SUPREME COURT OF YUKON

Citation: *Cobalt Construction Inc.* v. *Kluane First Nation*, 2013 YKSC 124

Date: 20131216
S.C. No. 13-A0078
Registry: Whitehorse

Between:

COBALT CONSTRUCTION INC.

Plaintiff

And

KLUANE FIRST NATION

Defendant

Before: Mr. Justice L.F. Gower

Appearances:

Meagan Lang (agent for Karen Martin) — Counsel for the Plaintiff
Gary W. Whittle — Counsel for the Defendant

REASONS FOR JUDGMENT

INTRODUCTION

[1] In this application, the defendant, Kluane First Nation ("KFN"), seeks: firstly, security for costs (estimated to be $53,574.10) pursuant to s. 254 of the *Business Corporations Act*, R.S.Y. 2002, c. 20 (the "*Act*"); and, secondly, a stay of the action commenced by the plaintiff, Cobalt Construction Inc. ("Cobalt"), until the security is given.

[2] The action arises from a tendering dispute regarding the upgrade of certain roads in Burwash Landing, Yukon. Cobalt submitted a bid for the work to KFN, along with two other competing contractors. Cobalt alleges that its bid was not only the lowest, but also

included a bid bond, which was required by KFN's tender documents. Cobalt further alleges that the successful bidder, Kluane Corp. not only submitted a higher bid price, but failed to include a bid bond with its bid. Accordingly, Cobalt claims that KFN breached its obligations under the tender documents by: (a) accepting a materially noncompliant bid; (b) failing to evaluate the bids in accordance with the ranked criteria (the highest ranking being the bid price); and (c) exhibiting bias in favour of Kluane Corp. because it is a corporation directly related to KFN. The action was commenced on September 16, 2013 and KFN's statement of defence was filed October 9, 2013.

ISSUES

[3] The principal dispute in this application is whether Cobalt has sufficient, or indeed any, exigible assets to enable it to pay KFN's court costs if KFN is successful in defending the action. However, a number of sub-issues were also argued:

1) Has KFN met its initial onus to establish that "it appears" Cobalt will be unable to pay KFN's costs, if successful?
2) If so, has Cobalt met its evidentiary burden to establish that it has sufficient exigible assets to pay those costs?
3) If security for costs is ordered, what should be the amount and in what fashion should they be paid?, and
4) Should there be a stay of the action pending the payment of security for costs?

ANALYSIS

[4] Section 254 of the *Act* states:

> "In any action or other legal proceeding in which the plaintiff is a body corporate, <u>if it appears</u> to the court on the

> application of a defendant that the body corporate will be unable to pay the costs of a successful defendant, the court may order the body corporate to furnish security for costs on any terms it thinks fit." (my emphasis)

[5] This section was considered by Hudson J. in *Inukshuk Resources Inc. v. 413152 B.C. Ltd. et al.*, 2002 YKSC 26. There, Hudson J. noted that the predecessor to s. 254 read "if it appears by credible testimony", but that the current provision reads "if it appears". At para. 34, he concluded:

> "I take it that this change in wording can only serve to reduce the standard of proof required to one of appearance only, not proven appearance. I take the phrase "all relevant circumstances" to reinforce the view that the standard of proof is a low one.

It is not immediately clear what Hudson J. was referring to when he referenced the phrase "all relevant circumstances", however I expect he was referring to the principles engaged in security for costs applications discussed by the British Columbia Court of Appeal in *Kropp v. Swanaset Bay Golf Course Ltd.,* [1997] B.C.J. No. 593, which he discussed earlier in his reasons. *Kropp* dealt with a provision in the British Columbia *Companies Act* which is similar to our s. 254*.* At para. 17, the Court of Appeal referred to the English decision in *Keary Development v. Tarmac Construction*, [1995] 3 All E.R. 534 (Eng. C.A.), which set out the principles engaged in the application of such provisions:

> "1. The court has a complete discretion whether to order security, and will act in light of all the relevant circumstances;
>
> 2. The possibility or probability that the plaintiff company will be deterred from pursuing its claim is not without more sufficient reason for not ordering security;
>
> 3. The court must attempt to balance injustices arising from use of security as an instrument of oppression to stifle a legitimate claim on the one hand, and use of

impecuniosity as a means of putting unfair pressure on a defendant on the other;

4. The court may have regard to the merits of the action, but should avoid going into detail on the merits unless success or failure appears obvious;

5. The court can order any amount of security up to the full amount claimed, as long as the amount is more than nominal;

6. Before the court refuses to order security on the ground that it would unfairly stifle a valid claim, the court must be satisfied that, in all the circumstances, it is probable that the claim would be stifled; and

7. The lateness of the application for security is a circumstance which can properly be taken into account." (my emphasis)

[6] In any event, Cobalt's counsel did not take issue with the suggestion that KFN's initial onus is a low one. Nor was there any dispute between the parties that it is only after the defendant meets its initial onus that the evidentiary burden shifts to the plaintiff. In *Citizens for Foreign Aid Reform Inc. v. Canadian Jewish Congress*, [1999] B.C.J. No. 2160 (S.C.), at para. 14, Romilly J. set out the steps to be followed in an application for security for costs:

> "1. Does it appear that the plaintiff company will be unable to pay the defendants' costs if the action fails?
>
> 2. If so, has the plaintiff shown that it has exigible assets of sufficient value to satisfy an award of costs?
>
> 3. Is the court satisfied that the defendants have an arguable defence to present?
>
> 4. Would an order for costs visit undue hardship on the plaintiff such that it would prevent the plaintiff's case from being heard?"

[7] In Ontario, the equivalent to s. 254 is Rule 56.01(1)(d), which provides:

> "The court, on motion by the defendant …may make such order for security for costs as is just where it appears that,
>
> …
>
> (d) the plaintiff …is a corporation…and there is good reason to believe that the plaintiff or applicant has insufficient assets in Ontario to pay the costs of the defendant or respondent." (my emphasis)

This provision was considered by the Ontario Court of Appeal in *City Commercial Realty Services (Canada) Ltd. v. Bakich*, [2005] O.J. No. 6443. The Court there similarly held that there was a lighter or reduced initial onus on the defendant to raise a belief of insufficiency, but that the belief must nevertheless go beyond mere conjecture, hunch or speculation. At paras. 7 and 8, the Chambers Judge stated:

> "7 Under rule 56.01(1)(d), the moving party is not required to establish that a corporation has insufficient assets to pay costs, but only to establish that there is good reason to believe that the corporation has insufficient assets to pay the costs. As Philp J. noted in *737071 Ontario Inc. v. Min-A-Mart Ltd.*, [1996] O.J. No. 1173 (Ont. Gen. Div.) at para. 5: "This lighter onus is based on the belief that it would be unfair to insist that the defendant prove something that is within the knowledge of the plaintiff."
>
> 8 Even though the onus is a reduced one, the moving party must still provide enough information about the corporation to raise a belief of insufficiency that goes beyond mere conjecture, hunch, or speculation." (my emphasis)

[8] In the case at bar, KFN's counsel stressed that the test for security for costs in Ontario is more stringent than that in the Yukon, because Ontario uses the words "good reason to believe", whereas, in the Yukon, a defendant merely has to establish an 'appearance' that the plaintiff will be unable to pay costs. Therefore, he says the Ontario case law on point is distinguishable. Cobalt's counsel submitted that the initial onus in Ontario is similar to that in the Yukon, in the sense that it is comparably low, and that the

Ontario cases are therefore still helpful. However, Cobalt's counsel found no cases subsequent to *Inukshuk* which have given any content to the Yukon standard.

[9] In *Cigar500.com Inc. v. Ashton Distributors Inc*. (2009), 99 O.R. (3d) 55 (S.C.), Code J. also addressed Ontario Rule 56.01 and noted that it, like s. 254 of the Yukon *Act*, gives rise to a shifting onus between the plaintiff and defendant and that "the standard of proof also changes as the onus shifts" (para. 20). At para. 24, Code J. referred with approval to *Websports Technologies Inc. v. Cryptologic Inc*., [2003] O.J. No. 5455 (S.C.), stating that Master Haberman had helpfully explained the policy reasons for insisting that defendants satisfy their initial onus under the Rule on the basis of "proven facts" rather than "mere conjecture, hunch or speculation". Code J. then went on to quote Master Haberman directly:

> "This motion is brought pursuant to subrule 56.01(1)(d), such that Cryptologic must demonstrate that there is "good reason to believe" that Websports has insufficient assets in Ontario to pay their costs at the end of the day. While all agree that this subrule places a higher onus on corporate plaintiffs, the phrase "good reason to believe" must have some meaning. In my view, it involves something more than a hunch or a concern. <u>There must be some evidence placed before the court from which the court can accept that the concern is genuine and that it is based on proven facts regarding the corporation's current financial</u> <u>circumstances.</u> A bald assertion that a party has insufficient assets, on its own, cannot satisfy the first part of the test. If that was all that was required, motions of this kind would be brought to "test the waters", in all cases where a plaintiff corporation alleges that the defendant's action has caused it to sustain a significant loss, with no information as to the state of a company's financial affairs and no legitimate basis for concern. The 2-part test, with the initial onus on the moving party, is intended to discourage parties from bringing these costly motions without actual grounds. <u>While the moving party need not go so far as to prove that there are insufficient assets, they must, at least, prove facts from which a court</u>

> can conclude that there is good reason to believe that that is the case." (my emphasis)

[10] Although the wording of the Ontario test is different from that in the Yukon, I note that the former also begins with the words "where it appears that". Having said that, the additional wording "good reason to believe" may well give rise to a slightly higher onus than the 'appearance' standard in the Yukon. Hudson J. held in *Inukshuk*, that "the standard of proof … [is] one of appearance only, not proven appearance" (para. 34), however I am unsure what he meant by the latter phrase.

[11] I find the reasoning in *Websports*, cited above, to be helpful in giving flesh to the bones of the Yukon test. Firstly, it seems to me that the 'appearance' that the plaintiff will be unable to pay the successful defendant's costs need only be based on a reasonable inference. Here, I agree with *Websports* that the appearance must go beyond mere conjecture, hunch or speculation. Secondly, although I would not go so far as *Websports* to say that the inference must be drawn from "proven facts", I would suggest there must be 'some evidence' capable of proving the underlying facts upon which to draw the inference.

[12] In the case at bar, counsel jointly submitted that, in determining the underlying facts relating to the defendant's initial onus, the Court can look to the evidence of both parties on the application. I agree with the correctness of that approach, as did Code J. in *Cigar500*, at para. 30.

[13] The evidence tendered by KFN in discharging its initial onus is twofold. First, it points to a certificate of title showing that Cobalt is the owner of certain real property in the City of Whitehorse which, as of March 31, 2011, had a stated value of $1.2 million. However, KFN also points out that the certificate of title indicates this property is subject

to encumbrances totalling $2,706,050: a 2008 mortgage in favour of the Business Development Bank of Canada (“BDC”) of $706,050; a 2010 Certificate of Pending Litigation (“CPL”) in favour of BDC; a 2011 mortgage in favour of Jevco Insurance Company (“Jevco”) of $500,000; and a 2012 mortgage in favour of BDC of $1.5 million. Although Cobalt disputes that all of these mortgages are still active, KFN notes that, in any event, Cobalt’s president, Shaun Rudolph, has deposed that the actual indebtedness to BDC on the 2012 mortgage, as of December 1, 2013, was $1,729,339.80. Thus, on the evidence of either party, KFN submits that the value of this land is substantially exceeded by the registered encumbrances and it cannot be considered an exigible asset.

[14] Here, I understand the term “exigible” to mean any asset which could be seized through the execution of a judgment and its value realized by a subsequent sale, for the benefit of any creditor of Cobalt. Land which is encumbered by debts exceeding its value would not be considered exigible, since the secured creditors would be paid in priority to any unsecured judgment creditors.

[15] The second piece of evidence initially tendered by KFN on this application was a search of the Yukon Personal Property Security Registry done on October 8, 2013, which discloses approximately 20 secured creditors of Cobalt and 111 items of collateral. I note that KFN’s counsel did not appear to rely on this evidence at the hearing. For that reason, and for others which will soon become obvious, I do not find this evidence to be particularly probative of the state of Cobalt’s solvency, and I give it little weight.

[16] The evidence tendered by Cobalt is principally found in the affidavit of Shaun Rudolph. He deposed that he has over 14 years’ experience in earthmoving construction

and that he incorporated Cobalt in January 2010. His operations manager has over 30 years of experience in the industry.

[17] Mr. Rudolph also deposed that the real property referred to in the certificate of title is a 20-acre piece of land next to the Alaska Highway in the City of Whitehorse on which Cobalt's ten-bay shop and rebuild facility is situated. He further deposed that Cobalt purchased this property from Golden Hill Ventures Ltd. ("Golden Hill") on March 28, 2011, and it was then valued at $1.2 million. Mr. Rudolph deposed that three of the outstanding encumbrances on the title relate to the indebtedness of Golden Hill and should have been discharged at the time of the purchase. With respect to the BDC 2008 mortgage and the 2010 CPL, Mr. Rudolph has appended an email from BDC's counsel, dated November 20, 2013, confirming that counsel has instructions to provide Cobalt with a release of the CPL and a discharge of the mortgage. With respect to the 2011 Jevco mortgage, Mr. Rudolph has appended an email from a representative of that company, dated November 19, 2013, confirming that Jevco would be discharging the mortgage from title "right away".

[18] KFN's counsel objected to Cobalt's evidence that the above encumbrances would be discharged, as it is hearsay. Cobalt's counsel submitted that it is trite law that hearsay evidence is admissible on interlocutory applications.

[19] Rule 49(12)(a) of the Yukon Rules of Court states:

> "(12) An affidavit may state only what a deponent would be permitted to state in evidence at a trial, except that, if the source of the information is given, an affidavit may contain statements as to the deponent's information and belief, if it is made
>
> (a) in respect of an application for pre-trial order…"

[20] In *Canada (Attorney General) v. Acero*, 2006 BCSC 1015, Bennett J. as she then was, considered the British Columbia equivalent of our Rule 49(12)(a), and concluded that firsthand hearsay is generally admissible on interlocutory matters in civil proceedings. At paras. 15-17, she stated:

> "15 There are a number of proceedings in criminal law and in the civil law in which statutes provide for the admission of hearsay for the truth of its contents. In British Columbia, an affidavit in an interlocutory application may be made "on information and belief". Rule 51(10) of the B.C. *Supreme Court Rules* states:
>
> > (10) An affidavit may state only what a deponent would be permitted to state in evidence at a trial, except that, if the source of the information is given, an affidavit may contain statements as to the deponent's information and belief, if it is made
> >
> > (a) in respect of an application for an interlocutory order,
>
> 16 In interlocutory applications, second-hand hearsay is generally inadmissible: see *Ulrich v. Ulrich* (2004), 25 B.C.L.R (4th) 171, *Foote v. Foote* (1996), 6 B.C.L.R. (2d) 237. If the deponent refers to hearsay, the source of the information must be clearly set out: *Meier v. Canadian Broadcasting Corporation* (1981), 28 B.C.L.R. 136 (B.C.S.C.)…
>
> 17 <u>In summary, on interlocutory matters in civil proceedings in British Columbia, hearsay is generally admissible, provided it identifies the source from which the information is based and the deponent is familiar with the information and believes it to be true</u>. Further, it appears that second-hand and third-hand hearsay is not admissible in affidavits in British Columbia." (my emphasis)

[21] In the case at bar, Mr. Rudolph failed to expressly depose in his affidavit that he believed the representations of BDC's counsel and Jevco's representative to be true. However, there is no question that he identified the sources of the information regarding

the pending discharge of these encumbrances, and I am satisfied in reviewing his evidence as a whole on this point, that he is relying on that information and therefore implicitly believes it to be true. In the result, I accept that in real terms, the only encumbrance which will remain against the certificate of title for Cobalt's Whitehorse property is the 2012 BDC mortgage which, as of December 1, 2013, was outstanding in the amount $1,729,339.80. Although Mr. Rudolph deposed that he made a further monthly payment against this debt on November 23, 2013, it was not made clear to me how much that reduced the total indebtedness. Therefore, I will assume for the time being that the BDC debt still exceeds the value of the property in 2011, which was $1.2 million. Accordingly, the land cannot be considered an exigible asset of Cobalt's.

[22] KFN's counsel also noted that Cobalt's indebtedness to BDC is further secured by a General Security Agreement, dated April 30, 2012. A copy of that document is appended to Mr. Rudolph's affidavit and confirms that Cobalt granted BDC "a fixed and specific charge" in all of Cobalt's "present and after-acquired personal property", which was defined in the Agreement in sufficiently broad terms to include all of Cobalt's motor vehicles, heavy equipment and other personal property. This led KFN's counsel to stress that none of Cobalt's personal property could be considered as "exigible" for the purposes of this application, since it is all encumbered by the General Security Agreement. Once again, if any asset encumbered by the General Security Agreement were to be seized for the purpose of realization, BDC's security would be expected to take priority over the judgment debt of an unsecured creditor of Cobalt.

[23] On the other hand, Cobalt's counsel submitted that the General Security Agreement only attaches to Cobalt's assets to the extent of the amount of its

indebtedness to BDC at the present time, which I understand to be something slightly less than $1.7 million, after the November 23rd payment which Mr. Rudolph deposed to making. Further, counsel submitted that Mr. Rudolph has provided additional evidence that Cobalt owns other assets, the value of which significantly exceeds the amount of the BDC debt. In particular, Cobalt's counsel pointed to Mr. Rudolph's deposition that the company "owns over 200 pieces of equipment, including pick-up trucks, excavators, rock trucks, dozers, graders, loaders, packers and cranes" (para. 19), which he estimated to have a value of "over $5 million" (para. 22). Mr. Rudolph also stated that only 27 of the 200 plus pieces of equipment are subject to financing (para. 19). For example, he deposed that Cobalt owns 68 pickup trucks which are unencumbered and, based on their purchase prices, he estimates their combined value to be $320,481. Similarly, he deposed that Cobalt owns 17 unencumbered bulldozer tractors, which he valued at $273,475, based on their purchase prices. Admittedly, these last two examples were uncorroborated by any independent evidence.

[24] However, Mr. Rudolph further deposed that the value of just 50 of Cobalt's 205 pieces of equipment is estimated to be $2,359,550, based on the prices each was purchased for, mostly in 2010 and 2011 (para. 22). Here, Mr. Rudolph has attached copies of the bills of sale for each group of these items of equipment showing the purchase price and the date of purchase.

[25] KFN's counsel submitted that, notwithstanding this evidence, Cobalt has still failed to produce any evidence: (a) that it continues to own this equipment today; or (b) of the present marketability of each of the pieces. Accordingly, counsel suggested that this evidence is not probative of the extent to which Cobalt has any exigible assets right now.

Further, KFN's counsel vigorously argued that Cobalt ought to have produced further independent evidence of its current solvency, such as financial statements and appraisals of value, and that an adverse inference can be drawn from its failure to do so. In general, counsel suggested that it would have been relatively easy for Cobalt to provide such information and that it ought not be allowed to rely on the evidence of Mr. Rudolph alone on many of these points.

[26] Cobalt's counsel cautioned that expecting Cobalt to produce certain evidence for the purposes of determining the defendant's initial onus on the security for costs question would be tantamount to shifting the burden of proof to the plaintiff. That, said counsel, would be an error in law similar to the one committed by the Master appealed from in *Cigar500*. As stated by Code J., at para. 25:

> "The authorities are clear that the second step onus on the plaintiff is not even reached until the defendants satisfy their initial burden."

Notwithstanding the differences in the wording between our s. 254 and Ontario Rule 56.01(1)(d), that is also the law in the Yukon. Accordingly, counsel submitted that I should not draw any adverse inference against Cobalt for failing to produce certain evidence at this stage of the analysis, because the onus here remains with KFN. I agree.

[27] Having said that, the additional evidence provided by Mr. Rudolph is capable of proving that Cobalt is a profitable corporation which is: (a) meeting its liabilities; (b) able to obtain financing; and (c) able to secure bonding for projects under contract (para. 30). In this latter regard, Mr. Rudolph has deposed that, in addition to its private sector work, Cobalt has been awarded 12 Yukon Government contracts since 2010, all of which

required that Cobalt qualify for and provide bonding, which it did. Mr. Rudolph indicated that the total value of these contracts was $2,156,664 (para. 32).

[28] I return briefly to the two complaints made by KFN's counsel about Cobalt's evidence on the 50 pieces of equipment valued at $2,359,550. Firstly, looking at Mr. Rudolph's affidavit as a whole, and in particular, his deposition that "Cobalt owns over 200 pieces of equipment" (para. 19), there is simply no reason to conclude that it does not currently own this equipment. Secondly, I concede that there is no evidence from Cobalt as to the present marketability of this equipment. However, I nevertheless feel safe in drawing the inference that, even allowing for a reasonable rate of depreciation, the value of this equipment likely exceeds the extent of Cobalt's indebtedness to BDC by a significant amount. Further, there is additional evidence to suggest that there are 155 other pieces of equipment which presumably also have significant value. All of this suggests that Cobalt will be able to pay costs in the neighbourhood of $53,000, if required. Lastly, there was no application by KFN's counsel to cross-examine Mr. Rudolph on his affidavit, notwithstanding that I raised this option with counsel during the hearing. Therefore, Cobalt's evidence in this regard is uncontradicted.

[29] I also challenged KFN's counsel to provide me with case authority supporting his suggestion that a plaintiff/respondent to an application for security for costs ought not to be able to rely on its own evidence, even when it is a corporation. None was provided.

[30] Where does all this leave the defendant KFN in terms of discharging its initial onus to establish that "it appears" Cobalt will be "unable to pay" KFN's estimated costs of $53,574.10 if it is successful at trial? Admittedly, it appears to be reasonable to infer from the tendered evidence that Cobalt's real property in the City of Whitehorse is not

presently an exigible asset which would enable it to pay KFN's estimated costs. However, Cobalt obviously has assets apart from the real property. Even given the encumbrances on the land, KFN has not persuaded me that there is any evidence regarding Cobalt's solvency capable of supporting a reasonable inference that Cobalt will be unable to pay KFN's estimated costs. Indeed, Cobalt's uncontradicted evidence leads to the very opposite reasonable inference that, on the basis of the likely total value of its equipment alone, Cobalt should be well able to pay those costs, if necessary.

CONCLUSION

[31] As KFN has not satisfied its initial burden, the evidentiary burden does not shift to Cobalt, and KFN's application for security for costs must be dismissed.

[32] In the event that I am wrong in finding that KFN has not discharged its initial onus, it may be obvious from what I have concluded above that I would nevertheless be satisfied that Cobalt has satisfied its evidentiary burden to establish that it has exigible assets of sufficient value to satisfy KFN's estimated costs.

[33] Given these conclusions, it is unnecessary for me to deal with the question of the amount of the security for costs or the stay of the action pending payment of same.

[34] Pursuant to Rule 60(12)(b), as the successful party on an application, Cobalt would generally be entitled to costs as costs in the cause, unless this Court otherwise orders. However, each party sought costs in any event of the cause; KFN in its Notice of Application and Cobalt in its Memorandum of Argument. Because I consider KFN's failure to meet its initial burden as a reflection of the relative weakness of its application, I am satisfied that Cobalt should be awarded costs in any event of the cause.

GOWER J.