COURT FILE NO.: 09-CV-384829
DATE: 20091119

SUPERIOR COURT OF JUSTICE - ONTARIO

RE: TWO-TYME RECYCLING INC. v. RONALD WOODS, DARLENE JOAN WOODS, RALPH WOODS, PATRICIA WOODS, TARA LYNN WOODS and AMANDA LOUISE WOODS

BEFORE: MADAM JUSTICE HARVISON YOUNG

COUNSEL: EDWARD J. BABIN, CLIFFORD JACKMAN, for the Plaintiff

BRADLEY TEPLITSKY, for the Defendants

DATE HEARD: November 3, 2009

REASONS FOR DECISION

Introduction

[1] This is an application to set aside a Mareva Injunction and Certificate of Pending Litigation on the basis of made material non-disclosure and a false statements allegedly made in the affidavit material filed in support of the ex parte motion.

[2] The Plaintiff, Two-Tyme Recycling Inc., ("TTR") is a waste management company which was started by the Defendant Ron Woods ("Ron") and his wife Darlene Woods ("Darlene") at some point prior to 2003. For a number of years, it was run as a family business, employing a number of family members including their daughters, Tara and Amanda. For a number of years, the business was run out of the family home which was owned jointly by Ron and Darlene and Ron's parents Ralph and Patricia Woods, who are also named as defendants in this action.

[3] Over a number of years, a number of shareholders invested in TTR although the business continued to be run primarily by Ron and Darlene Woods. Ron ran the operational side and Darlene ran the office and administrative operations. The application for the Mareva injunction was made following the discovery of irregularities and alleged fraud while TTR was preparing for a sale of some of its assets earlier in 2009.

[4] Perell J. granted the ex parte injunction and Certificate of Pending Litigation against the Woods' home on August 12, 2009. This was extended by Belobaba J. on August 24, 2009 and was unopposed by the Defendants who filed no material on that motion.

[5] In addition to their claim that the affidavit evidence violated the rules requiring full and frank disclosure, the Defendants submit that Mr. Kirk Schizas, the current President of TTR, the primary affiant., failed to disclose that his evidence was, in some important respects, based on information and belief and that these omissions in themselves are grounds for vacating the order.

[6] In opposing this motion, TTR denies that there was any material non-disclosure. It argues that, in any event, the Woods' submissions relating to non-disclosure or false statements concern largely secondary allegations in relation to the principal alleged fraud. TTR's central claim is that the Woods diverted over $600,000 of Company funds to a TD Band account which was supposed to have been used for very limited purposes, and then withdrew and misappropriated those funds.

[7] TTR also submits that Mr. Schizas' evidence was based on his own knowledge, and that to the extent that it was not, that he identified the source of the information. In the alternative, the TTR argues that, even if there was some material non-disclosure on its part, the Court retains a residual discretion and should exercise it to maintain the injunction as, to dissolving it would result in an injustice.

The Issues

[8] The issues on this motion to set aside may be set out as follows:

(i) was there deliberate misleading or non-disclosure?
(ii) was there material misleading or non-disclosure?
(iii) was the affidavit evidence deficient for not being within the knowledge of the affiant and failing to disclose the source of the information?
(iv) assuming that the Court answers "no" to (i) but "yes" to any or both of (i) and (ii) above, should the Court exercise its residual discretion to continue the injunction despite these deficiencies?

[9] For the reasons that follow, I conclude that the Defendants have not established that the Plaintiffs violated the rules requiring full and frank disclosure on an ex parte motion so as to warrant the setting aside of the Mareva Injunction in this case.

Background

[10] In 2003, TTR sold some shares to Kirk Schizas, Costa Schizas and Christopher Rotter, leaving Ron with a 51% interest. In 2006, Ron sold a 10% interest to Richard Heim and another 10% interest to Robert and Maureen Beggs, leaving Ron with a 31% interest.

[11] By about 2006, a number of the new shareholders were concerned that the business was not doing as well as they had expected. Mr. Rotter became more involved, though still on a part-time basis, in the sales and marketing side with a view to increasing revenue. Although this seems to have resulted in an increase in revenue, TTR continued to struggle financially. One of the significant problems appeared to be the amount of outstanding accounts receivable.

[12] In December 2008, TTR received a letter of intent from BFI to purchase the assets of the front end business, consisting for the most part of vehicles, containers and customer contracts, including accounts receivable. An agreement was finalized and dated March 24, 2009, signed by all the shareholders including Ron Woods. The closing date was set for June 1, 2009.

[13] As part of the assets being sold included both customer agreements and accounts receivable, it was essential to ensure that these records were in order. In the course of this review, a number of problems became apparent. One major concern was the fact that in attempting to reconcile TTR's accounts receivable, customers who, according to TTR records were shown as owing money, claimed to have paid their accounts.

[14] The events between March 24, 2009 and the end of May, 2009 are detailed in the materials before the court and need not be recited here except to say that by May 27, 2009, Ron Woods was demanding that the sale not proceed. He did, in fact, move for an injunction to prevent the closing on June 1, 2009 which was dismissed by Wilton-Siegel J. At a shareholders' meeting held on Friday, May 29, 2009, Ron Woods was removed as an officer. The employment of Darlene, Tara and Amanda was terminated on or shortly after that date.

[15] In addition, part of the agreement with BFI was that TTR had to release the security interest held by TD Bank in its assets. Prior to June, 2006, the TD Bank account had been TTR's business account. In June, 2006, TTR had moved the business account to HSBC. It did not close the TD Bank account, of which Ron and Darlene were the only signatories, because an outstanding balance on an old line of credit remained. It is clear from all the evidence filed before the Court that this account was not to be used as a business account, but was to be very minimally active as was necessary to cover a few automatic debits from the account.

[16] It became apparent, however, in the course of the investigation that took place earlier in 2009, that there had actually been enormous activity through this account. Deposits in the amount of $678,045.14 in customer revenue had been made into the account. The amounts deposited had then been withdrawn by Darlene or transferred to credit cards or other personal accounts held by the Woods, and virtually none of it remains.

[17] These payments were not entered in the company program, TRUX, and did not appear in any company records. Most if not all of these funds came from customers paying bills, which, according to the company records, had not been paid. These facts are not contested, although Darlene denies that she forged the earlier statements sent to the shareholders.

[18] In its notice of motion dated August 12, 2009 in which it sought, ex parte, a Mareva Injunction and a Certificate of Pending Litigation against the Woods' home, the Plaintiffs set out the "particulars of the misappropriation of TTR's property, and other fraudulent conduct, of which TTR has to date become aware…" as follows:

(a) Using a second corporate bank account, in the name of TTR, with the Toronto-Dominion Bank ("TD Bank"), to deposit $678,045.14 in customer revenue paid to TTR;
(b) Removing the full amount of these deposits for the personal benefit of the defendants;
(c) Disguising activity within the second corporate bank account (an account known to the other shareholders, but intended solely for the purpose of making continuing interest payments on an outstanding corporate line of credit) through the preparation of false bank statements that concealed information with respect to all transactions apart from the authorized interest payments;
(d) Receipt of substantial cash payments from TTR's customers not deposited to the credit of TTR;
(e) Utilizing credits earned by TTR through business trade accounts for their personal benefit and not for the benefit of the company;
(f) The removal of important accounting a business records from the offices of TTR; and
(g) Refusal to return a loader owned by TTR, for which the defendant Ronald has been charged with theft by the authorities.

[19] The Plaintiff filed two affidavits in support of the motion. Kirk Schizas swore one on August 11, 2009, and Chris Rotter swore another on May 31, 2009. Darlene Woods swore three affidavits, dated September 10, 23, and 25, 2009. Ronald Woods swore one dated September 10, 2009.

The Law

[20] It is well established that the failure of a moving party to make full and fair disclosure may result in the dissolution of an ex parte injunction. As the Defendants submit, the test on whether to set aside an ex-parte order for non-disclosure of material facts is whether the omitted disclosure might have had an impact on the original order being made: see *United States v. Yemec*, 2003 CarswellOnt 3762 at para. 35; *Wachsmann v. Zahler* 2002 CarswellOnt 3594 at para 8. Having said this, it is also now clear that, apart from cases in which the failure to make full and fair disclosure is deliberate, the Court has a residual discretion to decline to set aside the injunction in such circumstances.

[21] A mistake or non-disclosure in an ex parte application does not necessarily mean that an order obtained by that application must be discharged. The mistake or non-disclosure must be material. As Justice Sharpe wrote in *United States v. Friedland* 1996 CarswellOnt 5566 (Ct. J. (Gen. Div.) (W.L.), "a plaintiff should not be deprived of a remedy because there are mere

imperfections in the affidavit or because inconsequential facts have not been disclosed" (para. 31).

> The Court is entitled to consider whether the alleged non-disclosure would have affected the decision to issue the injunction when deciding whether it was material. In a case where the Court finds that such a matter of non-disclosure was not material, it may decline to vacate the injunction: see, for example, *Alberta (Securities Commission) v. Maitland Capital Ltd.* 2008 CarswellOnt 4141 (S.C.J.) (W.L.).
>
> In the event that the Court actually makes a finding of material non-disclosure, the Court retains a residual discretion to in any event maintain the injunction. As Justice Sharpe has written in the latest edition of his text, *Injunctions and Specific Performance*, where "dissolution would result in injustice to the plaintiff, the punitive rationale may be outweighed": *United States v. Yemec*, supra, at .

Analysis

[22] The issues to be considered, then, are whether the Defendants have established that the ex parte injunction was granted on the basis of (i) material that was deliberately false or misleading, (ii) material non-disclosure or inaccuracies; and (iii) information that was not within the knowledge of the affiant. In the event that the Court concludes that there was material (though unintentional) non-disclosure or misinformation, the Court may consider whether, pursuant to its residual discretion, it should decline to vacate the injunction.

[23] At the beginning of his submissions, Mr. Teplitsky for the Defendants stated that he was not taking issue in this proceeding with the allegations of fraud concerning the TD Bank account. This, in light of the evidence before the Court, was a sensible position for him to take. It is an important aspect of the context of the Defendants' motion to set aside the Mareva Injunction that the evidence of the TD Bank fraud is central to this Plaintiff's case, and was central to the ex parte application before Perell J.

[24] The Defendants argue, to begin with, that there were a number of lies in the affidavit evidence. I disagree that the Defendants have established this. TTR says that it is wrong to focus on alleged inaccuracies or items of non-disclosure in isolation, but they must be considered in the context of all the evidence and cross-examinations. I agree.

[25] In their submissions, both parties addressed all the grounds to set aside the injunction in terms of the allegations relating to the TD Bank, those relating to Bray's Auto & Metal Recycling, and those relating to the Trade Business Exchange and My Trade Bank. I will do so in the same manner as follows.

The TD Bank Issue

[26] As outlined above, the Plaintiff's central allegation is that the Defendants' misappropriated, at a minimum, over $600,000 in just less than three years by diverting

payments made by customers which should have been deposited into the HSBC account into the TD Bank account. These amounts were never entered into the TRUX accounting system and never appeared in the TTR books. The amounts deposited, however, did get transferred out of the account for the benefit of Ron and Darlene Woods, either as cash withdrawals, transfers to personal credit card accounts, or to personal bank accounts. The entire amount appears to have been dissipated. Significant portions of the funds were withdrawn by Darlene and apparently spent at Casino Rama.

[27] In her affidavit dated September 10, 2009, Darlene Woods claimed that the funds were used to repay loans they had made to TTR, and to reimburse them for company expenses. She also claimed that it was appropriate for TTR to have paid some expenses relating to the Woods' home as, prior to 2007, the business was run from their home, and after that, the home continued to be operated as a second location for TTR. In her affidavit sworn September 25, 2009, one day after the first day of her cross-examination and before its continuation on September 29, 2009, she claimed that she had been sexually assaulted by Mr. Rotter and that he had directed her as far as the use of the TD Bank account, and claimed that some of the cash withdrawals had been given to him. He has vigorously denied these allegations.

[28] The Woods claim that the Schizas affidavit failed to make disclosure of material facts relating to number of aspects of this issue. They claim that Mr. Schizas' failure to inform the Court that the Woods' home had been and continued, to some extent, to operate as a TTR place of business was one example of material non-disclosure as was the fact that the Woods' sometimes put business items on their personal credit cards for which they were entitled to be reimbursed by TTR.

[29] There is, in my view, no material non-disclosure established with respect to the TD Bank issue. First of all, the evidence indicates that the Woods did not file any expense reports with respect to any of the amounts withdrawn by them from the TD Bank, which would have been the proper and routine procedure. Darlene Woods herself, the evidence indicates, filed monthly expense report claims on the "Simply Accounting" system used for this purpose. For this reason, the alleged non-disclosure that the Woods' home was used for TTR purposes is beside the point. TTR did not see any such claims. This omission was, in my view, neither material nor deliberate.

[30] Similarly, the suggestion that Mr. Schizas should have mentioned the shareholder loans is without merit; as there was no company record of the repayment or request for repayment of such loans. The essence of the TTR's complaint is the fact that TTR knew nothing of the funds that were going into or coming out of this account. None of the amounts that customers were paying that were deposited into the TD Bank account showed up in company records at all. In short, the failure to mention the above facts was, in the context of these facts, not material.

[31] As TTR submitted in its factum, the denials and assertions made by the Defendants in this matter have consistently shifted and grown more improbable. None of them change the fact that substantial Company funds were flowing into the TD Account and then being withdrawn, transferred into other accounts, or otherwise being used for the benefit of the Defendants,

without ever being recorded on the books and records of the Company. Indeed, Darlene Woods admits this was the case, but now claims, in effect, that Mr. Rotter made her do it.

Bray's Auto & Metal Recycling

[32] Mr. Schizas says in his affidavit that Chris Rotter had explained that the company should have received $146,000 from the sale of cash metal from Bray's Auto & Metal Recycling, implying that the Defendants stole this amount. The Defendants argue that this was a clear lie. TTR acknowledges that the implication was not entirely accurate, but submits that as it is clear that the source of information was Chris Rotter and the Rotter affidavit says the $146,000 is unaccounted for, it is obvious that Mr. Schizas was drawing the inference. The Rotter affidavit reviews the basis for this statement, and was also before Perell J. The reasonable conclusion is that Mr. Schizas merely misinterpreted the Rotter affidavit. The Defendants have not discharged the heavy onus of showing the Mr. Schizas lied. It does not make sense that he would have when the Rotter affidavit was part of the same record.

[33] This reference to the $146,000 in Mr. Schizas' affidavit is one of the examples the Defendants rely on in support of its argument that Mr. Schizas did not have first hand knowledge and failed to identify the source of his belief. I disagree with this. As Mr. Babin for the Plaintiff submitted, it is clear from reading this portion of the affidavit that Mr. Schizas is relying on Mr. Rotter, and Bray's itself, as the source of his information.

[34] The issues relating to Bray's and the cash apparently unaccounted for were quite central to the Defendants's submissions to set aside the injunction. As TTR submitted, however, this issue was not central to the original application for the injunction before Perell J.; it was mentioned neither in the factum nor in oral submissions. In addition, as Mr. Babin argued, the central and material importance of the Bray issue, especially if one reads the Schizas and Rotter affidavits together, is the fact that cash receipts were (and remain) unaccounted for. There is nothing in evidence to suggest that this is not the case. In fact, the reference in the Schizas affidavit to the Bray's issue is in a section with the heading "cash receipts". Accordingly, I include that there was no material inaccuracy relating to this issue.

Trade Business Exchange and My Trade Bank

[35] The "Trade Business Exchange" and "My Trade Bank" were business exchange programs through which TTR provided services to local businesses and received goods and services in exchange. The Schizas affidavit says: "TTR has learned that the defendants provided the services of TTR to many local businesses, but rather than receive goods and services of benefit to the company, received personal benefits". The Defendants raise a number of issues with this.

[36] Subsequent evidence and cross examination revealed that Mr. Schizas had not disclosed the fact that, to his knowledge at the time he swore the first affidavit, other shareholders had used the trade business exchange account to receive personal benefits. Mr. Teplitsky submitted that this was intentional and material non-disclosure and that, had it been disclosed, it could have affected the outcome of the motion.

[37] In retrospect, I agree with the Defendants that Mr. Schizas should have disclosed this fact. I am not satisfied, however, that the motion might not have been granted had he disclosed this fact, for two reasons. First, as Mr. Babin submitted forcefully, the big issue concerning the Trade Business Exchange program was not merely the fact that the Defendants were benefiting personally from it, but rather the extent of, as he put it, the abuse.

[38] Second, the benefits received included expensive home improvements such as carpeting and a hot tub, which are relevant because of the "link" with the home that is the subject of the Certificate of Pending Litigation. Third, and again, the "elephant in the room" throughout all of this is the rest of the evidence that was before the Court relating to the money that was being deposited into the TD Bank account, withdrawn to the benefit of the Woods. I am also not satisfied that Mr. Schizas withheld this fact intentionally.

[39] I conclude that the failure to disclose the fact that other shareholders has used the trade business exchange to receive personal benefits was not material in the circumstances of this motion. If it was, I would find, as I will discuss below, that the court should exercise its residual discretion to dismiss the motion on the facts of this case.

[40] The Defendants also submit that Mr. Schizas did not disclose the source of his information and belief on this issue. Again, I disagree. It is clear that he relies on information from Chris Rotter that he had seen the hot tub at the Woods home. He also relied on reports from Trade Business Exchange and My Trade Bank, which are attached to the Schizas affidavit.

[41] In summary, a review of all the material, including the cross-examinations of Mr. Schizas and Darlene Woods, does not satisfy me that any imperfections in the materials files on the ex parte motion were "material" in the sense discussed by Sharpe J.A., in *United States v. Friedland*, *supra*. I am unable to say that, but for the imperfections alluded to, the injunction might not have been granted. The main reason for this is the fact that the evidence relied on by TTC is very strong, particularly with respect to the TD Bank fraud and the misappropriation of over $600,000 which has, it seems, been largely dissipated. Within this context, the problems alluded to by the Defendants, such as that discussed in the context of unaccounted for cash payments apparently made by Bray's, do not seem as material as they might if that was the or the main basis upon which the ex parte injunction had been granted to begin with.

Residual discretion

[42] As I have indicated, I am not satisfied that TTR has deliberately misstated or omitted any material fact. Moreover, I am not satisfied that the Plaintiff failed to disclose any facts that were material in the circumstances of this case, and I am not satisfied that the decision to grant the motion was based on inadmissible hearsay and that the injunction might not otherwise have been granted. I am satisfied that, in any case, this is a case in which the Court's residual discretion should be exercised to dismiss the Defendant's motion to set aside the injunction.

[43] As I indicated, the only issue that, in my view, should have been disclosed is the fact that other shareholders also received some personal benefits through the trade business exchange program. I am not satisfied that this was material and that the injunction might not otherwise

have been granted, and I am of the view that this is an appropriate circumstance for the Court to exercise its jurisdiction in favour of continuing the injunction despite my view that this is something that should have been disclosed.

[44] In *Sherwood Dash Inc. v. Woodview Products Inc.*, Justice Perell reviewed the law on this issue and observed that interpreting the rules against non-disclosure too strictly might encourage unscrupulous defendants to allege material non-disclosure when they have a hopeless case on the merits. The purpose of the rule is to deprive the plaintiff of an advantage improperly obtained and to remind litigants of the duty to be frank and candid at ex parte applications. Where those principles do not apply, the rule is not as strictly enforced.

[45] A review of this case as a whole does not indicate that the Plaintiff secured "an advantage improperly obtained". Viewed as a whole, including the affidavits and the cross-examinations, the evidence of misappropriation remains overwhelming.

[46] In addition, the Court should not, in reinforcing the importance of being frank and candid in ex parte applications, insist on unattainable standards of perfection. The period from January through to the bringing of this injunction application in August, 2009 was a stressful one. Ron Woods was removed as a shareholder at the end of May, 2009 and the employment of the other members of the Woods family was terminated. Many company records disappeared at that time and computer access to records was blocked (although some records have been recovered). The investigations into the fraud were continuing and TTR was struggling to get on with its business as well, having discovered very significant fraud. As Lord Slade noted in *Brink's Mat Ltd v. Elcombe and Others*(1987), [1988] 3 All E.R. 188 (Eng. C.A.) at 194, 195, ex parte applications, by their very nature "usually necessitate the giving and taking of instructions and the preparation of the requisite drafts in some haste". The borderline between material facts and non-material facts is not always clear. For this reason, and without discounting the "heavy duty of candour and care" which falls upon those making such applications, Lord Slade cautioned against application of the principle to "extreme lengths".

[47] Similarly, Sharpe J.A. observed as follows in *America v. Friedland*, [1996] O.J. No. 4399 at paras. 30-31 (Gen. Div.):

> The duty of full and frank disclosure is, however, not to be imposed in a formal or mechanical manner. Ex parte applications are almost by definition brought quickly and with little time for preparation of material. A plaintiff should not be deprived of a remedy because there are mere imperfections in the affidavit or because inconsequential facts have not been disclosed. There must be some latitude and the defects complained of must be relevant and material to the discretion to be exercised by the Court. (See *Mooney v. Orr*, (1994) 100 B.C.L.R. (2d) 335; *Rust Check v. Buckowski* (1994), 58 C.P.R. (3d) 324.

[48] Lord Slade also noted that complaints of material non-disclosure appear to arise frequently where they constitute the only hope of obtaining the discharge of injunctions in cases where there is little hope of doing so on the substantial merits of the case or on the balance of

convenience. He called this strategy a *tabula in naufragio* (a "plank in a shipwreck"); the last, desperate hope of a defendant who wishes to save their assets before an inevitable judgment is rendered against them at trial: see *Brink's Mat Ltd v. Elcombe and Others*, supra, at 195.

[49] As Mr. Babin pointed out, the Plaintiffs were putting this motion material together shortly in difficult circumstance as outlined above. This has meant not only that it has been harder to investigate this issue, but it has impaired the operations of the business. While Mr. Babin candidly acknowledged that this was not an "overnight emergency injunction" case, he noted that the two weeks between the receipt of the bank information from TD Bank and this motion were intense. This was, in my view, an example of a circumstance in which the imposition of a standard of perfection would be unjust.

[50] As I have discussed above, I do not find that there were material omissions or mistakes in the record before Perell J. Given the extent of the evidence before Perell J., particularly relating to the TD Bank account, it is very difficult to imagine that the Mareva Injunction might not have been granted but for the matters raised by the Defendants.

[51] For the foregoing reasons, I conclude that the motion must be dismissed. If the parties are unable to agree as to the costs of this motion, they may make written submissions to me within 30 days, on a schedule which they agree to between themselves.

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Harvison Young J.

DATE: November 19, 2009