINSON SHEPPARD SHAPIRO Me Charles Flam
Gambazzi, Dott. Marco	500-05-016687-939	$ 8,291,062.23	ROBINSON SHEPPARD SHAPIRO Me Charles Flam
Geam SA : (NB as per letter dated June 19, 2007, GEAM is bankrupt and the liquidator, PricewaterhouseCoopers SA has neither mandated RSS to continue the suit, nor instructed it to desist.)	500-05-016682-930	$ 6,829,201.01	ROBINSON SHEPPARD SHAPIRO Me Charles Flam
Köser, Marion and Rita	500-05-007306-945	$ 1,902,187.42	ROBINSON SHEPPARD SHAPIRO Me Charles Flam
Mediacommunication SA	500-05-005894-942	$ 11,298,739.00	ROBINSON SHEPPARD SHAPIRO Me Charles Flam
Moon Properties SA	500-05-008819-936	$ 73,933,630.59	ROBINSON SHEPPARD SHAPIRO Me Charles Flam
Orwamar Elablissement	500-05-016683-938	$ 15,852,606.02	ROBINSON SHEPPARD SHAPIRO Me Charles Flam
Woodstock Trading Corp.	500-05-016684-936	$ 1,318,335.78	ROBINSON SHEPPARD SHAPIRO Me Charles Flam
Manolita SA	500-05-017465-939	$ 1,381,012.32	ROBINSON SHEPPARD SHAPIRO Me Charles Flam
DaimlerChrysler Canada Inc.) - [One claim]		$ 37,717,131.00	GOWLING LAFLEUR HENDERSON Mtre Jack Greenstein, 1 Place Ville-Marie, 37th Floor, Montreal, Quebec , H3B 3P4 STIKEMAN, ELLIOTT- counsel Me Stephen Hamilton 1155 René-Lévesque Blvd. West, 40th Floor Montréal, Quebec H3B 3V2
Jointly CIBC Mellon Trust Company as trustee for the Health and Welfare Trust and plaintiff Daimlerchrysler Canada Inc.	500-05-005391-931	$ 21,668,046.00	
Jointly CIBC Mellon Trust Company as trustee for the Pension Funds and Plaintiff DaimlerChrysler Canada Inc.		$ 100,540,421.00	
Jointly CIBC Mellon Trust Company, as trustee for the SUB Trust and Plaintiff DaimlerChrysler Canada Inc.		$ 10,948,037.00	
Von Wersebe, Lüder	500-05-002418-950	$ 845,026.34	Lavery de Billy s.e.n.c.r Me Sylvie Boulanger 1 Place Ville Marie, Bureau 4000 Montreal, Quebec H3B 4M4
	Total active files	$ 614,045,655.38	
INACTIVE FILES			
Crédit Suisse and Crédit Suisse Canada	500-05-007483-938	$ 84,600,000.00	BYERS CASGRAIN
Banca del Gottardo	500-05-010555-942	$ 19,770,539.95	STIKEMAN, ELLIOTT
Banca Unione di Credito	500-05-010554-945	$ 12,997,375.00	STIKEMAN, ELLIOTT
Banque Paribas (Suisse) SA	500-05-010556-940	$ 26,602,908.04	STIKEMAN, ELLIOTT
State Bank of India	500-05-004735-948	$ 1,556,383.58	STIKEMAN, ELLIOTT
Deucher, Adolf H.	500-05-002456-950	$ 101,645.00	STIKEMAN, ELLIOTT
Aktiengesellschaft, Plaintiff in continuance of suit (previously Girocredit Bank Aktiengesellschaft der	500-05-002455-945	$ 14,831,308.19	STIKEMAN, ELLIOTT
Laurentian Bank of Canada	500-05-003929-930	$ 10,335,290.41	STIKEMAN, ELLIOTT
LGT Bank In Liechtenstein Aktiengesellschaft	500-05-010036-943	$ 8,247,681.02	STIKEMAN, ELLIOTT
White, Anne and Arthur	500-05-018272-938	$ 53,821,132.44	STIKEMAN, ELLIOTT
Trevanus Anstalt	500-05-016686-931	$ 1,057,139.20	ROBINSON SHEPPARD SHAPIRO
Bunnemann, Angelika and Klaus	500-05-005893-944	$ 424,248.93	ROBINSON SHEPPARD SHAPIRO
Irwinlown Overseas SA	500-05-015176-934	$ 44,313,463.44	ROBINSON SHEPPARD SHAPIRO
Lorus Associated S.A.	500-05-015177-932	$ 20,570,625.00	ROBINSON SHEPPARD SHAPIRO
Mora Hotel Corp. NV	500-05-016681-932	$ 7,065,462.35	ROBINSON SHEPPARD SHAPIRO
Cardori SA	500-05-016685-933	$ 3,521,502.41	ROBINSON SHEPPARD SHAPIRO
Yosaly Investment Inc.	500-05-017465-939	$ 1,030,440.45	ROBINSON SHEPPARD SHAPIRO

PV 12/03/08 PAGE 12C

Coopers Lybrand
Re: Castor Holdings Ltd.

Plaintiff	Court No	Amount of claim	Law firm / lawyer
Billesberger-Durr, Gabi	500-05-001661-949	$ 483,078.92	LANGLOIS KRONSTRÖM DESJARDINS
Boss, Annie and Walter	500-05-001662-947	$ 263,345.47	LANGLOIS KRONSTRÖM DESJARDINS
Brandhoff, E.	500-05-001663-945	789,146.05	LANGLOIS KRONSTRÖM DESJARDINS
Cantal Anstalt, FL	500-05-001664-943	$ 22,584.48	LANGLOIS KRONSTRÖM DESJARDINS
Coleone Foundation	500-05-001665-940	$ 11,482,263.06	LANGLOIS KRONSTRÖM DESJARDINS
Cumaressen Farelhumby	500-05-001675-949	$ 82,002.39	LANGLOIS KRONSTRÖM DESJARDINS
Deischl, Birgit	500-05-001666-948	$ 114,390.70	LANGLOIS KRONSTRÖM DESJARDINS
Dyckhoff, Gabi	500-05-001667-946	$ 107,810.90	LANGLOIS KRONSTRÖM DESJARDINS
Dyckhoff-Stromeyer, Daniela	500-05-001668-944	$ 1,427,852.47	LANGLOIS KRONSTRÖM DESJARDINS
Fontainbleu Apartment Limited	500-05-001669-942	$ 9,314,948.97	LANGLOIS KRONSTRÖM DESJARDINS
Haenlein, Sabine	500-05-001670-940	$ 80,513.54	LANGLOIS KRONSTRÖM DESJARDINS
Hieber, Liz	500-05-001671-948	$ 93,294.23	LANGLOIS KRONSTRÖM DESJARDINS
I.C.R. Foundation	500-05-001672-946	$ 201,777.95	LANGLOIS KRONSTRÖM DESJARDINS
Mayer, Lothar	500-05-001673-944	$ 294,222.41	LANGLOIS KRONSTRÖM DESJARDINS
Notafinanz Anstalt	500-05-001674-942	$ 171,291.31	LANGLOIS KRONSTRÖM DESJARDINS
Reichel, Rosmari	500-05-001677-945	$ 93,429.52	LANGLOIS KRONSTRÖM DESJARDINS
Schmitz, Gerd	500-05-001678-943	$ 163,049.62	LANGLOIS KRONSTRÖM DESJARDINS
Schwarze, Renate	500-05-001679-941	$ 43,771.75	LANGLOIS KRONSTRÖM DESJARDINS
Scuba Foundation	500-05-001680-949	$ 54,727.99	LANGLOIS KRONSTRÖM DESJARDINS
Seidl-Beaucamp, Marita	500-05-001681-947	$ 175,124.44	LANGLOIS KRONSTRÖM DESJARDINS
Slielner, Marie	500-05-001682-945	$ 67,415.56	LANGLOIS KRONSTRÖM DESJARDINS
Stromeyer, Hilmar	500-05-001683-943	$ 2,475,307.31	LANGLOIS KRONSTRÖM DESJARDINS
Stromeyer, Martin A., Hans and Walther	500-05-002803-946	2,637,647.69	LANGLOIS KRONSTRÖM DESJARDINS
Thaller, Sandra	500-05-001684-941	$ 185,458.93	LANGLOIS KRONSTRÖM DESJARDINS
Unionmatex GmbH	500-05-001685-948	$ 16,057,267.95	LANGLOIS KRONSTRÖM DESJARDINS
Wiedner, Lucy	500-05-001687-944	$ 52,709.50	LANGLOIS KRONSTRÖM DESJARDINS
Wynendaël Foundation	500-05-001688-942	$ 2,873,277.44	LANGLOIS KRONSTRÖM DESJARDINS
Raborn, Bernice Louise	500-05-001676-947		LANGLOIS KRONSTRÖM DESJARDINS
Caisse Centrale Desjardins	500-05-012357-933	$ 17,140,072.65	FISHMAN FLANZ MELAND PAQUIN
Gan Canada / Gan General Ins. Co.	500-05-002030-946	$ 2,472,445.20	FISHMAN FLANZ MELAND PAQUIN
Gebr. Westhoff GmbH & Co. ROH & Rosikaffee KG (Berlin)	500-05-002031-944	$ 5,339,120.32	FISHMAN FLANZ MELAND PAQUIN
Hongkong and Shanghai Banking Corporation Ltd.	500-05-007400-938	$ 21,320,819.68	FISHMAN FLANZ MELAND PAQUIN
Industrial Bank of Japan (Canada)	500-05-002032-942	$ 5,080,710.52	FISHMAN FLANZ MELAND PAQUIN
Roynat Inc.	500-05-013061-930	$ 9,883,984.80	FISHMAN FLANZ MELAND PAQUIN
Société Générale (Canada)	500-05-011477-930	$ 22,136,911.36	FISHMAN FLANZ MELAND PAQUIN
	Total inactive files	$ 444,028,920.49	

CANADA
PROVINCE OF QUEBEC
DISTRICT OF MONTREAL

NO: 500-05-001686-946

Estate of late Peter N. Widdrington
Plaintiff
c.
Elliot C. Wightman et al
Defendants

SCHEDULE 4

Information: Defendants

PAGE: 789

De : "Gaudet, Serge (Heenan Blaikie)" <SGaudet@Heenan.ca>
Destinataire : <pwcew@judex.qc.ca>
CC : "Gilles Paquin" <gpaquin@ffmp.ca>, "Jack Greenstein" <Jack.greenstein@go...
Date : 2010-04-28 12:56
Objet : Lettre à Madame la juge St-Pierre
Pièces jointes : Lettre a Madame la juge St-Pierre -28 avril 2010.PDF; Pièces jointes a la lettre du juge - 28 avril 2010.PDF

Voir pièces jointes.

Heenan Blaikie<http://www.heenanblaikie.com/images/email/heenanlogo.jpg>
<http://www.heenanblaikie.com/images/email/heenanline.jpg> Caroline Tremblay
Adjointe de Me Serge Gaudet et
Me Jeremy Wisniewski
Litige/Litigation
HEENAN BLAIKIE S.E.N.C.R.L., SRL / LLP

T 514 846.1212 poste 3629 catremblay@heenan.ca
1250, boul. René-Lévesque Ouest, bureau 2500, Montréal (Québec) Canada H3B 4Y1 *
heenanblaikie.com

Heenan Blaikie

PAR COURRIEL

Le 28 avril 2010

L'honorable Marie Saint-Pierre, j.c.s.
Cour supérieure
Palais de justice de Montréal
1, rue Notre-Dame Est, bureau 16.43
Montréal (Québec) H2Y 1B6

Notre référence : 013384-0001

Objet : ***The estate of the Late Peter N. Widdrington***
c. Elliot C. Wightman and als
CS 500-05-001686-946

Serge Gaudet

T 514 846.2293
F 514 921.1293
sgaudet@heenan.ca

1250, boul. René-Lévesque Ouest
Bureau 2500
Montréal (Québec)
Canada H3B 4Y1

heenanblaikie.com

Madame la Juge,

Lors d'une récente séance de gestion, vous avez demandé une liste complète des défendeurs au dossier Widdrington. Veuillez donc trouver ci-joint la liste complète des parties défenderesses dans le cadre de ce dossier, laquelle est à jour. Nous avons comparu pour tous ces défendeurs, sauf à l'égard de la succession de Glenn Wittrien, tel qu'expliqué ci-après.

Selon ce qu'indiquent nos dossiers, seules deux parties défenderesses au présent dossier ont fait l'objet d'avis de changement de statut, suite à leur décès, soit M. Glenn Wittrien et Madame Christine E. Sinclair.

Dans le cas de Mme Sinclair, suite à un jugement ordonnant la continuation de l'instance, nous avons comparu pour M. Alan Smith, en sa qualité d'exécuteur et liquidateur à la succession de Mme Sinclair, et ce, afin de continuer l'instance sur ses

derniers errements valides, selon ce qui est prévu à l'article 261 C.p.c. (tel qu'il se lisait avant le 1er janvier 2003)[1].

Dans le cas de M. Wittrien, un jugement ordonnant la continuation de l'instance a été rendu le 12 décembre 2007, à l'encontre de Madame L.G. Wittrien, en sa qualité d'exécuteur testamentaire de la succession. Cependant, nous n'avons pas produit de comparution au nom de la représentante de la succession, celle-ci ne nous ayant pas donné mandat de le faire, étant donné son intention de mettre la succession en faillite (ce qui fut fait le 25 février 2008). Nous n'avons donc aucun mandat pour représenter la succession de M. Wittrien dans le cadre du présent dossier et ce, depuis la date de l'avis de changement de statut le concernant (1er novembre 2006).

Une copie des documents pertinents est jointe à la présente.

Veuillez agréer, madame la juge, l'expression de nos sentiments distingués.

Heenan Blaikie S.E.N.C.R.L., SRL

Serge Gaudet
SG/ct

P.j.

c.c. Me Gilles Paquin (Fishman Flanz Méland Paquin)
Me Jack Greenstein, c.r. (Gowling Lafleur Henderson)
Me Raynold Langlois (Langlois Kronström Desjardins)
Me Charles E. Flam (Robinson Sheppard Shapiro)
Me Sylvie Boulanger (Lavery De Billy)

HBdocs - 8347152v1

[1] «Dans les cinq jours de leur comparution, les personnes visées par l'ordonnance peuvent soit demander au tribunal de la révoquer ou de la modifier, soit continuer l'instance sur ses derniers errements valides». Cette disposition s'applique à la présente instance (cf. art. 179 de la loi portant réforme du *Code de procédure civile*, L.Q. 2002, c. 7.)

LIST OF DEFENDANTS
[WIDDRINGTON FILE – 500-05-001686-946-]
As of April 28, 2010

ANNEX

RENÉ M. AUBRY
JOHN D. BALL
JEAN BEAUDRY
MARCEL BERTRAND
GEORGES F. FOURNIER
GILLES GAGNON
IAN GERGOVICH
PIERRE GILL
ANDRÉ A. GIROUX
MICHAEL J. HAYES
IAIN D. HUME
SEBASTIEN IANNITELLO
DENIS LANGELIER
BERNARD LAUZON
MICHAEL F. MACEY
ZYGMUNT MARCINSKI
JEAN-GUY MARTIN
PIERRE SECCARECCIA
BERNARD R. SMITH
JACQUES ST-AMOUR
NORAH K. TAYLOR
MICHAEL WHITWORTH
ELLIOT C. WIGHTMAN

Chartered accountants, carrying on business in partnership under the firm name and style of Coopers & Lybrand and Laliberté Lanctôt Coopers & Lybrand, having a place of business at 1170 Peel Street, Suite 330, Montreal, Quebec

and

MICHEL BÉDARD
FRANCOIS BERNIER
WILLIAM G.K. BODEN
DENIS GIRARD
JAQUELIN LÉGER
JEAN PELLETIER

CHRISTIAN ROUSSEAU
MARC SHEEDY
LIONEL VÉZINA

Chartered accountants, carrying on business in partnership under the firm name and style of Coopers & Lybrand and Laliberté Lanctôt Coopers & Lybrand, having a place of business at 2 Place Quebec, Room 536, in the City of Quebec, Province of Quebec

And

ROBERT M. BOSSHARD
SEAN R. CASEY
R. IAN COWAN
ROBERT G. GLENNY
GINO A. SCAPILLATI

Chartered accountants, carrying on business in partnership under the firm name and style of Coopers & Lybrand – Chartered Accountants, having a place of business at 21 King Street West, 2nd Floor, in the City of Hamilton, province of Ontario

And

DAVID E. GRAHAM
BRYAN D. STEWART
TERRANCE G. WICHMAN

Chartered accountants, carrying on business in partnership under the firm name and style of Coopers & Lybrand – Chartered Accountants, having a place of business at 175 Columbia Street West, in the City of Waterloo, Province of Ontario

And

SPENCER H. CLARK
ROBERT B. LEMON
ALLAN A. McDERMID

IAN D. McINTOSH
JOHN M. SAVEL

Chartered accountants, carrying on business in partnership under the firm name and style of Coopers & Lybrand – Chartered Accountants, having a place of business at 275 Dundas Street, in the City of London, Province of Ontario

And

A. JOEL ADELSTEIN
TREVOR J. AMBRIDGE
DAVID H. ATKINS
SHARON BACAL
RONALD B. BLAINEY
HUGH J. BOLTON
J. DOUGLAS BRADLEY
DONALD A. BROWN
HAROLD A. BURKE
RICHARD S. BUSKI
TONY P. CANCELLIERE
DENNIS H. CARTWRIGHT
PAUL G. CHERRY
CHRISTIE J.B. CLARK
GRAHAME J. CLIFF
JAMES S. COATSWORTH
GEOFFREY A. COOKE
WILLIAM J. COTNAM
PAUL W. CURRIE
RICHARD C. CURTIS
KEVIN J. DANCEY
ALEXANDER M. DAVIDSON
ALAN G. DRIVER
J. PETER ECCLETON
H. GLENN FAGAN
BRIAN C. FOLEY
DAVID FORSTER
STEPHEN H. FREEDHOFF
A. RIK GANDERTON
ANTHONY F. GIBBONS
PAUL B. GLOVER
J. BRYAN GRAHAM
GARY J. HASSARD
BRENT D. HUBBARD

ROBERT M.C. HOLMES
BRENDA J. HUMPREYS
ROBERT H. JOHNSON
ROBERT E. LAMOUREUX
PETER K. LANE
DEAN R. LEVITT
ROBERT E. LOWE
C. ANDREW McASKILE
JILL H. McALPINE
ISRAEL H. MIDA
PAUL J. MURPHY
ROBERT J. MUTER
BARRY J. MYERS
GABRIEL NACHMAN
BERNARD J. NISKER
RICHARD C. PETIT
W. DAVID POWER
RICHARD ROHDE
JAMES S. SALOMAN
CHARLES L. SEGUIN
ALAN SMITH, as executor and liquidator of the estate of Christine E. Sinclair
DAVID W. SMITH
ROBERT J. SPINDLER
A. DEAN SUMMERVILLE
MICHAEL A. TAMBOSSO
MICHAEL R. VAN EVERY
DEREK W. WILLIAMS
LAURENCE H. WRAGG

Chartered accountants, carrying on business in partnership under the firm name and style of Coopers & Lybrand – Chartered Accountants, having a place of business at 145 King Street West, in the City of Toronto, Province of Ontario

And

ALAN FREED
RONALD G. JACKSON
JOHN J. LISOWSKI
ALLAN D. LUMSDEN
J. DAVID SCHIJNS
RICHARD A. VICKERS

Chartered accountants, carrying on business in partnership under the firm name and style of Coopers & Lybrand – Chartered Accountants, having a place of business 55 Metcalfe Street, 12th Floor, in the City of Ottawa, Province of Ontario

And

ANTHONY J. PANICCIA
PAUL J. CHARKO
LORIS MACOR

Chartered accountants, carrying on business in partnership under the firm name and style of Coopers & Lybrand – Chartered Accountants, having a place of business at 500 Ouellette Avenue, in the City of Windsor, Province of Ontario

And

RAYMOND A. CADIEUX
ANDRE G. COUTURE
DAVID J. DRYBROUGH
FREDERICK M. FLORENCE
JAMES R. HOLLAND
SERENA H. KRAAYEVELD
DAVID LOEWEN
GERALD F. PYLE
GERALD H. RODRIGUE
CAROL L. STOCKWELL
PAUL D. WRIGHT

Chartered accountants, carrying on business in partnership under the firm name and style of Coopers & Lybrand – Chartered Accountants, having a place of business at 2300 Richardson Building, One Lombard Place, in the City of Winnipeg, Province of Manitoba

And

FRANKLIN M. BALDRY
MONTE F. GORCHINSKI

GERALD P. SCHERMAN

Chartered accountants, carrying on business in partnership under the firm name and style of Coopers & Lybrand – Chartered Accountants, having a place of business at 500 – 123-2nd Avenue South, in the City of Saskatoon, Province of Saskatchewan

And

JUSTIN FRYER
RONALD P. GRATTON
C. ROY KRAKE
JOHN E. LAWRENCE
GERARD A.M. LUIJKX
RODERICK W. MACLEAN
DALE S. MEISTER
WILLIAM E. PATTERSON
BRIAN K. PAWLUCK

Chartered accountants, carrying on business in partnership under the firm name and style of Coopers & Lybrand – Chartered Accountants, having a place of business at 2400 Bow Valley Sq. III, 255-5th Avenue S.W., in the City of Calgary, Province of Alberta

And

A.W. KEITH ANDERSON
DANIEL J. BLOCK
WILLIAM D. BURCH
BARRY L. JAMES
DONALD A. MacLEAN
JOHN A. MacNUTT
MELVIN J. MAJEAN
ALAN D. MARTIN
FREDERICK M. PARTINGTON
JOSEPH F. PRESTON
KENNETH D. RAWSON
N. DAVID ST. PETER
JOHN M. TWEEDLE

Chartered accountants, carrying on business in partnership under the firm name and style of Coopers & Lybrand – Chartered Accountants, having a place of business at 2700 Oxford Tower, 10235 – 101 Street, in the City of Edmonton, Province of Alberta

And

ERIC S.Z. ANDREW
RODNEY C. BERGEN
LENARD F. BOGGIO
JOHN H. BOWLES
DAVID P. BOWRA
CRAIG G. BUSHELL
W. JOHN DAWSON
DARRYL R. EDDY
RODNEY B. JOHNSTON
JOHN C. KAY
PATRICIA J. LAJOIE
JOHN E. LARSEN
LEDFORD G. LILLEY
MARTIN A. LINSLEY
JOHN D. PETERS
PIROOZ POURDAD
GARY D. POWDROZNIK
C. DOUGLAS PROCTOR
PETER J. SPEER

Chartered accountants, carrying on business in partnership under the firm name and style of Coopers & Lybrand – Chartered Accountants, having a place of business at 1111 West Hastings Street, in the City of Vancouver, Province of British Columbia

And

ELAINE S. SIBSON
GARY R. STAFFORD
MARCUS A. WIDE
J. HAP WRIGHT

Chartered accountants, carrying on

business in partnership under the firm name and style of Coopers & Lybrand – Chartered Accountants, having a place of business at 1701 Hollis Street, Suite 1200, in the City of Halifax, Province of Nova Scotia

And

LAWRENCE R. COSMAN
HUGH R. TIDBY
R. DALE URQUHART
PETER WILSHAW
Ms. L.G. Wittrien in her capacity as executor of the Estate of GLENN L. WITTRIEN, in bankruptcy.

Chartered accountants, carrying on business in partnership under the firm name and style of Coopers & Lybrand – Chartered Accountants, having a place of business at 801 Brunswick House, 44 Chipman Hill, in the City of Saint John, Province of New Brunswick

And

G. COLIN BAIRD
CHARLES M. FOLLET
JAMES A. KIRBY
RONALD J. WALSH

Chartered accountants, carrying on business in partnership under the firm name and style of Coopers & Lybrand – Chartered Accountants, having a place of business at 235 Water Street, 7th Floor, in the City of St-John, Province of Newfoundland

And

DAVID G. ARSENAULT
C. MARY H. BEST
BRIAN W. CAMERON
IRWIN W. ELLIS

RALPH H. GREEN
J. WALTER MacKINNON
JOHN M. MULLIGAN
MICHAEL L. O'BRIEN

Chartered accountants, carrying on business in partnership under the firm name and style of Coopers & Lybrand – Chartered Accountants, having a place of business at 134 Kent Street, 6th Floor, in the City of Charlottetown, Province of Prince Edward Island

And

COOPERS & LYBRAND – CHARTERED ACCOUNTANTS, a professional partnership carrying on the profession of chartered accountancy and having its head office at 145 King Street West, in the city of Toronto, Province of Ontario

Defendants

CANADA
PROVINCE OF QUÉBEC
DISTRICT OF MONTRÉAL

SUPERIOR COURT

N°: 500-05-001686-946

THIS 16 TH DAY OF SEPTEMBER 2009

PRESENT:

THE HONOURABLE RICHARD MONGEAU J.C.S.

ESTATE OF THE LATE PETER N. WIDDRINGTON

PLAINTIFF

– VS –

ELLIOT C. WIGHTMAN et als.

DEFENDANTS

JUDGMENT

[1] **THE COURT** is seized with a *Motion in continuance of suit* by Plaintiff;

[2] **HAVING** heard the representation of the Plaintiff's attorneys;

[3] **CONSIDERING** the absence of Contestation;

[4] **FOR THESE REASONS, THE COURT:**

[5] **GRANTS** Plaintiff's *Motion in continuance of suit*;

[6] **ORDERS** that the suit be continued between Plaintiff and Mr. Alan Smith in his quality as testamentary executor of the Estate of Christine Sinclair;

[7] **THE WHOLE**, without costs.

J.C.S.

Judge of the Superior Court

COPIE CONFORME
TRUE COPY

Greffier adjoint
Deputy Clerk

CANADA

PROVINCE OF QUEBEC
District of Montreal

SUPERIOR COURT

No: 500-05-001686-946

ESTATE OF THE LATE PETER N. WIDDRINGTON

Plaintiff

vs

ELLIOT C. WIGHTMAN ET AL., including Defendant CHRISTINE SINCLAIR

Defendants

and

ALAN SMITH, in his quality of Executor and Trustee of the Estate of the Late Christine Sinclair

Defendant in Continuance of Suit

APPEARANCE IN CONTINUANCE OF SUIT

We, the undersigned attorneys, hereby appear in the present instance on behalf of Defendant in Continuance of Suit, ALAN SMITH, in his quality of Executor and Trustee of the Estate of the LATE CHRISTINE SINCLAIR, in order to continue suit on its last valid proceedings, under reserve of all legal objections.

MONTREAL, September 30, 2009

COPIE CONFORME/TRUE COPY

(S) HEENAN BLAIKIE S.E.N.C.R.L., SRL/LLP

HEENAN BLAIKIE S.E.N.C.R.L., SRL/LLP

(s) Heenan Blaikie LLP

HEENAN BLAIKIE LLP
Attorneys for Defendant in Continuance of Suit
ALAN SMITH, IN HIS QUALITY OF EXECUTOR AND TRUSTEE OF THE ESTATE OF THE LATE CHRISTINE SINCLAIR

CANADA

PROVINCE OF QUEBEC
DISTRICT OF MONTREAL

N° 500-05-001686-946

SUPERIOR COURT

ESTATE OF THE LATE PETER N. WIDDRINGTON

Plaintiff

vs.

ELLIOT C. WIGHTMAN ET AL.,
Defendants

NOTICE OF CHANGE OF STATUS
(Art. 255 C.C.P.)

TO : Me Sylvie Boulanger
POULIOT MERCURE
1155 René-Lévesque Blvd. W.
31st Floor
Montreal, Qc H3B 3S6

Me Leonard W. Flanz
FISHMAN FLANZ MELAND PAQUIN
1250 René-Lévesque Blvd. W.
Suite 4100
Montreal, Qc H3B 4W8

Me Charles E. Flam
ROBINSON SHEPPARD SHAPIRO
800 Square Victoria
Suite 4700
Montreal, Qc H4Z 1H6

Me Jack Greenstein, c.r.
GROWLING LAFLEUR HENDERSON
1 Place Ville Marie
37th floor
Montreal, Qc H3B 3P4

Me Raynold Langlois
LANGLOIS KRONSTRÖM DESJARDINS
Tour Scotia
1002 Sherbrooke W., 28th Floor
Montreal (Quebec) H3A 3L6

TAKE NOTICE that the following defendant has passed away :

Name of deceased defendant(s)	Date of death
Wittrien, Glenn L.	January 19, 2004

PLEASE GOVERN YOURSELVES ACCORDINGLY.

MONTREAL, November 1, 2006

/s/ HEENAN BLAIKIE

HEENAN BLAIKIE LLP
Attorneys for Defendants

True copy:

HEENAN BLAIKIE LLP

District of New Brunswick
Division No. 01-Saint John
Court No.
Estate No. 51-1042357

NOTICE OF BANKRUPTCY AND OF IMPENDING AUTOMATIC DISCHARGE OF FIRST-TIME BANKRUPT AND REQUEST OF A FIRST MEETING OF CREDITORS
IN THE MATTER OF THE BANKRUPTCY OF
THE ESTATE OF THE LATE LAWRENCE GLENN WITTRIEN BY ITS EXECUTOR PETER WILSHAW
(Summary Administration)

TAKE NOTICE THAT:

1. The Estate of the Late Lawrence Glenn Wittrien by its Executor Peter Wilshaw filed an assignment in bankruptcy on the 25th day of February 2008 and the undersigned A. C. POIRIER & ASSOCIATES INC. was appointed as trustee of the estate of the bankrupt by the official receiver, subject to the affirmation by the creditors of the trustee's appointment or the substitution of another trustee by the creditors.

2. Pursuant to paragraph 155 (d.1) of the Act, a first meeting of creditors will be required only if, within the first thirty days after the date of bankruptcy the official receiver or creditors who have in aggregate at least 25 percent in value of the proven claims request a meeting to be held.

3. To request such a meeting and to vote at a meeting, a creditor must lodge with the trustee before such request for a meeting, a proof of claim and, where necessary, a proxy.

4. Enclosed with this notice is a form of proof of claim, a form of general proxy, and a list of creditors with claims amounting to 25 dollars or more, showing the amounts of their claims.

5. Also enclosed pursuant to section 102(3)(a) of the Act, is information concerning the financial situation of the bankrupt and the obligation of the bankrupt to make payments to the estate of the bankrupt, as required under section 68 of the Act.

6. Creditors must prove their claims against the estate of the bankrupt in order to share in any distribution of the proceeds realized from the estate.

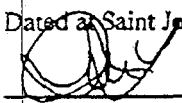
7. Pursuant to section 168.1 of the Act, the bankrupt, being an individual who has never before been bankrupt, will be given an automatic discharge on the 26th day of November 2008 unless the Superintendent of Bankruptcy, the trustee of the estate of the bankrupt, or a creditor of the bankrupt, gives notice of intended opposition to the discharge of the bankrupt before that date.

8. Any creditor who intends to oppose the discharge of the bankrupt shall state in writing the grounds for their opposition, and send a notice to this effect to division office, the trustee of the estate of the bankrupt, and the bankrupt at any time before the 26th day of November 2008.

9. If any creditor opposes the discharge of the bankrupt, a court fee applies.

10. If the discharge of the bankrupt is opposed, the trustee will apply to the court without delay for an appointment for the hearing of the opposition in the manner prescribed by the Act, unless it is a matter to be dealt with by mediation pursuant to Subsection 170.1(4) of the Act.

Dated at Saint John, New Brunswick, this 27th day of February 2008.



A. C. POIRIER & ASSOCIATES INC. - Trustee
133 Prince William Street, Suite 401
Saint John, NB E2L 2B5
Telephone: (506)634-1202
Fax: (506)634-1205

CANADA
PROVINCE OF QUEBEC
DISTRICT OF MONTREAL
NO: 500-05-001686-946

SUPERIOR COURT

THIS 12th DAY OF DECEMBER 2007

PRESENT:

THE HONORABLE W. CLAUDE DECARIE J.C.S.

ESTATE OF THE LATE PETER N. WIDDRINGTON

PLAINTIFF

-VS-

ELLIOT C. WIGHTMAN et als.

DEFENDANTS

JUDGMENT

[1] **THE COURT** is seized with a *Motion for the issuance of an Order in continuance of suit* by Plaintiff;

[2] **HAVING** heard the representation of the Plaintiff's attorneys;

[3] **CONSIDERING** the absence of Contestation;

[4] **FOR THOSE REASONS, THE COURT:**

[5] **GRANTS** Plaintiff's *Motion for the issuance of an Order in continuance of suit*;

[6] **ORDERS** that the suit be continued between Plaintiff and Ms. L.G. Wittrien in her quality as testamentary executor of the Estate of Glenn L. Wittrien;

COPIE CONFORME-TRUE COPY
FISHMAN FLANZ MELAND PAQUIN
P.P. Fishman Flanz Meland Paquin

[7] ORDERS ~~that the said Executor and Trustee of the Estate named in the~~ preceding ~~Order to appear in Court within ten (10) days of service of the Order~~ to be ~~issued~~;

[8] THE WHOLE without costs.

Judge of the Superior Court

COPIE CONFORME
TRUE COPY
LUCIE SAVOIE
Greffier adjoint
Deputy Clerk

Heenan Blaikie

PAR COURRIEL

Le 28 avril 2010

L'honorable Marie Saint-Pierre, j.c.s.
Cour supérieure
Palais de justice de Montréal
1, rue Notre-Dame Est, bureau 16.43
Montréal (Québec) H2Y 1B6

Notre référence : 013384-0001

Objet : ***The estate of the Late Peter N. Widdrington***
c. Elliot C. Wightman and als
CS 500-05-001686-946

Serge Gaudet

T 514 846 2293
F 514 921 1293
sgaudet@heenan.ca

1250, boul. René-Lévesque Ouest
Bureau 2500
Montréal (Québec)
Canada H3B 4Y1

heenanblaikie.com

Madame la Juge,

Lors d'une récente séance de gestion, vous avez demandé une liste complète des défendeurs au dossier Widdrington. Veuillez donc trouver ci-joint la liste complète des parties défenderesses dans le cadre de ce dossier, laquelle est à jour. Nous avons comparu pour tous ces défendeurs, sauf à l'égard de la succession de Glenn Wittrien, tel qu'expliqué ci-après.

Selon ce qu'indiquent nos dossiers, seules deux parties défenderesses au présent dossier ont fait l'objet d'avis de changement de statut, suite à leur décès, soit M. Glenn Wittrien et Madame Christine E. Sinclair.

Dans le cas de Mme Sinclair, suite à un jugement ordonnant la continuation de l'instance, nous avons comparu pour M. Alan Smith, en sa qualité d'exécuteur et liquidateur à la succession de Mme Sinclair, et ce, afin de continuer l'instance sur ses

derniers errements valides, selon ce qui est prévu à l'article 261 C.p.c. (tel qu'il se lisait avant le 1er janvier 2003)[1].

Dans le cas de M. Wittrien, un jugement ordonnant la continuation de l'instance a été rendu le 12 décembre 2007, à l'encontre de Madame L.G. Wittrien, en sa qualité d'exécuteur testamentaire de la succession. Cependant, nous n'avons pas produit de comparution au nom de la représentante de la succession, celle-ci ne nous ayant pas donné mandat de le faire, étant donné son intention de mettre la succession en faillite (ce qui fut fait le 25 février 2008). Nous n'avons donc aucun mandat pour représenter la succession de M. Wittrien dans le cadre du présent dossier et ce, depuis la date de l'avis de changement de statut le concernant (1er novembre 2006).

Une copie des documents pertinents est jointe à la présente.

Veuillez agréer, madame la juge, l'expression de nos sentiments distingués.

Heenan Blaikie S.E.N.C.R.L., SRL

Serge Gaudet
SG/ct

P.j.

c.c. Me Gilles Paquin (Fishman Flanz Méland Paquin)
Me Jack Greenstein, c.r. (Gowling Lafleur Henderson)
Me Raynold Langlois (Langlois Kronström Desjardins)
Me Charles E. Flam (Robinson Sheppard Shapiro)
Me Sylvie Boulanger (Lavery De Billy)

HBdocs - 8347152v1

[1] «Dans les cinq jours de leur comparution, les personnes visées par l'ordonnance peuvent soit demander au tribunal de la révoquer ou de la modifier, soit continuer l'instance sur ses derniers errements valides». Cette disposition s'applique à la présente instance (cf. art. 179 de la loi portant réforme du *Code de procédure civile*, L.Q. 2002, c. 7.)

PAGE: 809

De : "Gilles Paquin" <gpaquin@ffmp.ca>
Destinataire : <pwcew@judex.qc.ca>
CC : <sgaudet@heenan.ca>
Date : 2010-05-07 14:54
Objet : Castor Holdings Ltd. - Coopers & Lybrand - Liste des défendeurs
Pièces jointes : Gaudet Serge - Amendement liste défendeurs 2010-05-07.pdf

Madame la juge,

Veuillez trouver ci-joint une lettre de Me Gilles Paquin dans l'affaire mentionnée en rubrique.

Nous vous prions d'agréer, Madame la juge, l'expression de nos sentiments les plus respectueux.

Hélène Desbiens
Adjointe de Gilles Paquin
Fishman Flanz Meland Paquin, S.E.N.C.R.L.
1250, boulevard René-Lévesque Ouest
Bureau 4100
Montréal (Québec) H3B 4W8
Canada

Téléphone : (514) 932-4100
Télécopieur : (514) 932-4170
Courriel : hdesbiens@ffmp.ca
Site Web : www.ffmp.ca

FISHMAN FLANZ MELAND PAQUIN

S.E.N.C.R.L./LLP
AVOCATS ET PROCUREURS
BARRISTERS AND SOLICITORS

PAR COURRIEL

LEONARD W. FLANZ
AVRAM FISHMAN
GILLES PAQUIN
MARK E. MELAND
NICOLAS BEAUDIN
ALAIN DAIGLE
SUZANNE VILLENEUVE
MARTIN H. SCHEIM
RONALD M. AUCLAIR
MARGO R. SIMINOVITCH
JASON DOLMAN
NICOLAS BROCHU
TINA SILVERSTEIN

Montréal, le 7 mai 2010

HEENAN BLAIKIE S.E.N.C.R.L., S.R.L.
1250, boulevard René-Lévesque Ouest
Bureau 2500
Montréal (Québec) H3B 4Y1

À l'attention de M^e^ Serge Gaudet

OBJET : Castor Holdings Ltd. – Coopers & Lybrand
Re : Liste des défendeurs
500-05-001686-946

Cher Confrère,

Nous accusons réception de votre lettre du 4 mai 2010 et nous notons avec surprise que vous avez choisi de transmettre copie de votre lettre à Madame la juge St-Pierre. La Cour avait clairement exprimé le vœu de laisser les avocats entre eux convenir des questions factuelles concernant la liste des défendeurs, en spécifiant que son intervention serait limitée aux débats, s'il y a lieu, sur l'opportunité ou le droit à l'amendement.

À cet effet, vous avez certainement pris note du fait que je n'ai pas transmis copie de ma lettre du 3 mai à Madame la juge St-Pierre. Cette façon de procéder est nécessaire pour permettre des discussions franches et ouvertes entre les parties et éviter à chaque partie de devoir adopter des positions parce que le tribunal est impliqué.

La première étape des discussions dans cette affaire relève d'un travail qu'on peut qualifier de clérical, soit l'identification des défendeurs dans chacun des dossiers. Dans l'exécution de ce travail, il est inévitable que des erreurs puissent être commises. C'est pourquoi, dans ce cas comme dans d'autres cas, nos bureaux respectifs collaborent pour identifier, s'il y a lieu, ces erreurs.

Quant au tableau que nous vous avons transmis avec notre lettre du 3 mai 2010, nous reconnaissons que certaines erreurs s'y sont glissées, puisque les noms des défendeurs dans les actions en garantie ont été inclus dans le tableau. Nous avons compilé un nouveau tableau pour les 28 dossiers actifs. Ce tableau en format Excel vous sera transmis électroniquement, ainsi qu'aux autres procureurs impliqués. Le tableau a été compilé à l'aide des plumitifs et, encore une fois, il est possible qu'il y ait

des erreurs de compilation puisque dans plusieurs de ces dossiers, notre bureau ne représente pas les demandeurs. D'ailleurs, nous avions indiqué dans notre lettre du 3 mai que les autres procureurs des demandeurs devraient intervenir à cet égard.

Je comprends que la Cour a demandé aux parties de lui fournir une liste de tous les défendeurs impliqués dans tous les dossiers Castor, qu'il y ait ou non demande d'amendement.

D'autre part, nous prenons note de votre intention de contester une demande d'amendement visant à rectifier la désignation des défendeurs. Vos commentaires concernant le délai à faire une telle demande d'amendement nous semblent non pertinents compte tenu de la jurisprudence constante qui permet les amendements même après jugement et qui confirme le principe que l'amendement a un effet rétroactif. Quant à votre argument de prescription, nous soulignons qu'il s'agit possiblement d'un moyen de défense que les défendeurs visés pourraient faire valoir, mais que ce moyen de défense n'empêche pas l'amendement. En fait, les tribunaux, encore une fois, ont à maintes reprises confirmé qu'il n'est pas approprié de se prononcer sur la question de la prescription au stade de la demande d'amendement. Je vous réfère à cet effet à la décision de la Cour suprême du Canada dans l'affaire *Veilleux c. Marineau*, 1969 R.C.S. 861.

Cela dit, nous réévaluerons notre décision de demander ou non l'amendement des procédures dans le dossier Widdrington et nous ferons part de notre décision au tribunal dès la reprise des auditions.

Sur la question de la chose jugée quant à la responsabilité de Coopers qui résultera du jugement Widdrington, mon commentaire dans ma lettre du 3 mai aurait dû être compris comme s'appliquant aux « questions communes ». Nous sommes d'accord avec vous que le jugement Widdrington sera opposable à tous les défendeurs dans les autres dossiers Castor à l'égard des « questions communes », même si certains d'entre eux ne sont pas défendeurs dans le dossier Widdrington.

Quant à votre demande de mettre à jour l'identité des parties demanderesses, nous n'avons aucune objection à entreprendre de travail. Cependant, vous comprendrez qu'il n'y a pas vraiment d'urgence à cet égard, puisque les autres dossiers Castor sont suspendus.

Enfin, compte tenu du fait que vous avez transmis copie de votre lettre du 4 mai à Madame la juge St-Pierre, nous lui transmettrons copie de la présente lettre pour qu'elle soit informée de la situation, sans toutefois lui transmettre la copie du tableau des défendeurs puisque Madame la juge a déclaré qu'elle ne voulait pas être impliquée à ce stade du processus, laissant aux procureurs la charge de convenir de cette question factuelle.

Veuillez agréer, cher Confrère, l'expression de nos sentiments les plus distingués.

FISHMAN FLANZ MELAND PAQUIN S.E.N.C.R.L.

Gilles Paquin

GP/hd
p.j.

c.c. L'honorable Marie St-Pierre, J.C.S. (sans p.j.)
c.c. M[e] Jack Greenstein, c.r. (Gowling Lafleur Henderson)
c.c. M[e] Raynold Langlois (Langlois Kronström Desjardins)
c.c. M[e] Charles E. Flam (Robinson Sheppard Shapiro)
c.c. M[e] Sylvie Boulanger (Lavery De Billy)

CANADA
PROVINCE DE QUÉBEC
DISTRICT DE MONTRÉAL

PROCÈS-VERBAL D'AUDIENCE
Audience au mérite

COUR SUPÉRIEURE
Chambre civile

No
500-06-001686-946

Référée de

Salle prévue
16:03

Date
Le 3 mai 2010

L'HONORABLE MARIE ST-PIERRE J.C.S.

JS1012

Partie demanderesse		Procureur(s)	
Estate of late Peter N. Widdrington		FISHMAN FLANZ MELAND PAQUIN Me Mark Meland Me Margo Siminovitch (morning only) Me Gilles Paquin (jusqu'à 09 :48 a.m.)	
Les autres demanderesses	Absentes		Présents
		GOWLINGS LAFLEUR, HENDERSON Jack Greenstein (absent) 1 Pl. Ville Marie 37 étage Montréal	

Partie défenderesse		Procureur(s)	
Elliot C. Wightman et al.		HEENAN BLAIKIE Me Gary Rosen Me Mindy Paskel-Mede Me Tibor Holländer (jusqu'à 10 :33 a.m.)	
	Présent	Me Guy Sarault (jusqu'à 10 :33 a.m.)	Présents

Nature de la cause
Responsabilité

Montant : $

Cote(s)	Requête (s)
	PROCÈS

Greffier(ière)	Interprète	Sténographe
Claire Le GUERRIER	N/A	N/A

ENREGISTREMENT NUMÉRIQUE

	Début	Fin		Début	Fin
Audition AM :	09:29	12:24	Audition PM :	14:01	16:28

Affaires référées au maître des rôles	Résultat de l'audition
	Cause en progrès

HEURE

09 : 29 **OUVERTURE DE L'AUDIENCE**
Identification de la cause et identification des procureurs

09:30	Commentaires du Tribunal Annexes A à D
	PAGE: 814
09:39	Comments by Me Meland Comments by Me Rosen
09:40	Représentations de Me Gilles Paquin
09:44	Comments by Me Rosen Commentaires du Tribunal
09:45	Représentations de Me Gilles Paquin Échanges avec le Tribunal
09:48	Me Paquin quitte la salle d'audience Commentaires du Tribunal Suite aux représentations de Me Paquin et en l'absence de Me Gaudet, il y aura suivi de l' Annexe C
09:49	Comments by Me Siminovitch Comments by Me Rosen
09:51	Commentaires du Tribunal: Annexe D – le suivi sera fait lundi, le 10 mai 2010 : durée maximale 30 minutes
09:51	Comments by Me Meland Comments by Me Rosen
09:52	Représentations de Me Meland
10:06	Échanges entre le Tribunal et Me Meland
10:07	Représentations de Me Siminovitch Échanges avec le Tribunal
10:09	Représentations de Me Rosen Échanges avec le Tribunal
10:31	Comments by Me Meland
10:32	Comments by the Court
10:33	Me Holländer leaves the courtroom Me Guy Sarault leaves the courtroom
10:34	Comments by Me Meland

C A N A D A
PROVINCE DE QUÉBEC
DISTRICT DE MONTRÉAL

C O U R S U P É R I E U R E

DOSSIER N° : 500-05-001686-946

sous la présidence de : **L'HONORABLE MARIE ST-PIERRE, j.c.s.**

ESTATE OF
LATE PETER N. WIDDRINGTON
ET AL

partie demanderesse

- C. -

ELLIOT C. WIGHTMAN
ET AL

partie défenderesse

COMPARUTIONS :

Me MARK MELAND,
Me MARGO SIMINOVITCH (morning only),
Me GILLES PAQUIN (until 9:48 A.M.),
pour Estate of late Peter N. Widdrington
et autres demanderesses.

Me JACK GREENSTEIN, (absent)
pour Daimler Chrysler.

Me GARY ROSEN,
Me MINDY PASKELL-MEDE,
Me TIBOR HOLLÄNDER (until 10:33 A.M.),
Me GUY SARAULT (until 10:33 A.M.),
pour la partie défenderesse.

CH100503AMPM **Le 3 mai 2010.**

interrogé en chef, nous avons siégé de 9 h 30 à 12 h 00 et de 14 h 00 à 16 h 30, pour donner une pause de deux heures; si c'est encore le souhait, j'aimerais qu'on me l'indique, et s'il y a des difficultés, qu'on me les mentionne.

Et nous avions aussi fait deux jours, journées de pause, et alors, comme j'ai mentionné que j'allais accepter un maximum de trois jours, je veux savoir comment, pendant la semaine, on envisage que ces journées-là puissent se dérouler.

Me MARK MELAND
on behalf of the Plaintiffs :

My Lady, with your permission, just in terms of the schedule for this morning, maître Paquin is here in respect to the issue of the list of Defendants.

THE COURT :

Okay.

Me MARK MELAND :

Perhaps he could make a very brief representation to the Court, it would give my friends also an idea where we're coming from, and

then we could deal with the other issues. That's my suggestion to the Court.

Me GARY ROSEN
on behalf of the Defendants :

I have no objection. The only remark I'll make is that, that issue is certainly an issue that I am completely... almost... well, not completely unfamiliar with, but I certainly have not been handling.

So to the extent that we will address it, and I know that maître Bolduc and maître Gaudet have been handling now.

THE COURT :

Alors, ce que je propose peut-être, effectivement, comme maître Paquin est ici et qu'il est le représentant de la Demande qui peut me faire part de la position de la Demande à cet égard-là, je procéderais à entendre immédiatement les représentations que maître Paquin peut avoir à faire et ça permettra peut-être de le libérer cela fait.

Je comprends de ce que vous me dites, maître Rosen, que vous ne seriez pas en mesure ce matin

vous-même de répondre à cela, mais vous allez prendre note, comme maître Sarault et maître Holländer qui sont ici prendront note de ce que maître Paquin a à signaler, et je comprends à première vue que ce sujet ne fait pas l'objet d'un accord actuellement et qu'il va falloir que l'on identifie de façon précise quel est le problème, s'il y a un problème, et que je m'occupe d'y apporter la solution voulue.

Me GILLES PAQUIN,
pour les demandeurs :

Merci, madame.

THE COURT :

Alors, je vous écoute.

Me GILLES PAQUIN :

Dans un premier temps, il y a une forme d'accord, en ce sens que, effectivement, pour les défendeurs dans l'action Widdrington, la liste communiquée par maître Gaudet correspond à notre liste à nous. Donc, il y a accord à cet égard-là.

THE COURT :

O.K.

Me GILLES PAQUIN :

Cependant, j'avais invité maître Gaudet à faire une rencontre avec nous parce qu'il y a plusieurs actions, comme vous le savez, et les défendeurs qui apparaissent nommés dans ces actions-là, les noms diffèrent d'une action à l'autre, et ce que j'ai proposé, ou ce que j'avais l'intention de proposer, c'est effectivement de communiquer une position commune et s'entendre sur effectivement avoir dans l'action Widdrington l'ensemble des défendeurs qui sont visés par les autres actions.

Donc, actuellement, nous avons fait ce travail de réconciliation – quand je dis "nous", du côté de la Demande – nous n'avons pas jusqu'à maintenant communiqué avec maître Gaudet parce que, comme je vous disais, j'avais invité à faire une rencontre, ça n'a pas eu lieu, mais c'est ce qui arrive, mais donc, l'intention de la Demande est essentiellement, si nécessaire, de demander d'amender l'action Widdrington de façon à refléter que tous les défendeurs visés dans toutes les

actions sont également visées par l'action Widdrington; compte tenu que c'est une cause commune, ça réglera cet aspect-là de la question.

Donc, c'est le constat que je fais aujourd'hui et la demande que je fais au Tribunal, ce serait essentiellement, si nécessaire, de soit fixer une date ou possiblement, je présume qu'il sera préférable que la procédure soit signifiée et, à ce moment-là, s'il y a un accord, tant mieux, s'il n'y en a pas, le Tribunal verra à pouvoir dégager du temps pour nous entendre.

THE COURT :

Il est... bon, il est certain que, dans un premier temps, maître Rosen me dit qu'il n'est pas en mesure de répondre à cela, mais je pense qu'il faudra que maître Gaudet s'y adresse, s'y attaque.

Le jugement que je rendrai est un jugement qui a, à l'égard de toutes les questions communes, force de chose jugée, le mien ou celui que quelqu'un d'autre après moi rendra, le cas échéant, mais dans cette cause...

Me GILLES PAQUIN :

C'est ça.

THE COURT :

... de sorte que j'exige d'avoir l'identité de toutes les personnes qui, à titre de défendeurs, le cas échéant, sont susceptibles d'être impactées d'une manière ou d'une autre par cela.

Je comprends de ce que vous me dites au surplus, maître Paquin, qu'il y a peut-être aussi un débat potentiel sur le fait d'amender ou de ne pas amender dans l'action de Widdrington, là, c'est...

Me GILLES PAQUIN :

Bien, écoutez...

THE COURT :

Non mais...

Me GILLES PAQUIN :

D'un point de vue procédural.

THE COURT :

D'un point de vue procédural, peut-être que ce sera une difficulté que la Défense pourra mettre de l'avant, mais que les gens soient défendeurs au moment où on se parle dans l'action de Widdrington

ou qu'ils ne le soient pas, moi, je veux 100 % des gens identifiés comme défendeurs dans tous les dossiers qui sont dans l'annexe des dossiers connexes que nous avons faits dans ce procès et qui donnent lieu à une annexe d'un procès-verbal, que je pourrai retracer, le cas échéant.

Alors, si la liste reçue de maître Gaudet ne comporte que les personnes identifiées dans l'action Widdrington...

Me GILLES PAQUIN :

Exact.

THE COURT :

... il faudra compléter cette information-là avec tous les noms de toutes les autres personnes qui sont dans tous les dossiers.

Me GARY ROSEN :

That was not clear to me, I apologize.

THE COURT :

I'm not saying it was clear...

Me GARY ROSEN :

And it would be helpful...

THE COURT :

... but it's...

Me GARY ROSEN :

It would be...

THE COURT :

... as far as I'm concerned, I want to have...

Me GARY ROSEN :

It would be helpful...

THE COURT :

... everyone.

Me GARY ROSEN :

... My Lady... it would be helpful, My Lady, if you could just point at least myself to the *procès-verbal*...

THE COURT :

Yes, I did ask... je vais pouvoir vous

l'identifier, là...

Me GARY ROSEN :

Oui, ça va.

THE COURT :

... c'est à maître Bolduc que je m'étais adressée dès le début du dossier et j'ai exigé qu'il y ait une liste qui soit faite de tous les dossiers...

Me GARY ROSEN :

Liste des procédures.

THE COURT :

... qui étaient sujets...

Me GARY ROSEN :

Oh, une liste des dossiers ?

THE COURT :

... au jugement que j'allais rendre.

Me GARY ROSEN :

Non, non, ça, je m'en souviens.

THE COURT :

Et j'ai même exigé qu'il y ait un porte-parole de part et d'autre qui soit identifié, de sorte que s'il y avait quelque changement que ce soit en cours de route, les porte-parole identifiés de part et d'autre avaient le devoir de m'en prévenir.

Je n'ai jamais été prévenue de quoi que ce soit jusqu'à maintenant, de sorte que, quant à moi, la liste telle qu'elle est dans une annexe d'un procès-verbal, elle est toujours la liste en vigueur. S'il y a des changements, je m'attendrai à ce que les porte-parole, qui sont identifiés dans les PV et dans la transcription, s'adressent à moi pour me prévenir de ça, mais autrement, moi, j'ai cette liste, là, et ce sont tous les dossiers actifs qui sont impactés par le jugement que je rendrai.

Me GARY ROSEN :

Ça va.

THE COURT :

Mais la date précise du procès-verbal, là, il faudrait que je le cherche, mais...

Me GILLES PAQUIN :

C'est en juin 2008, Madame le Juge...

THE COURT :

C'est bien possible...

Me GILLES PAQUIN :

... c'était maître Siminovitch.

THE COURT :

... parce que je l'ai demandé, je crois, dès janvier 2008...

Me GILLES PAQUIN :

Exact.

THE COURT :

... puis ça a pris un certain temps avant que le travail puisse être fait et échangé de part et d'autre pour que tout le monde s'entende.

Me GILLES PAQUIN :

Exact. Donc, au niveau de la liste des causes actives, appelons-les comme ça, je pense que les parties, effectivement, ont fait leurs devoirs et

ont soumis au Tribunal une liste conjointe avec tout le monde... avec laquelle tout le monde est d'accord.

THE COURT :

Oui.

Me GILLES PAQUIN :

Le cheminement additionnel, c'est de déterminer les défendeurs, pour une raison qu'on ne peut pas vous expliquer 15 ans plus tard, là, il y a des différences dans les défendeurs nommés qui sont là.

THE COURT :

Moi, j'ai... oui. Ce que je pense être à première vue, mais je comprends que la personne qui est responsable de ça, qui est maître Gaudet, est pas ici ce matin, là.

Me GILLES PAQUIN :

C'est ça.

THE COURT :

Mais... alors, c'est une réaction que j'ai

pour l'instant, c'est pas une ordonnance, mais...

Me GILLES PAQUIN :

Oui.

THE COURT :

... mais je... il est clair que je vais exiger, si on ne me les donne pas volontairement, par une ordonnance l'ensemble des noms, ça, je veux dire, il y a pas aucun doute dans mon esprit, et ma réaction est la suivante, je pense que les procureurs de part et d'autre devraient, par une rencontre ou autrement, s'asseoir et régler cette affaire de façon précise, simple, au coût le plus minime possible, et s'il reste une difficulté, le cas échéant, qui m'apparaîtrait à première vue être une difficulté d'apparier les noms des uns et des autres dans une procédure ou dans l'autre, et qui met en cause, potentiellement, le fait qu'on doive s'interroger sur les droits d'amender ou de ne pas amender, bon, bien, vous me soumettrez la difficulté juridique de l'amendement, le cas échéant, mais avec des données factuelles qui, à mon avis, ne devraient pas nécessiter mon intervention, les avocats devraient être capables

de faire ça tout seuls.

Me GILLES PAQUIN :

Très bien, madame.

THE COURT :

Et j'aimerais bien que ça soit fait d'ici au début de la semaine prochaine, idéalement, parce que je n'anticipe pas que je sois appelée à siéger pour entendre de la preuve ou des représentations bien au-delà de la semaine prochaine. Alors, j'aimerais bien que tout ça se règle dans les prochains jours. Mais je ne connais pas, pour le moment, l'horaire de maître Gaudet et celui...

Peut-être pouvez-vous tenter de le rejoindre, maître Paquin.

Me GILLES PAQUIN :

Définitivement, Madame la Juge.

THE COURT :

Et s'il y a une difficulté, je vais être ici, alors on m'en informera.

Me GILLES PAQUIN :

Très bien.

THE COURT :

Et s'il y a un débat à faire, bien, j'aimerais bien qu'on puisse s'adresser à ce débat-là, et je crois que la semaine prochaine, nous ne siégeons qu'à compter de mardi, avec maître Flanz et les témoins qui viennent de l'Allemagne, de sorte que, au besoin, s'il y avait un débat, peut-être que la journée ou une partie de la journée de lundi pourrait être utilisée à cette fin-là.

Me GILLES PAQUIN :

Très bien, madame. Merci beaucoup.

THE COURT :

Merci.

Me GILLES PAQUIN :

Et, avec votre permission, je vais laisser mes collègues continuer.

THE COURT :

Merci.

Me GILLES PAQUIN :

Merci.

(Me PAQUIN QUITTE LA SALLE D'AUDIENCE)

THE COURT :

Alors, pour les fins du procès-verbal, madame Le Guerrier, vous allez indiquer que, suite aux représentations de maître Paquin et en l'absence de maître Gaudet en salle d'audience, puisqu'il n'était pas prévu qu'il soit nécessaire que maître Gaudet soit là ce matin, il y aura suivi du contenu de l'annexe C à la suite d'échanges entre maître Paquin et maître Gaudet.

Ça va, madame Le Guerrier ?

LA GREFFIÈRE :

Oui.

THE COURT :

Ça m'amène à revenir à l'annexe D, qui est la requête de maître Siminovitch. Alors, j'avais prévu que l'on convienne dès ce matin du moment où je pourrais entendre cela et, dépendamment des personnes qui doivent être présentes pour en