

affidavit of Dale Reagan

sworn before me, this 18th

day of June 2007


A COMMISSIONER FOR TAKING AFFIDAVITS

COURT FILE NO.: 04-CV-280686
COURT FILE NO.: 04-CV-278076CM2
DATE: 20050405

SUPERIOR COURT OF JUSTICE - ONTARIO

RE: Bridlewood Co-operative Inc. v. Superintendent of Financial Services

AND RE: Co-operative Housing Federation of Canada and Ken Skinner v. Bridlewood Co-operative Inc., Jeffrey McPherson, Shirley Bartholomew, Marion Stowe, Gayle Brown, Brian Renaud, Brian Garant and Dan Bornais

BEFORE: Mr. Justice H.J.W. Siegel

COUNSEL: *C.J. Tzekas and Megan Ferrier*, for the Applicant Bridlewood Co-operative Inc., and the Respondents Jeffrey McPherson, Shirley Bartholomew, Marion Stowe, Gayle Brown, Brian Renaud, Brian Garant and Dan Bornais

Stephen Scharbach, for the Respondent Superintendent of Financial Services

Murray Klippenstein and Vilko Zbogar, for the Applicants Co-operative Housing Federation of Canada and Ken Skinner

HEARD: March 1, 2005

ENDORSEMENT

[1] On this application Bridlewood Co-operative Inc. ("Bridlewood" or the "Co-op") applies to the Court for:

- (a) an order interpreting and determining the rights of the parties under the *Co-operative Corporations Act*, R.S.O. 1990, c. C. 35 (the "CCA"), including an interpretation of the words "sale", "other disposition" and "distribute" as those words are used in sections 68.1 and 171 of the CCA; and
- (b) a declaration that a proposed sale by Bridlewood of its homes to the members who presently occupy them, at prices reflecting the members' rights of occupancy, is permissible pursuant to the CCA.

[2] On the companion application by Co-operative Housing Federation of Canada ("CHFC") and Ken Skinner (Skinner"), a member of the Co-op and occupant of one of the homes, these parties seek, among other things:

- (a) a permanent injunction (1) prohibiting and enjoining Bridlewood from directly or indirectly transferring title to, or any interest in, the lands or housing units owned by the Co-op and or other assets

of the Co-op, or any part of the Co-op's property to any member or member's relative, and (2) prohibiting and enjoining any and all directors, officers, agents and members of the Co-op from taking any steps toward directly or indirectly transferring title to, or any interest in, any or all of the Co-op's property to any member or member's relative, and from spending any Co-op funds for that purpose; and

(b) an order pursuant to section 178 of the CCA requiring the Co-op and its directors, officers and employees to comply with subsection 5(3.1) and sections 98, 108, 171.2 and 171.3 of the CCA, articles 6 and 13 of the Co-op's Articles of Incorporation, and the Co-op's By-laws, by not taking any of the actions referred to the preceding paragraph.

[3] The two applications have been consolidated on consent of the parties.

Background

[4] The parties have agreed on the following facts.

[5] Bridlewood is a non-profit housing co-operative located in the Town of Essex, in the County of Essex.

[6] Bridlewood was incorporated on October 6, 1975 as a co-operative without share capital. Bridlewood enacted By-Law No. 1 on November 14, 1993 to regulate the general affairs of its business. Two additional By-laws, No. 2 and No. 3, were also enacted to deal respectively with occupancy agreements and sector support.

[7] Bridlewood owns and operates a co-operative housing complex consisting of 131 separate, 3-bedroom dwellings ("homes" or "units"). Each home is located on a separate lot registered on a plan of subdivision.

[8] Each member of Bridlewood occupies a home under a written agreement (an "occupancy agreement") entered into between Bridlewood and the member.

[9] The Financial Services Commission of Ontario ("FSCO") is an agency of the Ontario Ministry of Finance created by the *Financial Services Commission Act, 1997*, S.O. 1997, c. 28 (the "FSCA"). FSCO's responsibilities include enforcement of compliance with the CCA.

[10] CHFC is a non-profit co-operative association incorporated under the laws of Canada, the objects of which include ensuring the growth, stability, and independence of the non-profit co-operative housing movement in Canada. Bridlewood is not a member of CHFC.

[11] In September, 2003, at a special general meeting, Bridlewood's members authorized its board of directors to investigate the feasibility of the Co-op selling its homes to the members

who presently occupy them. It is intended that once the homes are sold to the members, the members would be free to occupy, rent, mortgage, sell or otherwise convey the homes to others without restriction.

[12] Bridlewood retained Ray Bower Appraisal Services Inc. to prepare an appraisal of one of Bridlewood's homes (the "Appraisal Report"). Because each home is subject to a right of occupancy, the Appraisal Report values the home subject to this right. The Appraisal Report also estimates the hypothetical fair market value of the home if it were unencumbered by this right of occupancy. The Appraisal Report concludes that the market value of the home is \$127,000 before taking into account the member's occupancy right, and that the market value is \$59,400 if the particular member's right of occupancy is found, as a matter of law, to survive the sale of the unit. As set out below, the market value becomes approximately \$51,000 using the average member's age in the calculation, rather than the age of the particular member whose home was the subject of the Appraisal Report.

[13] Bridlewood believes that its proposed sales are permitted by section 68.1 of the CCA, subject to securing various authorizations. It is FSCO's view that the proposed sales would amount to a distribution of Bridlewood's property to its members, which is prohibited by section 171.2 of the CCA.

[14] The parties seek a determination from the Court as to whether Bridlewood's proposal is a "sale" or "other disposition" of its property, as permitted by section 68.1 of the CCA, or whether it would amount to a distribution of Bridlewood's property to its members, in contravention of section 171.2 of the CCA.

The Legal Framework

[15] The following provisions of Bridlewood's Articles of Incorporation, its by-laws, the Occupancy Agreement and the CCA are relevant for the issues addressed on this motion.

[16] Article 6 of Bridlewood's Articles of Incorporation includes the following purposes:

(a) to own or lease and operate land and buildings for the purpose of providing residential accommodation to persons, the majority of whom shall be members of the Co-operative and who will occupy the housing units otherwise than as owners;

(b) to enter into occupancy agreements with its members upon such terms as it may deem advisable...

[17] In addition, section 5(3.1) of the CCA deems the Articles of Incorporation to include provisions to the effect that the primary objective of the Co-op is to provide housing to its members and that its activities are to be carried on without the purpose of gain for its members.

[18] Article 3.1 of By-Law No. 1 provides:

Membership in the Co-operative shall be open to all persons 18 years of age and over who are in agreement with the purpose and objects of the Co-operative and whose written application for membership on the form provided for that purpose, accompanied by the prescribed ten dollar (\$10.00) application fee has been approved by the directors.

[19] Article 8 of the Articles of Incorporation provides that those persons wishing to become members must give Bridlewood a loan, if required by the board of directors. The amount of the loan currently required of all applicants for membership is \$500. Article 11 sets the fee to become a member of Bridlewood at \$10.

[20] Article 1.5 of By-law No. 2, Bridlewood's Occupancy Agreement by-law, provides that:

Each acceptance of an application for occupancy shall contain the following conditions:

(a) that the applicant shall have also been accepted for membership in the co-operative;

(b) that the applicant enter into an Occupancy Agreement in the form prescribed from time to time by the Board; and

(c) that the applicant shall have made a Member's Loan to the Co-operative in the amount prescribed from time to time by the Board, and the membership fee shall also have been paid in full, plus Application Fee ten dollars (\$10.00) non returnable.

[21] In accordance with these by-laws, all members of Bridlewood are required to enter into a standard form occupancy agreement that, for the purposes of these applications, the parties have agreed is substantially in the form of the Occupancy Agreement attached as Schedule "G" to the Supplementary Application Record (the "Occupancy Agreement"). Once signed, the Occupancy Agreement gives the member the exclusive right to occupy one of Bridlewood's 131 homes. The Occupancy Agreement provides:

... in consideration of the terms of the Agreement and information given by the Member on his application, the Co-op hereby offers to the Member and the Member hereby accepts the Personal Right of Occupancy of the land and premises being Lot _____, Plan M-63, Town of Essex, and known municipally as _____, (referred to as the "home") upon the Terms and Conditions set forth in this Agreement, the Incorporation documents, By-laws and Rules of the Co-op, now in effect or hereinafter adopted by the Co-op from the date of this Agreement until its termination.

[22] Article 3 of the Occupancy Agreement grants each member the following right to peaceable possession:

In return for the fulfilment of the terms of this Agreement, the Co-op promises that the Member, during this period of Occupancy, may enjoy sole use and benefit of the described home and may enjoy in common with other members the use of all community property and facilities of the Co-op.

The member shall occupy the home only as a private dwelling and for no other purpose, and may enjoy the use, in common with the other Members of the Co-op, of all community property and facilities of the project, so long as he continues to be a member of the Co-op, occupies the home and abides by the terms of this Agreement.

[23] As a non-profit housing co-operative, Bridlewood must comply with the provisions of the CCA including, in particular, the provisions of sections 171.1 - 171.25 which are specific to non-profit housing co-operatives. Section 171.4 of the CCA provides:

Only a member of a non-profit housing co-operative has a right to occupy a member unit of the co-operative and, upon ceasing to be a member, a person ceases to have any occupancy rights.

[24] Section 171.8(1) of the CCA provides:

If a member of a non-profit housing co-operative does not have occupancy rights, his or her membership may be terminated in accordance with subsection 49(3) or section 66 but, if the member has occupancy rights, his or her membership or occupancy rights may be terminated only if both are terminated concurrently in accordance with subsection (2).

Issues

[25] The application raises the following two issues:

1. is the Bridlewood proposal permitted under the CCA?
2. does the Bridlewood proposal give rise to a breach of fiduciary duties or is it otherwise contrary to subsection 5(3.1) and section 108 of the CCA, article 13 of the Articles of Incorporation or the objects and purposes of Bridlewood?

I will discuss the first issue. Given the disposition of that issue below, I have not addressed the second issue.

Permission under the CCA

[26] The issue of permission under the CCA requires consideration of two questions:

1. is a sale of all or substantially all of the property of a Co-op permitted under the CCA?
2. does the Bridlewood proposal involve the sale of the Bridlewood property at its fair market value?

Is the Sale Permitted?

[27] It is agreed that Bridlewood has authority to sell all or substantially all of its property, if authorized by special resolution of its members, by virtue of section 68.1 of the CCA. It is further agreed that there is nothing in the CCA that prohibits Bridlewood from selling its property to its current members or that precludes dissolution of a Co-op. There is, therefore, no question that the Bridlewood proposal involves a sale of property for the purposes of section 68.1 of the CCA whether or not the sale is at the fair market value of the Co-op's property.

[28] However, sub-section 171.2(1) of the CCA provides that "a non-profit housing co-operative shall not distribute or pay any of its property to its members during its existence or on its dissolution." In addition, section 5(3.1)(c) of the CCA provides that, on dissolution, the remaining property of a non-profit housing co-operative after payment of liabilities shall be transferred or distributed among one or more non-profit housing co-operatives or charitable organizations. Article 13(b) of the Articles of Incorporation is substantially to the same effect.

[29] The parties therefore agree that a sale of property by a non-profit housing co-operative to its members at less than fair market value would constitute a distribution and be precluded by section 171.2(1) of the CCA.

[30] Accordingly, the issue of whether the Proposal is permitted under the CCA turns on whether or not the proposed sale of the property of Bridlewood is determined to be at its fair market value. If it is, then the Proposal is not prohibited by the CCA. If it is not, then the Proposal contemplates a distribution prohibited under section 171.2.

Does the Proposal Involve the Sale of the Bridlewood Property at its Fair Market Value?

[31] The determination of whether the Bridlewood proposal involves the sale of property at its fair market value turns on whether the occupancy rights of the occupants of the Co-op units can be characterized as rights of value in these occupants. In turn, this issue depends upon whether or not the occupancy rights are enforceable against third party purchasers of the units.

Position of Bridlewood

[32] Bridlewood argues that the occupancy rights of members should be enforceable against third party purchasers. The following three factual matters are important for understanding the position of the Co-op.

[33] First, all of Bridlewood's members have occupancy rights in their respective units. Over the last 10 years, no Bridlewood member has had his or her occupancy rights or membership terminated. Essentially, once a member enters into an Occupancy Agreement, the member has a right to use his or her home for as long as he or she wishes, subject only to honouring Bridlewood's minimal financial and conduct requirements.

[34] Second, article 1 of the Occupancy Agreement provides for payment of a monthly "occupancy charge" determined to be "the Member's fair share of the sum required by the Co-op and estimated by the Board of Directors to meet its annual expenses". It is understood that the occupancy charge does not include any component for profit or return on equity. Accordingly, Bridlewood proceeds on the basis that a purchaser of a unit subject to an Occupancy Agreement would be unable to charge rent which exceeds the amount necessary to recover the operating costs of the unit and reasonable reserves for future costs.

[35] Third, the Appraisal Report indicates a market rental for the units could be approximately \$1,000 and that the monthly occupancy charge is \$525. The Appraisal Report present valued the monthly benefit of \$475 received in respect of each unit by its occupants at approximately \$75,965, using the average member's age. As the Appraisal Report found the market value of the units before taking the right of occupancy into account to be \$127,000, Bridlewood's proposal would fix the fair market value of the units at approximately \$51,000.

[36] Bridlewood argues that the occupancy rights are enforceable against third party purchasers on three grounds. It submits that each ground supports its position that it has retained only the "reversionary interest" in the homes and cannot demand payment for the remaining value attributable to the occupancy rights because these rights have already been granted to the occupant members.

[37] First, it says the occupant acquires a contractual right under the Occupancy Agreement, based on the payment of consideration in the form of the \$500 loan contemplated by article 17 of the Occupancy Agreement and article 7 of By-law No. 1. It also relies on the absence of any provision in the Occupancy Agreement that terminates the Agreement on a sale of the applicable unit.

[38] Second, it asserts a statutory basis in reliance on the provisions of subsection 171.8 of the CCA, which sets out a code with respect to termination of membership in the Co-op. In particular, it points to paragraph 2 of subsection 171.8(2), which provides that membership and occupancy rights may be terminated only if the member ceases to occupy a member unit or on a ground set out in the by-laws. It also relies on subsection 171.8(1), cited above, which provides that if a member has occupancy rights, his or her membership or occupancy rights may be terminated only if both are terminated concurrently in accordance with subsection 171.8(2).

[39] Lastly, Bridlewood argues that the principle in *Freeborn v. Goodman*, [1969] S.C.R. 923 is applicable in the present action. I would note, however, that this decision involved enforcement in equity of a disposition of an interest in property secured by a covenant for quiet possession for which significant consideration had been paid and of which the third party had full knowledge. The present action involves determination of the extent of contractual rights for which the occupant has given only a \$500 loan as consideration and is, therefore, distinguishable.

Analysis and Conclusions

[40] I have concluded that the following principles govern the operation of the Occupancy Agreement, and the occupancy rights of the occupant of a unit, in the event of a sale of a unit to a third party:

1. an occupant can prevent a sale to a third party purchaser on the grounds that it would render the Co-op incapable of performing its obligations under the Occupancy Agreement;
2. after a sale of a unit, the Occupancy Agreement continues until it is terminated in accordance with its terms but is effective only against the Co-op and is not enforceable against a third party purchaser of a unit; and
3. upon a sale of a unit, an occupant becomes a tenant for purposes of the *Tenant Protection Act, 1997* S.O. 1997, c.24, initially having a monthly rental equal to the monthly charge payable to the Co-op immediately prior to the sale.

[41] In summary, the occupancy right of a member of the Co-op is a contractual right, supplemented by statutory rights under the CCA, that operates only between the member and the Co-op or an assignee of the Co-op which is also governed by the CCA. The occupancy right includes the right to prevent a sale of the unit to a third party. It does not, however, survive any such sale if an occupant consents to, or otherwise acquiesces, in the sale. At the point at which a sale occurs, the occupant becomes a tenant for purposes of the *Tenant Protection Act, 1997*. While the Occupancy Agreement may technically subsist after a sale of the applicable unit, there is no longer a member unit of the Co-op that can be the subject matter of that Agreement, and, accordingly, the Agreement ceases to have any legal significance. While termination of the member's membership in the Co-op does not occur automatically on the sale, as a practical matter it is probable it will occur in due course, at which time the Occupancy Agreement will also formally terminate in accordance with its terms.

[42] The following are my reasons in reaching these conclusions.

[43] First, the rights and obligations of the parties under the Occupancy Agreement cannot continue to operate in a meaningful manner after a sale to a third party. This indicates a clear intention that the Occupancy Agreement is to have effect only as an agreement between the Co-op and a member of the Co-op.

[44] For example, the right of peaceable possession in article 3 is subject to the occupant continuing to be a member of the Co-op. Similarly, article 5 provides that the member will surrender possession if he or she ceases to be a member of the Co-op and article 11 provides that the Occupancy Agreement terminates upon an occupant ceasing to be a member of the Co-op. As the occupant will cease to be a member of the Co-op at some point after a sale, if the Occupancy Agreement is intended to survive after that time as a right enforceable against a purchaser, these provisions must be rendered inoperative. There is, however, no provision in the Occupancy Agreement, the Occupancy By-Law or the CCA which addresses this legal consequence of sale by terminating the legal effect of these provisions while preserving the remainder of the Occupancy Agreement.

[45] Similarly, a number of provisions cannot operate without the continued existence or involvement of the Co-op. In article 3, the right of peaceable possession extends to all community property and facilities of the Co-op. Article 11 sets out an elaborate mechanism for expulsion of the occupant as a member of the Co-op, including an appeal mechanism to the board of directors of the Co-op. Article 14 provides that, in the event of a fire, the Co-op may decide not to restore the home in which event the Occupancy Agreement will be terminated but the member will be given the first opportunity to occupy a similar home in the Co-op when it becomes vacant. Article 22 provides that the right to assign the Occupancy Agreement is subject to the by-laws of the Co-op. Lastly, the provisions for reimbursement of improvements under article 27, which contemplate selection of a new occupant willing to pay the improvements made by a departing occupant, presuppose a waiting list maintained by the Co-op and a selection procedure administered by the Co-op. There is no provision in the Occupancy Agreement or otherwise which addresses the operation of any of the foregoing provisions after a sale of a unit.

[46] Second, I think that the definition of "occupancy rights" in sections 171.1 – 171.25 of the CCA is restricted to rights in respect of a unit owned by the Co-op, or an assignee of the Co-op that is governed by the CCA. While there is no formal definition of occupancy rights in the CCA, I believe the intended definition is found in section 171.4(1) which refers to "a right to occupy a member unit of the Co-operative" in the first part of the section. Using this definition, a member ceases to have occupancy rights when the member's unit ceases to be a "member unit of the Co-operative" as a result of a sale. Nothing in this section preserves occupancy rights in respect of a "member unit of the Co-operative" after a sale of the unit.

[47] Third, the absence of any provision in section 171.8 that contemplates continuation of occupancy rights after a sale of a unit supports the conclusion that such rights were intended to exist only in the context of a non-profit housing co-operative governed by the CCA. Section 171.8 is directed at the termination of membership rights in a non-profit housing co-operative rather than occupancy rights. It treats the termination of occupancy rights as a necessary concomitant of the termination of membership rights. It does not contemplate the scenario envisaged by Bridlewood in which membership rights, being redundant, are terminated and occupancy rights are continued. In any event, it cannot be interpreted to preserve occupancy rights after a sale based on the survival of membership rights. Bridlewood, itself, has recognized that continuation of membership rights after a sale would be inappropriate and has indicated it intends to terminate the membership rights in the Co-op immediately after the sale. I would also

observe that any attempt to avoid the operation of these provisions by maintaining the membership rights in the Co-op after a sale would probably be objectionable.

[48] Fourth, the Occupancy Agreement must be interpreted in the context of the purpose of the Co-op and the prohibition in section 171.2(1) of the CCA against distribution or payment of the Co-op's property to its members. Each of these contextual elements implies a limited grant of occupancy to members that is not enforceable against third party purchasers.

[49] As set out above, the objects of Bridlewood contemplate the provision "of rental accommodation to persons, the majority of whom shall be members of the Co-operative and who will occupy the housing units otherwise than as owners" and section 5(3.1)(a) of the CCA includes a deemed provision that the primary purpose of the Co-op is to provide housing to its members. Implicit in these objects is the intention that the housing units will be made available to new members upon a current occupant ceasing to be a member. The fact that membership in Bridlewood has not changed for ten years is irrelevant for this purpose. Permanent occupying rights - that is, rights that are enforceable against third party purchasers of the units - are therefore inconsistent with the stated purpose of the Co-op. That purpose is to provide accommodation to the current members of the Co-op from time to time in member units of the Co-op. It does not extend to conferring a special benefit on the members of the Co-op at a particular point in time.

[50] Similarly, the Occupancy Agreement must be interpreted in light of the provisions of section 171.2(1) of the CCA. If there are two possible interpretations of the Occupancy Agreement, the Court should give effect to the interpretation that does not contravene the CCA. Bridlewood says quite frankly that it is proceeding on the basis that it owns only a "reversionary interest" in the homes because it has given the value of the occupancy rights to its member occupants. This is a clear acknowledgement that under its interpretation of the Occupancy Agreement, Bridlewood believes that it has disposed of property of value to its members. If the Co-op were correct in its interpretation, the grant of occupancy rights would contravene the prohibition in section 171.2(1) of the CCA against the disposition of property of the Co-op to its members. I conclude, however, that the Occupancy Agreement should be interpreted more narrowly to provide for a concept of occupancy rights that excludes such a distribution.

[51] Fifth, the Occupancy Agreement contains a subordination provision which is intended to provide any mortgagee with the ability to sell the units under a power of sale free and clear of any occupancy rights. While this could be interpreted as supporting the applicant's position that occupancy rights would otherwise exist, I think its significance is otherwise. Based on the analysis set out above, the effect of the subordination provision is to remove the risk that occupants will assert rights of tenants upon sale and thereby excludes the associated cost of removal of the tenants if required as a condition of sale.

[52] Accordingly, I conclude that occupancy rights under an Occupancy Agreement are not enforceable against a third party purchaser. On this basis, the fair market value of a unit on a sale would be calculated without any significant reduction for the present value of a member's occupancy rights. Accordingly, as the Bridlewood proposal contemplates a sale to the members

of property of the Co-op at less than its fair market value, if implemented, the proposal would constitute a "distribution" for the purposes of section 171.2(1) of the CCA.

Additional Issues

[53] The Co-op also seeks a declaration that the proposed sale of homes to the members who currently occupy them, at prices reflecting the members' rights of occupancy, is "permissible" pursuant to the CCA. The CHFC and Skinner seek the relief set out above.

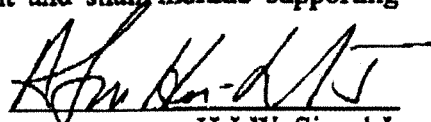
[54] The request for such relief raises the question of whether Bridlewood's proposal gives rise to a breach of fiduciary duty on the part of the directors of Bridlewood or a breach of their statutory duty under section 108 of the CCA. It similarly raises the question of whether the proposal contravenes subsection 5(3.1) of the CCA, article 13 of Bridlewood's Articles of Incorporation or the objects of the Co-op as set out in Article 6(a) thereof.

[55] Given the determination of this Court with respect to the issue of the treatment of occupancy rights for purposes of determining the fair market value of the units, I believe the views of the Court on these additional issues would be *obiter dicta*. I do not believe it would be appropriate to address these hypothetical issues on this motion and I decline to do so.

[56] I would note, in addition, that Bridlewood has advised the Court that it does not intend to implement the Bridlewood proposal before a final determination is made by this Court with respect to the treatment of occupancy rights for purposes of the valuation of the units under its proposal. It has also indicated that further action would be required, including formal approval by its board of directors and members, before the final form of its proposal could be implemented. These circumstances constitute a further reason why it would be premature for the Court to address these additional issues.

Costs

[57] The parties shall have 30 days from the date of these reasons to make written submissions with respect to the disposition of costs in this matter and a further ten days from the date of receipt of the submissions of the other parties to make any reply submissions they may wish to make. Any such submissions seeking costs shall identify all lawyers on the matter, their respective years of call and rates actually charged to the client and shall include supporting documentation as to both time and disbursements.


H.J.W. Siegel J.

DATE: April 5, 2005