



CORPORATE SECURITIES and FINANCE LAW REPORT

Volume 14 • Number 3

June / August 2009

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Guest Article

Jeffrey S. Leon, LSM, and Shara N. Roy of Bennett Jones LLP examine the collapse of the third-party ABCP market in Canada, and the various responses to it in their article entitled "Pain and Promise":

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GUEST ARTICLE

Pain and Promise: Lessons from the Collapse of the Third-Party ABCP Market in Canada

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Neither a borrower nor a lender be: for loan oft loses both itself and friend – Hamlet, Act I, Scene 3

Introduction

The financial crisis has dominated the headlines. The effect of Wall Street on Main Street was a central battle-cry during the U.S. presidential election and as recently as April 14, 2009, President Obama spoke to an audience at Georgetown University, trying to explain, among other things, traditional securitization and credit default swaps:

Investment banks would buy and package together these questionable mortgages into securities, arguing that by pooling mortgages, the risks had been reduced. [...] [Others] decided to make profits by selling billions of dollars of complicated instruments that supposedly insured these securities.

These complex issues are difficult to understand. At the risk of oversimplification, we will look at the crisis, and the response, in Canada from a litigator's perspective. In Canada, following the market freeze in third-party (non-bank) sponsored asset-backed commercial paper ("ABCP") in August 2007 a unique Canadian response was developed – the restructuring under insolvency legislation of a whole market. This solution potentially avoided years of complex and inter-related litigation through a "negotiated" (under the duress of a collapsed market) plan of arrangement, backed by a series of comprehensive releases. The plan may not affect all participants equally or equitably, however, both the lower court and the Court of Appeal for Ontario held that it was the best that could be done in the circumstances to attempt to retain, and even create, value for the participants. It remains to be seen whether value was created by the plan or whether the old adage "the first loss is the best loss" applies.

Corporate Securities and Finance Law Report

This Report is published five times a year under licence by LexisNexis Canada Inc., 123 Commerce Valley Drive East, Markham, Ontario, L3T 7W8, and is available by subscription only.

Web site: www.lexisnexis.ca

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ISBN 0-433-45102-5 **ISSN 0822-1082**

ISBN 0-433-45166-1 (print & PDF)

ISBN 0-433-45164-5 (PDF)

Subscription rates: \$260.00 plus GST (print or PDF)

\$315.00 plus GST (print & PDF)

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In this paper, we will explore the ABCP market, including the products and the participants; we will look at the market freeze in August 2007 and its causes; we will review the plan to restructure the non-bank sponsored ABCP market and the Ontario Superior Court of Justice's and the Court of Appeal for Ontario's decisions approving the plan; we will look at two trusts that elected not to be part of the overall restructuring and their fates; we will examine the reaction of the regulators in Canada to the market freeze and offer our own opinions on policy reform; and finally, we will review what this crisis has taught us generally about complex securities and specifically what happens when complex securities are the subject matter of litigation.

We expect increased government and private enforcement if the conspiracy amendments are passed.

ABCP Market overview

Overview

Asset-based financing is a relatively modern expression, synonymous with secured lending, and codified in statutes such the *Personal Property Security Act* in Ontario. It is to be distinguished from unsecured lending. In asset-based financing, a loan is secured by the pledging of an asset in the event of default by the borrower. Often the loan is in respect of the asset, but not always.

Various types of assets are captured under the rubric of asset-based financing and new asset classes were continually being created by the creative financiers behind these products. In the 1980s, asset securitization, also referred to as structured finance or asset-backed securitization, developed as a distinct type of asset-backed financing.¹ Asset securitization involves receivables, such as credit card or trade receivables, auto and equipment loans and leases, mortgages and, in more recent transactions, collateralized debt obligations (as defined below),² which are then held in special purpose vehicles ("SPVs") created for the purpose of holding the securitized assets. An SPV may be a corporation, a trust or a partnership.³ As we will see, in Canada, SPVs generally took the form of trusts.

ABCP is a part of the structured finance market and is a form of asset securitization. The ABCP market brings together investors wishing to invest in highly rated short-term money market debt securities and companies looking for an alternative source of debt financing, potentially at a lower cost than traditional commercial paper and banker's acceptances.⁴

In general, ABCP is created when a company sells financial assets to a trust in return for cash. The purchase of these assets by the trust is funded by the issuance of commercial paper, with a term to maturity of typically 30, 60 or 90 days but may be as long as 364 days. On maturity, new commercial paper is issued to replace, or “roll”, the maturing paper.

The growth of structured finance has created both opportunities and challenges for credit markets. According to the Bank of Canada, the capital markets are more “complete” due to structured finance products, because they allow optimal credit use exposures with lower transaction costs. From this perspective, “[r]isks can be unbundled, repackaged and effectively transferred to other market participants through structured financial products”. On the other hand, the Bank of Canada notes that structured finance products can be “highly complex, difficult to price accurately, illiquid and opaque in regard to their risk characteristics”.⁵

As we will explore in this paper, it was the complexity of the product itself coupled with a new form of debt, the subprime mortgage, that in large part proved to be the undoing of the non-bank sponsored ABCP market in Canada.

The Products

Due to the complexity of the market, which was largely unregulated, there is not necessarily a single description for the products. The descriptions in this paper reflect the authors’ understanding of the ABCP market, although we are aware that different participants in the market may have structured their products differently and used different descriptions. We have described the participants and the products for the purpose of continuity in the paper. The descriptions should not necessarily be relied upon in other contexts.

Traditional (Plain Vanilla) Securitization

Traditional securitization is generally described above. It involves the issuance of ABCP to fund the purchase by a trust of secured debt. The debt is backed by assets, which can be realized upon in the event of default and offer an additional layer of protection for the purchaser of the commercial paper.

Collateralized Debt Obligations

A collateralized debt obligation (“CDO”) is a more complex form of securitization. Rather than an investor investing in an asset directly as described above, the investor is exposed to the income and risks of only a part of a portfolio of assets. The portfolio assets (the underlying debt obligations) can contain any type of traditional credit assets.⁶

CDOs are generally sold in tranches with varying credit-risk profiles. The income and risk levels for the investor depend upon which tranche of the reference portfolio underlying the CDO the investor has purchased and the specific points at which the CDO begins to take part in portfolio’s losses.⁷ An R-1 (high) or AAA rated product is the top tranche, which would experience losses only after all other tranches had experienced 100% loss.

As multi-tranche instruments, CDOs offer flexibility in terms of structuring financial risks and returns for investors, allowing the tranches to be customized to the risk and yield objectives of individual investors. According to the Bank of Canada, CDOs were the fastest growing area of structured finance globally, with issuances exceeding US\$2 trillion in 2006.⁸

Credit Default Swap

A credit default swap (“CDS”) is akin to insurance, where one party seeks to protect itself against a defined credit event or events. The party seeking to be insured pay fees to another party who “insures” the first party if and when a certain credit event occurs. The insuring party may be required by the contract to post collateral so that the insured party can be sure the funds will be there should they need to be drawn upon.⁹

“Credit Arbitrage” Transactions

A credit arbitrage transaction is a general term that refers to many different types of transactions. The main difference between traditional and credit arbitrage transactions is that the “assets” backing credit arbitrage-type notes are themselves securities.

The collateral that backed these “credit arbitrage” transactions included investment-grade corporate debt

and other fixed income assets such as corporate bonds, and even other asset-backed securities, and CDOs. In the latter category, the assets underlying the CDOs could include synthetic exposures to any asset types acquired in the form of CDS or credit linked notes (“CLNs”).

Leveraged Super Senior Structures

A “leveraged super senior” (or “LSS”) structure was a type of credit arbitrage transaction. In an LSS structure, a leveraged (for instance 5-1) position is taken against exposure to a tranche of a portfolio of assets (under a CDO) by way of a CDS contract. In an LSS transaction, the tranche to which the position is exposed is the R-1(high) or AAA tranche, which is the tranche least likely (and last) to suffer any losses in the event of a credit default of the underlying assets. Therefore, it was deemed not necessary to purchase “insurance” for the full amount of the potential loss. Given the unlikelihood of any loss in the R-1 (high) or AAA tranche, “insuring” a twentieth of the loss (5-1 leverage), for example, was considered more than suitable. These transactions are also very profitable because the trust received the same premium payments as if it had fully funded its exposure.¹⁰

As a further protection under the LSS transactions, the “insured” is entitled, under the contract, to make a call on the “insurer” in the event of triggering events (“margin triggers”) to post additional collateral (“margin calls”) to ensure that the “insurer” has sufficient security in an event of default. These margin triggers were generally based on the market value of the transaction and were called “mark-to-market” triggers. These calculations, like the product themselves, were highly complex.¹¹

The Participants

The Sponsors

The Canadian sponsors of SPVs or trusts in the ABCP market can be roughly divided into the bank and the non-bank sponsors. The bank sponsors are affiliated with Schedule I banks and operate as divisions of those larger banks. The banks are publicly traded and the

ABCP divisions form but a part of the larger structure of the bank. The types of asset-originators, as defined below, typically courted by the banks were those companies who would generally be considered to be desirable clients of the banks themselves.

The non-bank sponsors were a smaller part of the ABCP market. Non-bank sponsors sprung up to take advantage of the opportunities in the market for loans secured by assets or originators not considered to be traditionally desirable by the banks. This included, for example, leases for construction equipment and agricultural equipment. They also stepped in to securitize smaller pools of assets. Generally, non-bank sponsored trusts also offered investors higher returns in the form of greater spreads on basis points (“bps”), which cost was passed on to the originators. Non-bank sponsors had great success in these areas and it was not long before the banks also made forays into this market.

In the Canadian market, all non-bank sponsors were private companies save one. Coventree Inc. went public in November 2006, less than a year before the collapse of the markets.

The structure for bank and non-bank sponsors was similar. The sponsor would establish a trust or trust to purchase the assets from the asset originator and issue the ABCP to pay for the purchase. The sponsors administered the trusts.

The Trustees

The issuer trustee established the trust. Generally, the beneficiaries of non-bank sponsored trusts were unnamed, unspecified charities.

The indenture trustee was appointed pursuant to the trust indenture to act on behalf of the creditors of the trust and to hold the securities in the underlying assets.

The Asset Originators

The asset originators provided the sponsors with the assets which then backed the ABCP. Certain asset originators also entered into CDO and CDS-type transactions.

Originators were not regulated and could be in any type of business. For the traditional securitization business, originators were, for example, General Motors who sold car loans or VISA sold credit card debt. For credit arbitrage transactions, the originators were more likely to be investment banks.

In May 2007, DBRS (as defined below) set out the following criteria for new asset originators:

- a) Management of the originator possesses deep, specific and reputable experience in the business.
- b) The originator has been conducting business for a minimum of two years or maintains a minimum unsecured long-term BBB (low) rating from DBRS.
- c) The originator has maintained and continues to maintain alternate financing arrangements so as to not create undue reliance on short-term ABCP financing.
- d) The originator maintains equity sufficient in substance to support the representation and warranties, covenants and indemnities provided in the securitization transaction.
- e) The receivables have been originated, managed and collected for a minimum of two years in order to demonstrate that the contracts are bona fide and the credit collection policies are time tested. For asset classes that are new or unique, it may also be appropriate that receivables initially season on an originator's balance sheet (up to six months) prior to the transfer to a securitization vehicle.
- f) The servicing of the receivables may also require the involvement of an experienced third party or a performance guarantor of suitable credit quality if an originator's servicing experience or resources are viewed inadequate.

The Liquidity Providers

Liquidity providers entered into agreements with trusts to provide funding to the trusts to meet their obligations if they were unable to "roll" their ABCP. Generally, the agreements provided that such funding was to be provided in the case of a defined liquidity drawn-down event. As we will examine more closely below, in Canada, DBRS (as defined below) required

that liquidity only be available in the event of a market disruption, as opposed to global-style liquidity, which agreements defined 'liquidity event' more broadly.

Often, the liquidity provider was not at arm's length from the transaction, but simultaneously played another role or roles. See our discussion of Devonshire Trust below.

Broker Dealers

The broker dealers were regulated through the Investment Industry Regulatory Organization of Canada ("IIROC"). They marketed and sold ABCP to investors. Generally, the broker dealers for non-bank sponsored ABCP were affiliated with the Schedule I Banks and also sold bank-sponsored ABCP.

The brokers also provided market-making lines to the sponsors, taking ABCP onto the banks' books if investors could not be found for the paper on a particular day.

Rating Agencies

DBRS Limited ("DBRS") was, almost exclusively, the credit rating agency for ABCP in Canada. DBRS was actively involved in the ABCP markets by providing ratings for the commercial paper issued by the trusts. DBRS provided these ratings in exchange for a fee and therefore had a commercial relationship with the trust and/or issuer. DBRS, like all ratings agencies, is not a regulator.

DBRS assigned ratings to ABCP based on the likelihood of losses in the reference portfolio. Rating ABCP is a complex task. To provide a rating, the rating agencies must first determine, for the portfolio as a whole, the probability of default. Then using complex models (including, default correlation, default probability and loss recovery rate) it is determined what the probability of loss is at each attachment point. The lower the probability of loss, the higher the credit rating for that specific tranche note.¹² The highest credit rating in Canada of R-1 (high) or AAA for ABCP which means that the probability of default or loss in the portfolio is extremely low.

In addition to reviewing the credit worthiness of the portfolio, DBRS also had many other requirements to

rate a product R-1 (high) or AAA. Among those requirements were certain liquidity facilities, in the event that a trust was unable to “roll” ABCP to fund maturing ABCP. This liquidity was necessary because of the timing mismatch between the maturing ABCP (which rolled for 30, 60 or 90 days, in general) and the long-term nature of the assets that backed the commercial paper. Without proper liquidity, this could give rise to a trust being unable to repay its ABCP holders when required.¹³

The trust was required to purchase liquidity from a liquidity provider. The liquidity provider was not necessarily a stranger to the transaction, but might also be, for instance, the asset originator. The liquidity provider would agree to pay the trust (so that it could pay its ABCP holders) when a defined liquidity event occurred. In the U.S., Moody's and S&P, as examples, required global-style liquidity, meaning that the liquidity provider was required to pay in the event of any inability by the trust to meet its obligations to its holders of ABCP to pay principal and interest. In this scenario, very little risk is held by the trust itself, therefore it is a very expensive liquidity product.

Until January of 2007, DBRS only required what termed “Canadian-style” liquidity. Under Canadian-style liquidity, the two pre-conditions to funding were: (1) the inability of the trust to issue new ABCP as a result of a “general market disruption” (“GMO”); and (2) the credit quality of the underlying assets had not deteriorated. This type of liquidity facility was much more cost-effective for the trust because some risk remained with trust and was not wholly transferred to the liquidity provider. However, on January 19, 2007, DBRS issued a press release stating that it was going to require global-style liquidity for all new structured finance transactions.

The Market Freeze in Non-bank Sponsored Commercial Paper

U.S. Subprime Mortgages

Due in large part to low interest rates, changes in legislation and the strong U.S. housing market, new

debt products were created and packaged into assets for the trusts, most notably among them subprime and Alternative A-paper mortgages.

Although there is no legal definition of subprime, generally subprime borrowers and loans have the following identifying characteristics:

- a) borrowers with lower credit scores;
- b) high debt-service-to-income ratio, greater than 40% on average;
- c) higher loan-to-value ratio, 80% or more;
- d) smaller loan size, \$100,000 on average;
- e) less documentation; and/or
- f) higher mortgage rates of 200 basis points on average over prime borrowers.¹⁴

A subprime borrower or loan generally meets two or more of the above factors. In addition, interest rates also often jump significantly after a honeymoon period.¹⁵ Subprime mortgages may also have elements of predatory lending, including prepayment penalties.

Alternative A-paper (or “Alt-A”) borrowers or loans generally would qualify for a traditional mortgage, but for one of the subprime factors listed above. Subprime and Alt-A borrowers also generally have higher levels of non-mortgage related indebtedness and relied heavily on their homes as a source of equity to refinance and meet their other obligations. From 1991 to 2005, borrowing against home equity increased from \$100 billion to over \$900 billion in the U.S.¹⁶

Other types of mortgage products also entered the strong housing markets, including 30 and 40-year amortization, interest-only and negative amortization loans. One study noted, prior to the market melt-down: “Because of its complicated nature, subprime lending is simultaneously viewed as having great promise and great peril.”¹⁷ In the third quarter of 2002, the Mortgage Bankers Association of America reported that subprime loans had a delinquency rate 5 ½ times higher than for prime loans (14.28% versus 2.54%). Over several years leading up to mid-2007, the number of subprime mortgages underwritten in the U.S. increased

significantly against a backdrop of rising house prices. The subprime mortgage industry grew from \$65 billion in 1995 to \$332 billion in 2003.¹⁸ Investment banks in the U.S. packaged many of these mortgages into pools securing mortgage-backed securities that were sold to investors.¹⁹

Subprime “Contagion” in the Canadian ABCP Market

U.S. subprime was not necessarily a large portion of the assets in the Canadian ABCP market, but it was a powerful force. The Bank of Canada stated that the assets behind the phenomenal growth in the Canadian markets was primarily foreign based:

Over the past two years, the Canadian ABCP market has experienced strong growth, largely because of the funding of synthetic CDO assets. Underlying this expansion has been the phenomenal growth of the global CDS market, which has been greatly facilitated the construction of synthetic CDOs. Given the relatively small volume of CDS based on Canadian debt securities, a significant portion of the credit risk associated with these CDOs is foreign based.²⁰

According to the Bank of Canada, strains in credit markets may be traced to the spring 2007, when a re-pricing of credit was triggered by news that delinquency rates and foreclosures associated with subprime mortgages in the U.S. had been rising quickly. Specifically, after three years of sustained declines, the delinquency rate on U.S. subprime mortgages started to increase in early 2006 and by the end of 2007 was over 9%.²¹ A number of originators of subprime and Alt-A mortgages filed for bankruptcy or stopped activity, leading to tighter lending standards and the removal of several alternative mortgage products from the market place.²²

In June 2007, credit rating agencies began to downgrade mortgage-backed securities and CDOs that included U.S. residential subprime mortgage debt. Risking defaults on U.S. subprime mortgages also initiated a sustained widening of long-term credit spreads in Canada and elsewhere.

In July and August 2007, spreads continued to widen due to downgrades and declining liquidity in the secondary market for CDOs and mortgage-backed securities. According to the Bank of Canada, the announcement by BNP Paribas on August 9, 2007, that it had closed

redemptions of three investment funds because it could not value their assets in the prevailing illiquid market environment for structured products, provided the catalyst for a sharp decrease in the global appetite for risk. This triggered a broader re-pricing of risky financial assets around the world, including in Canada.²³

These various events led to a “sharp and, in many cases, unprecedented widening in the spreads between rates in the short-term credit markets (such as ABCP, corporate paper, three-month LIBOR, and three-month bankers’ acceptances), and expected overnight rates (over the same term) in Europe, the United States and Canada”. The market participants’ ability to “roll” their ABCP in early August 2007 became more and more difficult. The problem in Canada was exacerbated by the issuance of \$3 billion in new ABCP on August 3, 2007.²⁴ As spreads widened further and further, certain risks increased, including the possibility of a call on liquidity providers based on an allegation of a general market disruption. In the broader market, Banks reacted to widening credit market spreads by increasing inter-bank lending spreads. At the same time, money market investor demand for ABCP diminished as spreads increased because the likelihood that trusts would have to draw upon back-up liquidity arrangements increased.²⁵

Transparency and Complexity

Exacerbating the issue of subprime mortgage fears was the extreme complexity of ABCP products and their relative lack of transparency. The Bank of Canada noted: “It is important to recognize that structured financial products only transfer risks, they do not eliminate them – the risks must ultimately rest somewhere, although it may now be more difficult to determine whether these risks are properly priced or unduly concentrated.”²⁶

Most asset-backed securities in the ABCP market were issued pursuant to a prospectus exemption under securities laws, meaning that no disclosure was required to be made to investors. Therefore, any disclosure that was provided to investors was done on a voluntary basis in accordance with market demand and practice. In addition, sponsors did not control their relationship with their investors. The market operated such that

notes were sold to investors through dealers, who acted as intermediaries between the investor and the trust-sponsor. Dealers often jealously guarded their investor lists to prevent poaching.

Voluntary disclosure was therefore made to the dealers, whom sponsors relied upon to pass long the information to investors. Such voluntary disclosure generally consisted of an information memorandum or term sheet which contained basic information about the issuer, sponsor, interest date, date of repayment, dealers distributing the security and details of any guarantee of payments. The information memorandum or term sheet was typically prepared at the inception of the program but could be updated whenever the sponsor so chose.²⁷

According to IIROC, very often the information memoranda did not disclose the underlying asset class composition, the asset and liquidity providers, the role of the sponsor, the issuing and paying agent or the distribution agents. In a June 2007 article in the *Bank of Canada Financial System Report*, the Bank of Canada said that “[t]he fact that securitization is a complicated process involving many participants would seem to argue for a high degree of disclosure. But the market is relatively opaque.”²⁸

Would transparency have solved the problem, however? The market was so complex that transparency might have simply confused the issue. When making investment decisions, dealers and investors relied almost exclusively on the credit ratings and the knowledge that the programs had liquidity support. There was no detailed public disclosure of asset class composition by trust issuer to differentiate the asset securitization strategy amongst ABCP trusts.²⁹

The Court of Appeal, in hearing the appeal of the lower court’s approval of a plan of arrangement to restructure the ABCP market, discussed further below, stated:

*The crisis was fuelled largely by a lack of transparency in the ABCP scheme. Investors could not tell what assets were backing their notes – partly because the ABCP Notes were often sold before or at the same time as the assets backing them were acquired; partly because of the sheer complexity of certain underlying assets; and partly because of assertions of confidentiality by those involved with the assets.*³⁰

Investors could not know whether the assets they were invested in had exposure to the collapsing U.S. subprime mortgage market or any related products or assets that were experiencing substantial losses as a result of the collapse. Out of fear and an abundance of caution, investors decided not to roll their investments, thereby aggravating the liquidity crisis.³¹

In December 2007, the *Bank of Canada Financial System Review* presented a detailed discussion of the ABCP market. The Bank explained that the turbulence in global financial markets was triggered by

*... concerns about the value of structured products based on U.S. subprime mortgages, reflecting growing delinquencies in these mortgages. This disquiet subsequently broadened to include a wide range of structured products – because some of these products contained subprime mortgages and because investors had difficulty in valuing these securities, owing to their complex structures and lack of information about the assets backing them. Liquidity evaporated in the secondary market for structured products since investors feared that they would be unable to sell assets quickly at prices commensurate with what they thought they should be worth – a fear that became a self-fulfilling prophecy.*³²

Perhaps transparency would have addressed the particular fears of investors at this time: U.S. subprime. However, full transparency may not have been meaningful to investors. With such a complex market and product, what would meaningful disclosure look like? This is a question the regulators are now attempting to answer, as discussed below.

The Canadian market encountered an additional difficulty because non-bank sponsored trusts were unable to draw on liquidity due to (according to the Bank of Canada) differing interpretations of liquidity providers’ contractual obligations and due to the narrower trigger event (a GMD) under those arrangements.³³ As stated above, DBRS began a move to requiring global-style liquidity for new structured finance transactions in January 2007. This was already required by the U.S. ratings agencies, Standard and Poor’s and Moody’s. In his affidavit in the Superior Court of Ontario action approving the restructuring plan, described below, Hy Bloom for one of the investor groups stated that this should have been a red-flag. Mr. Bloom stated that:

Standard and Poor's August 1, 2002 report warned that the liquidity agreement underpinning commercial paper in Canada was insufficient and that investing in such paper required a "leap of faith" that liquidity would still be there if a crisis arose. Consequently, Standard and Poor's concluded that there was no sufficient protection to give the Canadian commercial paper an investment grade.³⁴

Reasons for the Market Freeze on August 13, 2007

According to the uncontested evidence of Purdy Crawford, the Chair of the Pan-Canadian Investors Committee for Third Party Structured ABCP, in the Ontario court proceedings (as described below) to restructure the third party non-bank ABCP market, the market freeze in the week of August 13, 2007 was largely triggered by market sentiment, as news spread of significant defaults on U.S. subprime mortgages. As discussed above, in large part, investors in Canadian ABCP lost confidence because they did not know what assets or mix of assets backed their ABCP. Because of this lack of transparency, existing holders and potential new investors feared that the assets backing the ABCP might include subprime mortgages or other overvalued assets. Investors stopped buying new ABCP, and holders stopped "rolling" their existing ABCP.

Most of the assets supporting the trusts were long-term in nature, such as pools of residential mortgages, credit card receivables, equipment loans and leases, commercial mortgages, personal lines of credit, or CDSs. The long-term nature of the assets posed a matching problem for the ABCP because the cash flow generated from the assets did not match the cash flow required to repay maturing ABCP, a short-term debt instrument. Although the timing mismatch always had the potential to become a problem, the market continued along smoothly because investors reinvested or rolled their ABCP at maturity. Also, new ABCP was constantly being sold which was generating additional funds to repay maturing ABCP when investors did not roll their investment and required payment.³⁵ In the weeks leading up to August 13, 2007, investors began rolling their paper overnight only, as opposed to the traditional 30- to 90-day rolls.

As ABCP became due, trusts were therefore unable to fund repayments through new issuances or replacement notes. Trustees of some trusts made requests for

advances under the liquidity arrangements; however, many liquidity providers took the position that the conditions for funding had not been met, which as discussed above under Canadian-style liquidity would require a GMD, because the bank-sponsored ABCP programs continued to roll. With no new investment, no reinvestment, and no liquidity funding available, and with long-term underlying assets whose cash flows did not match maturing short-term ABCP, payments due on the ABCP could not be made.³⁶

Some of the asset providers made margin calls to certain trusts under their LSS swap contracts, requiring the trusts to post additional collateral. However, since the trusts could not issue new ABCP, roll over existing ABCP or draw on their liquidity agreements, those trusts were not able to post the additional collateral which was being demanded by the asset providers. The non-bank sponsored ABCP market simply froze on the morning of August 13, 2007.

Why Were the Banks Spared?

Although it is not possible to know for certain why bank-sponsored products did not suffer the same fate as the non-bank sponsored trusts in the Canadian ABCP market, and it is likely attributable to a number of different factors, the banks were able to inject their own liquidity into the bank-sponsored markets to keep the paper rolling in the short term until investors were willing to re-enter the market.

In its public disclosure, the Royal Bank of Canada (at note 25 to its Consolidated Financial Statements for the year ended October 31, 2008) described those facilities as follows:

Backstop liquidity facilities are provided to asset-backed commercial paper trust programs (programs) administered by us and third parties, as an alternative source of financing in the event that such programs are unable to access commercial paper markets, or in limited circumstances, when predetermined performance measures of the financial assets owned by these programs are not met. We generally provide liquidity facilities for a term of one to three years.

Backstop liquidity facilities are also provided to non-asset backed programs such as variable rate demand notes issued by third parties. These standby facilities provide liquidity support to the issuer to buy the notes if the issuer is unable to remarket the notes, as long as the instrument and/or the issuer maintains the investment grade rating.

The terms of the backstop liquidity facilities do not require us to advance money to these programs in the event of bankruptcy or to purchase non-performing or defaulted assets.

The Bank of Montreal stated in note 7 to its Consolidated Financial Statements for the year ended October 31, 2008 that: “The maximum amount payable under these backstop and other liquidity facilities totaled \$32,806 million as at October 31, 2008 (\$39,428 million in 2007). As at October 31, 2008, 1,143 million was drawn (\$16 million in 2007) in accordance with the terms of the backstop facilities...”

The non-bank sponsors did not have these types of well-funded backstop facilities in place to keep their paper rolling when the markets froze.

A ‘Made in Canada’ Solution is Found

The Montreal Accord

On August 16, 2007, a consortium of ABCP market participants met in Montreal. In attendance were the Caisse de dépôt et placement du Québec (“CDPQ”), National Bank, Desjardins Group, PSP Investments and six parties who were liquidity providers: ABN Amro Bank, N.V., Canada Branch; Barclays Bank PLC; Deutsche Bank AG; HSBC Bank USA, National Association; Merrill Lynch International; and UBS AG. DBRS was also present for the discussions.

The Montreal participants (other than DBRS) reached a 60-day standstill agreement in order to work towards a restructuring of all non-bank sponsored ABCP. The basic principles of the Montreal Accord were that: (i) all outstanding non-bank sponsored ABCP would be converted into term floating rate notes maturing at the same time as the underlying assets; and (ii) margin provisions under LSS swaps would be changed to create renewed stability. The first principle addressed the “timing mismatch” issue. The second preserved the value of the ABCP and its underlying assets by reducing the risk that the trusts would have to post additional security for the swap obligations or have assets seized and sold.³⁷ In addition, the parties agreed to rescind liquidity draw requests and to suspend collateral calls for assets.

Negotiations were more difficult and complex than originally anticipated and the standstill agreement was

extended more than once, until in March of 2008 the parties filed for protection under the *Companies’ Creditors Arrangement Act*, R.S.C. 1985, c. C-36 (the “CCAA”).

The Restructuring Plan

During the week of August 27, 2007, representatives of the CDPQ and National Bank, two of the four investors that signed the Montreal Accord, asked Purdy Crawford, Q.C. to chair the Pan-Canadian Investors Committee for Third Party Structured ABCP, which became known as the “Crawford Committee”. Mr. Crawford accepted the chairmanship of the committee on September 5, 2007 and an announcement was made regarding the formation of the committee on the following day.³⁸

The members of the Crawford Committee represented investors who held approximately 66.25% of the total \$35 billion of ABCP then outstanding and held significant positions in each series of ABCP.³⁹ In addition, representatives of DBRS and of the Department of Finance (Canada) were granted the status of observers. The mandate of the Committee provided that the Committee had been formed as an ad hoc committee with a view to maximizing recoveries efficiently and fairly and in the best interests of all holders of ABCP.⁴⁰

After many months of negotiations, the restructuring plan (the “Plan”) that was ultimately put forward involved approximately \$32 billion of ABCP issued by the trustees of 20 trusts, in 47 series. Not involved in the plan was approximately \$3 billion of ABCP that was issued by the trustees of Skeena Capital Trust and of Devonshire Trust. The ABCP issued by the trustee of Skeena Capital Trust has already been successfully restructured and the ABCP issued by the trustee of Devonshire Trust is still being addressed, as discussed further below.⁴¹

As part of the Plan, the indenture trustee for each series was required to “stand still” (that is, not take any steps to put the ABCP in formal default or take proceedings) in accordance with the Montreal Accord.

According to Mr. Crawford’s affidavit evidence in the court approval process for the Plan, the Plan, in theory, preserved value by decreasing the risk of a forced liquidation of assets in a depressed market, thus

maintaining the potential for higher recoveries as markets stabilize and improve. The Plan required certain compromises or changes from what investors originally bargained for, which were arguably necessary to obtain the benefits of agreements required to make the Plan work.⁴²

In its essence, the Plan would convert the noteholders' paper – which had been frozen and therefore effectively worthless for many months – into new, long-term notes that would trade freely, but with a discounted face value. The hope was that a strong secondary market for the notes would emerge in the long run.⁴³

The Plan aimed to improve transparency by providing investors with detailed information about the assets supporting their ABCP notes. It also addressed the timing mismatch between the notes and the assets by adjusting the maturity provisions and interest rates on the new notes. Further, the Plan adjusted some of the underlying credit default swap contracts by increasing the thresholds for default triggering events; in this way, the likelihood of a forced liquidation flowing from the credit default swap holder's prior security was reduced and, in turn, the risk for ABCP investors was decreased.⁴⁴

The Plan also required extensive mutual releases for all participants, which was the subject of contention before the courts, as explored below. The Plan as structured generally required the noteholders to release all participants from any cause of action (including negligence) except for (essentially) intentional fraudulent misrepresentation.

Under the Plan, the vast majority of the assets underlying ABCP were pooled into two master asset vehicles (known as MAV1 and MAV2). The pooling was designed to increase the collateral available and thus make the notes more secure. The Plan did not apply to investors holding less than \$1 million of notes. The number of retail investors holding ABCP came as a surprise to many of the participants and questions arose about whether ABCP could ever be a suitable investment for a retail investor, regardless of their sophistication. However, certain dealers agreed to buy the ABCP of those of their customers holding less than the \$1-million threshold and to extend financial assistance to these customers.⁴⁵

While it is true that the Plan was strongly supported by the vast majority of noteholders (96%), it was argued that if the voting had been conducted on a series by series basis, support for certain trusts would not have been as strong. While the vast majority of assets were transferred to MAV1 and MAV2, a third master asset vehicle (MAV3) was established to hold assets which were determined to be "ineligible". For example, any assets with exposure to subprime mortgages were deemed ineligible. One trust in particular, Ironstone Trust, had a large percentage of assets deemed ineligible for MAV1 and MAV2. Counsel for one noteholder group referred to MAV3 as the "gulag", and this description stuck with the asset vehicle throughout the proceedings. As a result of the transfer of its assets to MAV3, it became clear early on that holders of certain Ironstone notes would not be voting in favour of the Plan. In fact while the plan was supported by 96% of all noteholders, only 47% of Ironstone Series B noteholders voted in favour of the plan.

The Restructuring Approved at the Ontario Superior Court of Justice - *Metcalf & Mansfield Alternative Investments II Corp. (Re)*

A Plan by the Stakeholders for the Stakeholders

Under the CCAA, a plan of arrangement requires court approval. Justice Campbell of the Ontario Superior Court of Justice commented on the novelty of the solution, for an almost entirely unique problem, presented by the Plan:

The activities of the Investors Committee, most of whom are themselves Noteholders without other involvement, have been lauded as innovative, pioneering and essential to the success of the Plan. [...] The insolvency is of the ABCP market itself, the restructuring is that of the market for such paper – restructuring that involves the commitment and participation of all parties. The Latin words sui generis are used to mean something that is "one off" or "unique". That is certainly the case with this Plan.⁴⁶

Justice Campbell stated that the Plan as presented was a negotiated solution between the stakeholders and that the Plan would either be approved as a whole or would fall as a whole. Justice Campbell held that the court did not have the power to amend the Plan.⁴⁷ The court's analysis of the

Plan focused primarily on the power of the court to approve the Plan under the CCAA. Although interesting, this analysis is not the subject matter of this paper.

In the application, some stakeholders sought to have the Plan amended to exclude from the releases certain causes of action, namely claims of negligence and fraud against certain third parties. In his decision, Justice Campbell reported the results of information compiled by the court appointed monitor into the types of claims that might be made against third parties, including the trusts and their sponsors. The monitor reported that the potential claims against the proposed defendants were for the most part tort claims, including negligence, misrepresentation, negligent misrepresentation, failure to act prudently as a dealer/advisor, acting in face of a conflict of interest and fraud. The monitor also concluded that the potential defendants were likely to be banks or their employees, including the bank-associated dealers of ABCP.⁴⁸

Some noteholders claimed that both the CCAA and the relevant case-law did not permit the type of third party releases for negligence-based claims contemplated by the Plan.

In the result, the court held that the CCAA and the case-law did in fact permit the types of third party releases contemplated by the Plan:

It simply does not make either commercial, business or practical common sense to say a CCAA plan must inevitably fail because one creditor cannot sue another for a claim that is over and above entitlement in the security that is the subject of the restructuring, and which becomes significantly greater than the value of the security (in this case the Notes) that would be available in bankruptcy. In CCAA situations, factual context is everything. [...] There may well be situations on which compromise of some tort claims as between creditors is not directly related to the success of the Plan and therefore should not be released; that is not the case here.⁴⁹

The court held that it was unacceptable for the participants to be exposed to litigation under the Plan, wherein major concessions were made by all the parties.

The court went on to hold that claims of fraud, however, were of a much different nature than claims of negligence and should not be released under the Plan. Some noteholders argued that the definition of fraud under the Plan was not broad enough to permit all

claims of fraud. First, the exemption limited causes of action to authorized representatives of ABCP dealers. Second, the opposing noteholders were concerned that the permitted fraud claims would not cover instances where senior bank officials, possessing the requisite fraudulent intent, directed sales persons to make statements that the sales persons reasonably believed but that the senior officers knew to be false.⁵⁰ Justice Campbell allowed for the possibility that this type of fraud claim, and potentially others, might not be covered under the fraud exemption from the third-party releases. However, the court held that “the particular concern was to allow for those claims that might arise from knowingly false misrepresentation being made directly to the noteholders, who relied on the fraudulent misrepresentation and suffered damages as a result.”⁵¹ Justice Campbell held that the exemption as drafted accomplished that goal.

Appeal to the Court of Appeal for Ontario - *Metcalf & Mansfield Alternative Investments II Corp. (Re)*

Certain noteholders appealed Justice Campbell’s decision approving the Plan to the Ontario Court of Appeal. The noteholders appealed primarily on the basis that the Plan required them to grant third party releases for claims of negligence and some categories of fraud. The Court of Appeal granted leave to appeal on the basis that “[t]he proposed appeal raises issues of considerable importance to restructuring proceedings under the CCAA Canada-wide.”⁵²

The Court of Appeal described ABCP as “a sophisticated and hitherto well-accepted financial instrument [...] often presented by those selling it as a safe investment, somewhat like a guaranteed investment certificate.” The Court of Appeal went on to describe the ABCP market as “significant and administratively complex”.⁵³

For the complex market, the Investors Committee proposed a single but intricate plan involving all parties. The hope was that “the Plan would convert the Noteholders’ paper – which has been frozen and therefore effectively worthless for many months – into

new, long-term notes that would trade freely, but with a discounted face value. The hope is that a strong secondary market for the notes will emerge in the long run.”⁵⁴

The Plan called for the release of Canadian banks, dealers, noteholders, asset providers, issuer trustees, liquidity providers, and other market participants, being virtually all participants in the Canadian ABCP markets from any liability associated with ABCP, with the exception of certain narrow claims for fraud. The releases were *quid pro quo*, with each party releasing the other.⁵⁵

The Court of Appeal went on to consider whether the releases for negligence-based claims and some fraud-based claims were permitted under the CCAA and to review Justice Campbell’s decision that the Plan was fair and reasonable. Speaking for the court, Justice Blair noted the “skeletal” nature of the CCAA, and its role as “... remedial legislation to be liberally construed in accordance with the modern purposive approach to statutory interpretation” (at para. 44). Justice Blair held that (emphasis original, at para. 43):

... the CCAA permits the inclusion of third party releases [...] where those releases are reasonably connected to the proposed restructuring. I am led to this conclusion by a combination of (a) the open-ended, flexible character of the CCAA itself, (b) the broad nature of the term “compromise or arrangement” as used in the Act, and (c) the express statutory effect of the “double-majority” vote and court sanction which render the plan binding on all creditors ...

Justice Blair reasoned that the CCAA permits third-party releases that are “reasonably related” to the restructuring at issue because they are encompassed in the comprehensive terms “compromise” and “arrangement”. Such a reasonable connection existed in the Plan by virtue of the contributions being made by, for example, third parties like the assets providers.

In the result, the Court of Appeal upheld Justice Campbell’s decision:

*In insolvency restructuring proceedings, almost everyone loses something. To the extent that creditors are required to compromise their claims, it can always be proclaimed that their rights are being unfairly confiscated and that they are being called upon to make the equivalent of a further financial contribution to the compromise or arrangement.*⁵⁶

Quoting Justice Campbell, the Court of Appeal’s penultimate paragraph in its decisions reads:

*No Plan of this size and complexity could be expected to satisfy all affected by it. The size of the majority who have approved it is a testament to its overall fairness. No plan to address a crisis of this magnitude can work perfect equity among all stakeholders.*⁵⁷

Skeena Capital Trust and Devonshire Trust: Excluded from the Plan

Both Skeena Capital Trust and Devonshire Trust were subject to the Montreal Accord and the standstill agreements entered into as part of the Montreal Accord. However, neither the trusts nor the investors or other participants associated with the trusts were parties to the Plan under the CCAA described above.

Skeena Capital Trust Restructuring

Skeena Capital Trust (“Skeena”) was in the same position as other non-bank sponsored ABCP sponsors on August 13, 2007. Around the time of the market freeze, \$249 million Skeena Class A notes matured. Skeena was able to place \$176 million with investors and made draw requests from four separate liquidity providers for the remaining \$73 million. Three of the four liquidity providers provided funding for a total of \$40 million. Royal Bank of Canada (“Royal”) refused to advance the remainder of the funding on the basis that a market disruption had not occurred. Without full funding, Skeena was unable to pay the maturing notes: “[T]here is no provision for processing maturing notes of a specific security unless 100% of those notes maturing on any given day are funded. As a result, no transactions have been processed with respect to the Series A, Class A notes that have matured during the period from August 15th.”⁵⁸

Skeena was part of the Montreal Accord and entered into standstill agreements. By October 16, 2007, outside of the restructuring Plan, Skeena entered into an agreement whereby all of its investors were repaid their principal investment plus some accrued interest. The agreement was negotiated among Skeena’s Administrative Agent, Dundee Securities Corporation, its Co-Financial Arrangers, Edenbrook Hill Capital and Dundee Securities Corporation, the bank counterparties which provided assets to Skeena, as well as the Crawford Committee:

Under the proposed restructuring plan, \$2.1 billion of notes outstanding, covering “A” notes, “E” notes and term floating rate notes held by investors, will be redeemed at par plus a portion of the accrued interest; the amount of interest paid is proposed to be reduced by certain costs of the restructuring. Funding for this restructuring will be provided through the issuance of long term floating rate notes, issued by a new trust established for this purpose, to new investors which have been identified with the assistance of the bank counterparties and the Investors Committee.⁵⁹

This early success made investors hopeful for the Plan. However, Purdy Crawford warned: “[T]he substance and timing of the restructuring of Skeena are attributable in part to the unique facts and circumstances applicable to it. Alternative solutions will be required to effect successful restructurings of other trusts.”⁶⁰

As we will see below, with respect to Devonshire, not all stories had such a happy ending.

Devonshire Trust Litigation

Devonshire Trust (“Devonshire”), a sponsor and trust, had entered into two credit default swap transactions with Barclays Bank PLC (“Barclays”), as asset provider, liquidity provider and protection buyer (with Devonshire as the protection seller). These CDS transactions were also LSS transactions and therefore leveraged, as described above.

Although each entity fulfilled a separate and distinct role as, variously: sponsor, protection seller, protection buyer, asset provider and liquidity provider, the relationship between the parties was governed by a series of complex agreements: “To say that the series of contracts is complicated and inter-related is an understatement.”⁶¹ As protection buyer, Barclays essentially bargained with Devonshire, as protection seller, to assume the risk that a default would occur in return for periodic payments of premiums by the protection buyer. In this case, the agreement contemplated that Barclays would not actually make such payments as the credit protection was referential in nature.

Under the series of agreements, Devonshire was required to make initial payments to Barclays totaling \$600 million, for credit support, which Devonshire funded through a series of issuances of ABCP. At maturity, Barclays had the obligation to repay the amount of the initial payments to Barclays, less any amounts owed to Barclays under the agreements. DBRS required that the amount for the repayment be

secured. Therefore, the eligible credit support was paid into an account held by an appointed custodian.

Further, as liquidity provider, Barclays was required to make certain payments to Devonshire if a liquidity event occurred, which under Canadian-style liquidity was defined as a general market disruption.

Following the market freeze on August 13, 2007, Devonshire delivered market disruption notices to Barclays demanding liquidity payments. Barclays disputed that a market disruption had occurred and refused to make the requested liquidity payments.

On August 16, 2007, Devonshire and Barclays, among others, entered into standstill agreements contemplated by the Montreal Accord. Those standstill agreements were extended several times while the parties attempted to negotiate a restructuring. That restructuring has not yet occurred.

Barclays has claimed, in its amended reply and defence to counterclaim, that Devonshire was different from the other third party ABCP trusts due to the following cumulative reasons and therefore did not participate in the broader restructuring:

- a) a small number of credit default swaps;
- b) only one asset provider and liquidity provider;
- c) a small number of noteholders; and
- d) the Devonshire documents contained a term allowing termination by the asset provider in the event of the insolvency of the Trust.

On January 13, 2009, Barclays moved to enforce its rights under the agreements and sought to make certain liquidity payments to the trustee (in the amount of approximately \$71M) to satisfy its obligations further Devonshire’s liquidity calls in August 2007. Barclays also gave notice of early termination under the CDS contracts and sought to obtain the credit protection amount from the custodian. Devonshire contested Barclay’s interpretation of the standstill agreements and early termination notice and sought to obtain the credit protection amounts itself from the custodian.

Barclays began an action seeking, among other things, interim injunctive relief to prevent Devonshire’s trustee and indenture trustee from sending a notice to the

custodian requesting release of the credit protection amount. If Devonshire were to do so, in the face of Barclays' demand, the agreement with the custodian contemplated that the custodian would hold the funds and not accept instructions from either Barclays or Devonshire separately, but only from both of them jointly.

In the result, the court refused to grant the injunctive relief sought by Barclays as the Devonshire notices would maintain the *status quo* – the credit protection funds (being \$600 million) would remain with the custodian, pending a trial of the issues.⁶²

The court stated that one of the issues at trial will be whether the events of August 13-15, 2007 constituted a market disruption within the meaning of the contracts.⁶³ In fact, in its amended reply and defence to counterclaim, Barclays has specifically claimed that a “general market disruption event” is referable to the general Canadian ABCP market under the terms of the agreement and that a general market disruption of the general Canadian ABCP market, presumably to be distinguished from the smaller segment of the ABCP market discussed in this paper – the non-bank ABCP market, did not occur. In fact, Barclays claims that:

On or about August 11 to 12, 2007 [the week-end prior to the market freeze on Monday, August 13, 2007...] certain other large ABCP investors ... and certain other 3rd party ABCP Conduit Sponsors ... wrongfully, and lacking bona fides, conspired and agreed together to attempt to artificially manufacture a “Market Disruption Event” by simultaneously issuing Market Disruption Notices on August 13, 2007 and thereafter (the “attempted Manipulation”). ... [a certain] number of ABCP market participants ... in the course of the weekend prior to August 13, 2007, planned ... how to attempt to generate a Market Disruption.

The Attempted Manipulation involved a coordinated agreement amongst the group including certain large 3rd party ABCP Noteholders to refuse to roll maturing 3rd party ABCP and to issue Liquidity Notices with respect thereto. The predominant purpose of the Attempted Manipulation was to cause injury to Barclays (and other Asset Providers) by forcing Barclays to provide liquidity to Devonshire in the absence of a Market Disruption Event.

Barclays claims that Devonshire should be estopped from being able to claim that a market disruption occurred, based on their allegations that Devonshire conspired with other participants to cause the market freeze in order to make liquidity calls.

The gloves appear to be coming off in this case. A trial of the issue of whether a market disruption, as defined

by the agreements, occurred and, if it did, whether it was improperly caused by some of the participants, is likely to be as complex as the products and clearly controversial. The trial in this action is likely to commence in late 2009.

Regulatory Action

The Regulatory Environment Pre-Freeze

The OSA prohibits a commercial paper trust or other trust from trading in ABCP if such trade constitutes a “distribution” in Ontario unless either:

1. a preliminary and final prospectus have been filed by the trust with the OSC and either the trust has obtained registration as a dealer or underwriter under the OSA or the trade is made through a registrant (the “registration requirement”); or
2. the distribution is made in reliance on applicable registration and prospectus exemptions or a discretionary ruling issued by the OSC.

The trusts financed the purchase of securitized assets through the issuance of ABCP offered in reliance on the short-term debt exemption available under National Instrument 45-106 – *Prospectus and Registration Exemptions* (“NI 45-106”) of the Canadian Securities Administrator (“CSA”). The ABCP was sold through investment dealers who were registered under applicable securities laws.

The short-term debt exemption is contained in section 2.35 of NI 45-106, which provides as follows:

- (1) *The dealer registration requirement does not apply in respect of a trade in a negotiable promissory note or commercial paper maturing not more than one year from the date of issue, if the note or commercial paper traded:*
 - (a) *is not convertible or exchangeable into or accompanied by a right to purchase another security other than a security described in this section, and*
 - (b) *has an approved credit rating from an approved credit rating organization.*
- (2) *The prospectus requirement does not apply to a distribution of a security in the circumstances referred to in subsection (1).*

As a condition for utilizing the exemption available under section 2.35 of NI 45-106, ABCP must have a

maturity date of not more than one year from the date of issuance and have an “approved credit rating” from an “approved credit rating organization”.⁶⁴

In order for the trusts’ ABCP to be distributed under the short-term debt exemption, it had to be rated R-1 or higher by DBRS.

The requirement that short-term debt have an approved credit rating is designed to ensure the high credit quality of the debt. ABCP with an approved credit rating that otherwise satisfies the conditions of section 2.35 may be sold to any purchaser under the short-term debt exemption, regardless of such purchaser’s degree of sophistication or investment experience and regardless of the size of the investment.

The Regulatory Environment Post-Crisis – The Regulators React

The Provincial Securities Regulators

In the wake of the events on August 13, 2007, the various federal and provincial regulators moved to act. The provincial securities regulators, the Ontario Securities Commission (the “OSC”) and the *autorité des marchés financiers* in Quebec (the “AMF”), began investigations into the participants in the market over whom they had authority. For the OSC, that included the one public sponsor of the trusts – Coventree Inc. The OSC and the AMF also joined forces with IIROC, that began an investigation into the conduct of the investment dealers.

IIROC

IIROC, along with the CSA and other international agencies including the International Organization Securities Commission (“IOSCO”), published reports making various recommendations and seeking comment on proposed changes to its member regulations and guidelines.

In October of 2008, IIROC published a study entitled “Regulatory Study, Review and Recommendations concerning the manufacture and distribution by IIROC member firms of Third-Party Asset-Backed Commercial Paper in Canada”. IIROC’s findings have been extensively quoted from above, however, below is a summary of IIROC’s findings:

- a) The global credit derivatives market, which included such products as CDS and credit-linked notes, and Canadian third-party ABCP programmes grew rapidly and in parallel. Credit derivatives provided assets for third-party ABCP sponsors, enabling them to compete for ABCP market share in a market previously dominated by bank-sponsored ABCP programmes using more traditional assets.
- b) Third-party ABCP was issued under the same prospectus and registration exemptions that were intended for traditional commercial paper. They require, among other things, an “approved credit rating” from an “approved credit rating organization”. This is to be contrasted with the accredited investor exemption which focuses on the investor’s profile, not the product.
- c) Although ninety percent of third-party ABCP distribution was to institutional customers and inventory holdings, retail investors were attracted by low transaction costs enabling dealers who offered it to retail clients to cover transactions costs that left its yield advantage over other similarly rated money market instruments intact.
- d) Because of confidentiality agreements with sponsors, there was little transparency as to the specific underlying assets. Dealers and investors relied on the credit rating by DBRS and liquidity support for the programmes, albeit “Canadian-style” liquidity.
- e) Dealer members treated ABCP as a fungible money-market instrument offering a slightly higher yield but with little or no higher risk than other such instruments. They made no distinction between bank-sponsored and third party ABCP.
- f) Third-party ABPC was not regarded by most dealers as a new product distinct from bank-sponsored ABCP. Therefore, the dealers’ due diligence process for new products did not apply.

Along with the report, IIROC published for comment a list of best practices for product due diligence for its member dealers. The comments and the Best Practice Guidance Notice were published by IIROC on March 23, 2009 and the Best Practices Guidance Notice was updated and re-published on March 25, 2009 (the “IIROC Guidance

Notice”). Among the key best practices in the IIROC Guidance Notice are: (i) know your product; (ii) identification of new products; and (iii) due diligence.

(i) Know Your Product

Chief among the best practices recommendations was “know your product”. This rule stems from dealers’ obligations regarding suitability of investments for their clients. “Know your product” is already a requirement under IIROC Rule 29.27(a)(i). IIROC stated: “The requirement to ‘know your product’ is inherent in existing rules and does not require the adoption of a new rule. In addition, as the “you’re your product” requirement flows from existing rules, there is no need for a specific rule outlining the need for policies and procedures related to this requirement”.

The IIROC Guidance Notice received comments from members suggesting that dealers should be allowed rely on information provided by the issuer or manufacturer (sponsor) in complying with the know your product requirements. Although IIROC stated that member dealers are permitted to rely on issuers’ disclosure documents, member dealers may only rely on factual data and only in the absence of any apparent questionable data or claims. IIROC pointed out, however, that there is a difference between disclosure documents subject to securities laws and scrutiny by a securities regulator and sales materials. Dealers are required to make a judgment about the extent to which they can rely on disclosure materials – including whether it is informational or promotional and whether it is balanced in nature.

(ii) Identification of New Products

The IIROC Guidance Notice also requires that member dealers have a written procedure for vetting new products, which includes a list of factors which may tend to indicate that a member dealer is dealing with a new product. Even if a product is not new, if it is novel and complex, it may also require monitoring by the member. When dealing with an institutional investor, IIROC identified the following key characteristics of a new product, among others:

- (a) The product is new to the Canadian market place or to the dealer member (foreclosing reliance on due diligence done by other dealer members);
- (b) The product design raises a host of issues (including legal, funding, compliance or appropriateness) not previously considered;
- (c) The combined risk profile of the product is unique;
- (d) The product exposes the dealer member to market, liquidity or counterparty risk that is new or of a different magnitude; or
- (e) There has been a material modification to an existing product such that one or more of these factors is applicable.

The same criteria apply to new products for retail investors, in addition to the following criteria:

- (a) The product has never previously been sold to the dealer member’s retail clients;
- (b) The product has never previously been sold by a particular registered representation, a new type of retail investor or a particular geographic region; or
- (c) Certain changes to an existing product that change timing, expect loss or volatility.

These additional criteria recognize that retail investors differ from institutional investors, even if they are purchasing an exempt product or are an accredited investor. Further, such evaluation is by necessity fact-specific:

The list is not necessarily exhaustive of all factors that determine whether a product requires due diligence review. Dealer members should not simply assume that if something is similar to a product already in the marketplace, whether offered by the firm or competitors, that little or no review is necessary. [...] IIROC believes that when dealer members are unsure as to whether a product warrants review, the best practice is to err on the side of caution.⁶⁵

(iii) Due Diligence for New Products

IIROC goes on to recommend the components of a successful due diligence program:

- A standardized process that requires a written “new product” proposal;
- A preliminary assessment of a proposed product or concept by personnel or a department designated in the firm’s policies and procedures to determine, among other things, whether it is a new product or a material modification of an existing product, and the appropriate level of internal review;
- For new products or material modifications to existing products, detailed review by a committee or working group made up of representatives from all relevant sectors of the firm, including compliance, legal, finance, marketing, sales, and operations;
- A formal decision to approve, disapprove, or table the proposal by a new product committee or other decision-making group that includes members of the firm’s senior management;
- An assessment of the extent of training in product features and risks necessary to ensure that registered representatives and supervisors can judge the suitability of recommendations and sales to clients and the development and implementation of the necessary training;
- If the product is approved, a determination of the appropriate level of and process for post-approval follow-up, including consideration of:
 - Monitoring of customer complaints and grievances related to the product;
 - Reassessment of training needs on a continuing basis;
 - Monitoring of compliance with restrictions placed on the sale of the product;
 - Periodic reassessment of the suitability of the product.

The CSA

The CSA also published its own report and recommendations in October 2008: “Securities Regulatory Proposals from the 2007-08 Credit Market Turmoil and its Effect on the ABCP Market in Canada.” The comment period for the recommendations was extended to February 14, 2009 and at the time of publication of this paper, the comments and final proposal have not been released.

In its recommendations, the CSA makes a number of reform proposals to better regulate all aspects of the exempt market and ABCP in particular. Of particular note are the following proposals:

- a) Implementing a regulatory framework applicable to credit rating agencies that would require compliance with the recently amended code of conduct established by IOSCO. In addition, the CSA is considering requiring public disclosure of all information provided by an issuer that is used by a credit rating agency in rating an asset backed security;
- b) Amending the short-term debt exemption to make it unavailable for sales of asset-backed short-term debt including ABCP. This would require issuers who sell these products to do so by way of prospectus, or under another exemption;
- c) Reducing reliance on the use of credit ratings in securities legislation;
- d) Addressing the roles played by dealers and advisers with respect to ABCP; and
- e) Reviewing specific issues regarding mutual fund investments in ABCP.

Other Reports and Recommendations

On January 12, 2009, the Expert Panel on Securities Reform, lead by Thomas Hockin, delivered its Final Report and Recommendations (the “Hockin Report”). Chief among its recommendations was the creation of a single federal securities regulator to combat concerns about systemic risk in the capital markets, with accountability for the national markets as a whole:

The Canadian Securities Commission would be responsible for policymaking and rulemaking activities as well as the investigation and prosecution of regulatory offences. The Commission would work to meet the core objectives of securities regulation by following our guiding principles of regulatory conduct, including facilitating the reduction of systemic risk in the larger financial system.

On March 24, 2009, David Dodge, former Bank of Canada Governor, told a symposium that he believed that CDOs should be regulated as insurance products and that trading of CDOs should be banned: “They are insurance. Credit default swaps should not be allowed to be traded.”⁶⁶

In addition, several academic studies have been done recommending reform. John Chant, a professor of economics at Simon Fraser University, produced and published a research study for the Expert Panel on Securities Reform entitled “The ABCP Crisis in Canada: The Implications for the Regulation of the Financial Markets.” Chant explores, from an economics view point, the advent of the non-bank sponsored ABCP market in Canada and then its sudden fall, which Chant says was predictable. Chant makes the following reform recommendations:

- a) With respect to the prospectus exemptions:
 - i. Exemptions from prospectus requirements be based on principle, according to an issuer’s activities; and
 - ii. The prospectus exemption for commercial paper be reserved for single source issues holding traditional assets;
- a) Credit rating agencies register with securities authorities, adopt separate rating scales for structured products and make clearer the risks they cover; and
- b) The rules governing the sale and distribution of structured products reflect the characteristics of the product.⁶⁷

Chant also recommends that the banking regulator review the continuing suitability of on- and off-balance sheet distinctions for banking-related activities with respect to regulatory capital requirements and that the communication between regulators should be reviewed to determine whether greater communication could prevent or reduce the severity of crises in the future.⁶⁸

With respect to (a) above, Chant argues that traditional securitization products properly qualify for the prospectus exemption under securities laws, as described above. However, as products developed, they became more complex and more opaque to investors and were often highly leveraged. He argues that these types of products were not intended to be exempted by securities regulators and a principled approach to regulation of these products should be developed to avoid technical avoidance of the rules.⁶⁹

With respect to (b) above, Chant points to the interrelatedness of the credit ratings agencies with the

trust sponsors on the one hand (the sponsors significant pay fees to the credit ratings agencies to rate their products and credit rating agencies make recommendations to sponsors in respect of their products to achieve higher ratings) and the dependence on the other hand of investors on the ratings to buy products. Chant recommends that credit ratings agencies be registered with securities administrators and that in order to be registered, the agencies adopt a code of conduct based on the principles enunciated by IOSCO, namely: quality in the ratings process; monitoring and updating of the sponsor and trust; integrity in the ratings process; independence and avoidance of conflict of interest; and enumerated responsibilities to the investing public and issuers (including publishing policies and methodologies used to generate the ratings and publishing information regarding historical default rates of the ratings categories).⁷⁰

With respect to (c) above, Chant states that “[o]ne aftermath of the crisis is that it has become apparent that ABCP was sold to some investors for whom it was not appropriate. The restructuring efforts were stymied for some time by the discovery that more than 1,800 individual investors were among the holders of notes covered by the Montreal Accord. In addition, corporations, pension funds and others held ABCP in the apparent belief that it was a safe, short-term investment.”⁷¹

Chant states that better disclosure may not be the answer, due to the complexity of the products and instead supports IIROC’s approach in Rule 1800 requiring a dealer to designate experts responsible for reviewing the transactions and determining suitability.

However, Chant states that the timing of these initiatives must be right. The wake of the storm is not the appropriate time to implement a new set of regulations. Rather, Chant cautions that in order to be effective, the full extent of the aftermath of the subprime and ABCP crises must be known.

The Council on Foreign Relations issued a special report authored by Benn Steil in March 2009 entitled “Lessons of the Financial Crisis”. In that report, Steil states that for there to be lasting policy reform, the reform must, generally, accord with the self-interest of participants in the market.⁷² Steil argues that top-down regulation

cannot adjust quickly enough to such complex and evolving markets and heavy-handed regulation could also act to stifle growth.

To that end, among other things, Steil recommends the following reform:

- a) Borrower screening and monitoring – Steil argues that in the current system, originators do not have the necessary incentives to vet borrowers. In the U.S. mortgage market, lenders expected to sell off the mortgages they originated, thereby transferring away the risk of default. Steil advocates that “restrictions should be applied to lenders such that they are obliged to retain a material economic interest in the asset they originate.”⁷³
- b) Market infrastructure – In face of the collapse of major players in the U.S. financial market, and the U.S. government’s bail-out plans to prevent other collapses, Steil states that the financial integrity of financial institutions is integral to reform. Steil states that financial institutions should be strictly and continuously regulated to ensure that they are adequately financed.⁷⁴
- c) Corporate governance – Steil states that management is currently incentivised to create short term wealth, to capitalize on bonuses and share allocation plans tied to often quarterly performance targets, regardless of long term effects on the company. Steil argues for long term compensation reforms including claw-backs and longer vesting periods. Steil also states that risk monitoring should be made a primary Board of Directors focus.⁷⁵

In March 2009, the Financial Services Authority (“FSA”) in the United Kingdom released “The Turner Review – A Regulatory Response to the Global Banking Crisis”, written by Lord Adair Turner, Chairman of the FSA at the request of the Chancellor of the Exchequer. Lord Turner’s mandate was to review and make recommendations for reforming UK and international approaches to the way banks are regulated.

Lord Turner made 34 recommendations further to his review of the causes of the global banking crisis, including reforms to: (a) capital adequacy, accounting and liquidity, (b) institutional and geographic coverage of regulation; (c) firm risk management and governance; and (d) global and European cross-border banks.

Of particular interest is The Turner Review’s recommendation for minimum global standards. This is significant especially for the United Kingdom as part of the European Union and a global player in the markets. Presumably, such global standards could also apply in North America. The Turner Review recommends at recommendations 25 and 26 that:

25. International coordination of bank supervision should be enhanced by

- *The establishment and effective operation of colleges of supervisors for the largest complex and cross-border financial institutions.*
- *The pre-emptive development of crisis coordination mechanisms and contingency plans between supervisors, central banks and finance ministries.*

26. The FSA should be prepared more actively to use its powers to require strongly capitalised local subsidiaries, local liquidity and limits to firm activity, if needed to complement improved international coordination.

One of the obvious questions in respect of global standard is regulatory enforcement, especially by local authorities including over non-resident institutions. This issue would have to be addressed both at the global level and at the local level.

At recommendation 23, The Turner Review recommends:

23. The Walker Review⁷⁶ should consider in particular:

- *Whether changes in governance structure are required to increase the independence of risk management functions.*
- *The skill level and time commitment required for non-executive directors of large complex banks to perform effective oversight of risks and provide challenge to executive strategies.*

If changes in governance structure are made (or not made), public disclosure of those risk policies and the reason for the change (or the reason for lack of change) will be required for meaningful public disclosure.⁷⁷ In this case, transparency will assist the public to understand what process is in place to protect their investment from unreasonable risk.

Evaluating Regulatory Reform

Chant’s message of patience has considerable merit. Although swift action may sooth weary parties, only considered action will prevent a similar crisis in the future. In addition, as much as it may be desirable to lay blame, all parties, including the regulators and investors,

allowed the market to go on as long as it did, so long as things appeared to be functioning smoothly. However, change is needed to allow for more meaningful disclosure surrounding complex products and safeguards in place to ensure that only suitable investors purchase such products.

To that end, IIROC's Best Practices Guideline Notice will ensure that dealers take the time to understand the investments they are selling to investors. In addition, Chant's recommendations in respect of the prospectus exemptions are noteworthy.

In addition, there is merit to amendments to the accredited investor definition in NI 45-106. Presently, an individual is described as an accredited investor in the following circumstances:

(j) an individual who, either alone or with a spouse, beneficially owns, directly or indirectly, financial assets having an aggregate realizable value that before taxes, but net of any related liabilities, exceeds \$1,000,000,

(k) an individual whose net income before taxes exceeded \$200,000 in each of the 2 most recent calendar years or whose net income before taxes combined with that of a spouse exceeded \$300,000 in each of the 2 most recent calendar years and who, in either case, reasonably expects to exceed that net income level in the current calendar year,

(l) an individual who, either alone or with a spouse, has net assets of at least \$5,000,000,

Much like the principled approach to the prospectus exemption advocated by Chant, a measure of assets or income alone should not determine the ability of an investor to understand and accept the risks inherent in unregulated products and markets. In addition, the minimum amount exemption is not a proper guide either. It was generally understood that a minimum investment of \$100,000 for non-bank sponsored ABCP was required, which many participants believed would effectively bar retail investors from the market. As stated above however, following the market freeze, it was discovered that retail investors held in excess of \$200 million in non-bank sponsored ABCP, with one single retail investor holding in excess of \$20 million.⁷⁸

It is suggested therefore that a more principled approach be taken to evaluating whether an individual retail investor should be presumed to have the requisite

knowledge and ability to withstand high risk investments, even if they are packaged as low risk products.

Litigation Risk

ABCP Claims

Under the restructuring Plan for the non-bank sponsored Canadian ABCP market, the parties entered into extensive third party releases. The only claims that were not released were certain claims of fraud against the dealers. At the time of writing this paper, no such claims had been commenced.

For the one unstructured trust outside of the Plan, Devonshire, a proposed restructuring has descended into litigation between the trust on the one hand and the asset provider, liquidity provider and protection buyer on the other. A trial of the matters at issue in the litigation will be complex. Other litigation may also be commenced if the standstill agreements are no longer in effect. The current litigation is a snapshot of one aspect of possible litigation that could have occurred in an ABCP market without the implementation of the restructuring Plan. It is clear, judging from the complexity of the issues facing the parties in the Devonshire action, that what the Plan accomplished was avoiding hundreds of lawsuits, litigating very complex issues over many years. As a result of the compromises made by the participants, it is clear that their and the court's time and resources were spared the throes of litigation.

Litigation Risk Generally for Complex Products

With complex products comes litigation risk. If the product is difficult or complex to understand, then an issuer or dealer risks not fully understanding it or the associated risks. Without a proper understanding of the product, there is the further risk of not being able to properly explain it - in the case of an issuer, to the dealer and, in the case of the dealer, to the investor. A dealer may therefore not be able to make a proper suitability determination. This can lead to both regulatory and civil liability for the issuer and the dealer.

With the relatively new civil liability for reporting issuers in the secondary market for continuous disclosure violations, shareholder activism is on the rise. That shareholder activism more and more is taking the form of class actions. In January of 2009, NERA Economic Consulting released a report showing that Canadian securities class action suits increased 125% in 2008 over 2007.⁷⁹ The percentage figure may sound more impressive than the actual numbers (in 2007, there were four suits filed and in 2008 there were nine), but it is a substantial increase nonetheless, especially when you consider that in both 2005 and 2006, the number of suits filed was also four. However, when compared to the United States, which had 255 securities class action filings in 2008, Canada lags far behind.⁸⁰

However, the implications of a class action suit should not be dismissed. The NERA study also found that of the 42 securities class actions filed in Canada since 1997, 20 have settled for a total of \$3.6 billion and only one has reached a trial decision – *Danier Leather Inc.*, which was appealed to the Supreme Court of Canada. Of the 42 actions, 9 had cross-border elements with the United States. The remaining 21 suits claim upwards of \$3 billion in damages.⁸¹

The dearth of case law in this area, with only *Danier Leather* going to trial, makes it difficult to predict court decisions. A favourable result for the class at a certification hearing is enough to rattle even the steeliest nerves of a defendant issuer. This uncertainty contributes to the high settlement rate of class action suits in this area.

In addition, shareholders, or their lawyers, are becoming more activist. With respect to options back-dating, Siskinds LLP issued letters in 2007 to numerous TSX listed companies demanding independent investigations into their options practices. On behalf of investors, Siskinds commenced an action against two of those issuers in relation to options back-dating.

Shareholder activism with respect to subprime has already begun in the U.S. Shareholders of Citigroup Inc. (“Citigroup”) brought a derivative action against the current and former directors and officers of Citigroup seeking to recover losses arising from exposure to the subprime lending market.⁸² The shareholders alleged

that the directors and officers breached their fiduciary duties by failing to properly manage and monitor the risks associated with subprime lending and for failing to properly disclose Citigroup’s exposure to subprime assets. The shareholders alleged that the directors and officers ignored extensive “red flags” about the credit markets in pursuit of short term gains at the expense of the long term viability of the Company.

The shareholders alleged that most of Citigroup’s exposure was due to CDOs and special investment vehicles, which issued ABCP to then purchase loan receivables. The court held that the problems with the subprime markets left Citigroup unable to pay its investors – the special investment vehicles held subprime mortgages that had decreased in value and the market for ABCP had become illiquid. In the end, Citigroup was required to fund the special investment vehicles to the tune of \$49 billion, despite the arm’s length nature of the vehicles.

The shareholders sought to hold the directors and officers liable for these payments and resulting decrease in share price of Citigroup’s stock.

The defendants brought a motion to dismiss the claims. The court held that all but one of the shareholders’ claims should be dismissed. The court stated: “It is understandable that investors, and others, want to find someone to hold responsible for these losses, and it is often difficult to distinguish between a desire to blame *someone* and a desire to force those responsible to account for their wrongdoing.”⁸³

The court held that the directors and officers had not committed any wrongdoing in respect of subprime exposure: “Ultimately, the discretion granted directors and managers allows them to maximize shareholder value in the long terms by taking risks without the debilitating fear that they will be held personally liable if the company experiences losses.”⁸⁴

In Canada, the Supreme Court of Canada in the *BCE Inc. v. 1976 Debenture Holders* decision⁸⁵ has given strong affirmation to the business judgment rule, at least in change of control transactions, if the Board can show that it followed a proper process. Therefore, going forward, it may be important for a Board or management to properly document the decision to accept risk as a business decision.

Conclusion

With the collapse of the Canadian non-bank sponsored ABCP market, and a downturn in the financial markets as a whole, came the tremendous urge to identify and punish any and all wrongdoers. The regulators stepped in to attempt to restore investor confidence. What they found was a complex relatively unregulated market that had operated to achieve staggering profits in the right environment. When that environment changed, which change was precipitated by external factors, not the least of which was fear, the model ceased to work.

Although it might be satisfying, a rush to action in these circumstances in an effort to prevent a similar crisis would likely create more issues than it will solve. A solution will necessarily have to be as complex and flexible as the market itself and such an animal cannot be created overnight. It may also take time for the participants (including the regulators) to achieve the necessary distance from the events to recognize and acknowledge their own contributions to the collapse.

It will also take time to measure the ultimate success of the restructuring Plan. The Plan is likely a unique, one-off event not to be repeated. This type of resolution cannot be counted on in future financial crises. Therefore, participants in the market should conduct themselves on the basis that litigation is a possibility. Such litigation would result in claims and claims-over against various market participants, with investors looking to a host of market participants for recovery.

Well-defined rules of the game will help all participants avoid litigation and in the event of a dispute, will set standards by which conduct can be fairly judged. Such rules will also help restore investor confidence in the markets. These rules will have to be as novel as markets themselves to achieve the stated goals of securities regulation:

- a) To provide protection to investors from unfair, improper or fraudulent practices; and
- b) To foster fair and efficient capital markets and confidence in the capital markets.⁸⁶

More regulation is just more regulation. A better system should be the goal.

[An earlier version of this paper was presented to the 8th Annual Advanced Institute on Securities Litigation and Enforcement, Toronto, (April 20-21, 2009) and to the Commercial Bar Association North American Meeting 2009, Chicago (May 29, 2009).]

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- ² Bank of Canada *Financial System Review*, June 2007, at 24.
- ³ *Ibid* at 6.
- ⁴ *Ibid* at 21.
- ⁵ *Ibid*.
- ⁶ Investment Industry Regulatory Organization of Canada (IIROC), "Regulatory Study, Review and Recommendations concerning the manufacture and distribution by IIROC member firms of Third-Party Asset-Backed Commercial Paper in Canada", October 2008 at 10 [IIROC Study].
- ⁷ IIROC Study at 10. The percentage loss in the reference portfolio at which a CDO begins to participate in default losses is called the attachment point. The point at which it ceases to participate in further default losses is the detachment point.
- ⁸ Bank of Canada *Financial System Review*, June 2007 at 21.
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- ¹⁰ Bank of Canada *Financial System Review*, June 2007 at 24.
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- ²⁰ Bank of Canada *Financial System Review*, June 2007 at 25.
- ²¹ The reasons for increased delinquency may include a combination of lax lending standards, potential fraud, interest rate adjustments on adjustable rate mortgages and a softening of house prices in the United States led to a significant increase in the default and foreclosure rates for subprime mortgages: see CSA Proposal at 5.
- ²² Bank of Canada *Financial System Review*, December 2007 at 8.
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- ²⁴ *Ibid* at 3-4.
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³¹ IIROC Study at 70.

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³³ *Ibid.*

³⁴ Affidavit of Hy Bloom sworn April 14, 2008, filed in the *Metcalfe & Mansfield S.C.J.* proceeding at para 79.

³⁵ Affidavit of Purdy Crawford at para 9.

³⁶ Affidavit of Purdy Crawford at para 10 and Bank of Canada *Financial System Review*, December 2007 at 15.

³⁷ Affidavit of Purdy Crawford at paras 52-53.

³⁸ Affidavit of Purdy Crawford at paras 53-4.

³⁹ Affidavit of Purdy Crawford at para 56.

⁴⁰ Affidavit of Purdy Crawford at paras 53 and 55.

⁴¹ Affidavit of Purdy Crawford at para 19.

⁴² Affidavit of Purdy Crawford at para 74.

⁴³ *Metcalfe & Mansfield C.A.* at para 24.

⁴⁴ *Ibid* at para 25.

⁴⁵ *Ibid* at paras 26-7.

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⁶⁴ The terms "approved credit rating" and "approved credit rating organization" are defined in National Instrument 81-102 of the CSA.

⁶⁵ The IIROC Guidance Notice at 14.

⁶⁶ Joe Schneider "U.S., Canadian Banks Underestimating Loan Losses, Dodge Says", Bloomberg.com.

⁶⁷ John Chant, "The ABCP Crisis in Canada: The Implications for the Regulation of the Financial Markets", A Research Study Prepared for the Expert Panel on Securities Regulation at 5.

⁶⁸ *Ibid.*

⁶⁹ *Ibid* at 25-26.

⁷⁰ *Ibid* at 26-32.

⁷¹ *Ibid* at 38.

⁷² Council on Foreign Relations, "Lessons of the Financial Crisis" (March 2009) at 12.

⁷³ *Ibid* at 17-18.

⁷⁴ *Ibid* at 20.

⁷⁵ *Ibid* at 21-22.

⁷⁶ The Walker Review is a separate review by the FSA which is scheduled to report at the end of 2009 and will look at improving the professionalism and independence of risk management functions, embedding risk in remuneration policies and improving the skill level and time commitment of non-executive directors.

⁷⁷ A similar point is made by Robin Johnson, partner at Eversheds LLP, in his comment on The Turner Review.

⁷⁸ Factum of Representation Co-Counsel for the Retail Holders of ABCP, *Metcalfe & Mansfield S.C.J.*, filed May 5, 2008.

⁷⁹ NERA Economic Consulting, "Trends in Canadian Securities Class Actions: 1997-2008", January 2009.

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⁸¹ *Ibid.*

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⁸³ *Ibid* at 58.

⁸⁴ *Ibid.*

⁸⁵ [2008] S.C.J. No. 37, [2008] 3 S.C.R. 560.

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