

**ONTARIO  
SUPERIOR COURT OF JUSTICE**

BETWEEN:

**JENNIFER HOLLEY**

Plaintiff

- and -

**THE NORTHERN TRUST COMPANY, CANADA  
and THE ROYAL TRUST COMPANY**

Defendants

Proceeding Under the *Class Proceedings Act, 1992*

**AMENDED STATEMENT OF CLAIM**

**(Notice of Action Issued August 27, 2012)**

**RELIEF CLAIMED**

1. The Plaintiff, on her own behalf and on behalf of the class of persons defined at paragraph 4 below, seeks:

- a) damages for fraudulent breach of trust, and actual and/or constructive fraud in the amount of \$60 million;
- b) a declaration that the defendants acted fraudulently in relation to their role as trustees in overseeing the Nortel HWT (defined below);
- c) punitive, exemplary or aggravated damages in an amount to be determined by the court;
- d) pre-judgment interest pursuant to the *Courts of Justice Act, R.S.O. 1990, c. C.43*, as amended;
- e) costs of this action on a full or, alternatively, substantial indemnity basis; and
- f) such further and other relief as to this Honourable Court may seem just.

AMENDED THIS Nov. 14/13 PURSUANT TO  
 MOTION CE  
 CONFORMÉMENT À  
 L'ARTICLE 26.02 (1) (A)  
 THE ORDER OF  
 L'ORDONNANCE DU  
 JUGE / JUDGE  
 DATED / FAIT LE  
 [Signature]  
 JENNIFER HOLLEY  
 PLAINTIFF  
 THE NORTHERN TRUST COMPANY, CANADA  
 AND THE ROYAL TRUST COMPANY  
 DEFENDANTS

**DEFINITIONS**

2. Unless otherwise defined herein, capitalized terms shall have the meanings ascribed in the Glossary attached hereto as Schedule "A".

**THE PLAINTIFF AND CLASS**

3. The Plaintiff, Jennifer Holley, resides in the Village of Ompah, Ontario. She was previously a software designer with Nortel Networks Corporation ("Nortel") until she was forced to go on long-term disability ("LTD") when she was diagnosed with Crohn's Disease over 12 years ago. She subsequently developed depression for which she receives treatment. Despite attempts to return to work, her health did not permit her to do so. It is unlikely, given her current health, that the Plaintiff will ever be able to return to work on either a part-time or full-time basis.

4. The Plaintiff brings this action on her own behalf and on behalf of the following class of persons:

All Beneficiaries of the Nortel Health and Welfare Trust ("HWT").

Beneficiaries include:

- a) LTD Beneficiaries for LTD Income and LTD Life;
- b) LTD Beneficiaries participating under Optional Life for the LTD Optional Life Benefit;
- c) STB Beneficiaries in pay on or before December 31, 2010 for STBs;
- d) SIB Beneficiaries in pay on or before December 31, 2010 for SIBs; and
- e) Pensioners (including LTD Beneficiaries) for Pensioner Life.

(the "Class" or "Class Members").

## THE DEFENDANTS

5. The Defendant, The Royal Trust Company (“Royal Trust”), is a federal corporation with its registered office and headquarters in Montreal, Quebec. Royal Trust operates in Ontario and throughout Canada and its principal place of business in Ontario is in Toronto. Royal Trust provides estate, trustee and custodian services to institutions, corporations and government in Canada. Royal Trust acted as trustee of the Nortel HWT for several years including in 2005, up until November 30, 2005.

6. The Defendant, The Northern Trust Company, Canada (“Northern Trust”), is a federal corporation with its registered office and headquarters in Toronto, Ontario. Northern Trust is a provider of global custody, full trust and pension services, and information services to Canadian clients in all provinces. Northern Trust first began offering global custody services in Canada in 1984, and became the first foreign owned trust company with full trust powers in Canada in 1994.

7. Northern Trust was appointed as trustee of the Nortel HWT effective December 1, 2005 and continues to act as trustee of the trust, which is in the process of being wound-up. Northern Trust is also the trustee of Nortel’s pension plans.

## MATERIAL FACTS

### a) The Nortel HWT and Trust Agreement

8. Nortel (and its predecessors) historically provided various health and welfare benefits to its employees which were funded and administered through the Nortel Health and Welfare Trust (“Nortel HWT” or “HWT” or “Fund”).

9. The Nortel HWT was established in 1980 as a tax-efficient vehicle through which employee benefits would be provided. The HWT Financial Statements categorize the employee benefits plans as either Reserved Plans (plans for which *the Fund holds assets*) or Paid as Incurred Plans (benefits which are reimbursed *by Nortel* on an ongoing basis).

### 1. DESCRIPTION OF THE FUND

The Health and Welfare Trust Fund (the “Fund”) was established by Nortel Networks Limited (the “Administrator”) on January 1, 1980 in order to fund the employee benefits program for all eligible employees of Nortel Networks Limited and its Canadian subsidiaries (collectively, the “Company”) under the following plans:

*Reserved plans (plans for which the Fund holds assets)*

- (a) Long-term Disability Plan
- (b) Survivor Income Benefit Plan
- (c) Pensioners’ Insurance Plan
- (d) Employee – financed Group Life Plan (Group Life – Part II)

*Paid as Incurred Plans (to be reimbursed by Nortel Networks on an ongoing basis)*

- (e) Dental Plan
- (f) Extended Health Plan
- (g) Group Life Plan (Group Life – Part I)

10. The HWT is governed by an agreement between Northern Telecom Limited (a predecessor company to Nortel) and Montreal Trust Company (as trustee) dated January 1, 1980, and amended by agreements not approved by the Beneficiaries made as of September 24, 1984, June 1, 1994 and December 1, 2005 and further amended by letter agreement dated December 1, 2005 (collectively, the "Trust Agreement").

11. In order to secure the favourable tax treatment afforded to such trust arrangements, benefits paid from health and welfare trusts ("HWTs") must comply with the *Income Tax Act* and related Canada Revenue Agency ("CRA") Interpretation Bulletins and Rulings. In particular, the Interpretation Bulletin IT-85R2, dated July 31, 1986, titled Health and Welfare Trusts for Employees published by the CRA provides that the types of benefits that may be administered by an employer under an HWT arrangement are restricted to:

- a) group sickness or accident insurance plans;
- b) private health services plans;
- c) group term life insurance policies; or
- d) any combination of a) to c).

12. While the benefits, other than life insurance, provided through HWTs may be self-insured, in order to comply as a "group sickness or accident insurance plan", self-insurance of the long-term disability ("LTD") benefits must comply with Information Bulletin IT-428 titled Wage Loss Replacement Plans, dated April 30, 1979.

13. The Long-Term Disability Plan for LTD Beneficiaries constitutes a Wage Loss Replacement Plan under CRA Interpretation Bulletin IT-428. Accordingly, even if the benefits are not insured with a licensed insurer, the principles of insurance must be respected. Paragraph 7 of Interpretation Bulletin IT-428 provides:

If, however, insurance is not provided by an insurance company, the plan must be one that is based on insurance principles, i.e., funds must be accumulated, normally in the hands of trustees or in a trust account, that are calculated to be sufficient to meet anticipated claims. If the arrangement merely consists of an unfunded contingency reserve on the part of the employer, it would not be an insurance plan.

14. Nortel played a role similar to that of an insurance company for its employee, where the HWT's LTD reserve assets were similar to disabled life reserves that reflect the obligation of the insurance company for benefit continuation beyond policy termination. Once a claim is incurred and payments commence, the insurance company becomes liable for future benefit payments, usually through age 65, provided the individual continues to qualify under the terms of the benefit plan. The reserve reflects the present value of future benefit payments and claim-related expenses, adjusted for mortality and recovery assumptions, and discounted for projected interest earnings.

15. Prior to the establishment of the HWT, Nortel sought and obtained an advance income tax ruling from Revenue Canada (as it then was) by letter dated December 17, 1979. The ruling request letter, and the ruling from Revenue Canada, obtained on December 28, 1979, described the proposed funding arrangements, including the following:

- i) Health Care Plan – Nortel to make contributions to the HWT to satisfy the claims liability and may fund expected future claims, as actuarially determined;
- ii) Long Term Disability Plan – Nortel's contributions to be sufficient to satisfy all claims and may make additional/increased contributions based on an actuarial valuation or some other reasonable basis;
- iii) Survivor Income Benefit Plan – funding to be identical to that of long term disability, but employees required to make contributions.

16. The Trust Agreement imposed upon Nortel and the defendant trustees the obligation to ensure that the Nortel HWT was adequately funded. The Trust Agreement provides that employer contributions be sufficient to pay all claims against the HWT and that the adequacy of the fund is to be evaluated on a sound actuarial basis at least annually. Article IV of the Trust Agreement provides as follows:

ARTICLE IV – EMPLOYER’S CONTRIBUTIONS

1. **The Corporation and its designed affiliated or subsidiary corporations agree to make Employer’s contributions to the Trust Fund in amounts sufficient to pay any claims which may be asserted against the Trust Fund as a result of the administration of the Health and Welfare Plan, and as may otherwise be required from time to time by the Trust for the purposes of the Health and Welfare Plan, as determined by the Trustee on a sound actuarial basis.**

2. **The Trustee shall determine or cause to be determined, on a sound actuarial basis from time to time, and in any event, once every calendar year, the level of contributions to the Trust Fund necessary to fund adequately the Health and Welfare Plan.**

3. Subject to paragraphs (1) and (2) hereof, the Corporation and its designated affiliated or subsidiary corporations shall be responsible for the adequacy of the Trust Fund to meet and discharge any and all payments and liabilities under the Health and Welfare Plan. (emphasis added)

17. Sound actuarial practice requires that HWTs maintain sufficient funds to pay the present value of future benefits in respect of all incurred long-term disability claims and other incurred claims. Such incurred claims can be “asserted against the Trust Fund” and, accordingly, there was an obligation on the Trustee to ensure that the HWT was not in a position of shortfall with respect to the funding of these claims. The Trust Agreement imposes a mandatory obligation on the Trustee to undertake sufficient annual analysis to determine that there is a “sound actuarial basis” for the sufficiency of the assets in the trust funds to meet the requirements of the Health and Welfare Plan.

18. Other relevant parts of the Trust Agreement provide:

ARTICLE II – TRUST FUND

1. The trust fund is created for the purpose of providing the Health and Welfare Plan benefits for the benefit of the Employees.

2. All payments made to the trustee from time to time by the corporation and designated, affiliated or subsidiary corporations and by the employees, together with all profits, increments and earning thereupon, shall be **irrevocable** and constitute upon receipt by the trustee, the trust funds to be administered by the trustee in accordance with the terms of this trust agreement, the Health and Welfare Benefit Plan and the Eligibility Requirements.

...

ARTICLE VI – AMENDMENT AND TERMINATION

Upon receipt of the Notice of Termination the Trustee shall within one hundred twenty (120) days determine and satisfy **all expenses, claims and obligations arising under the terms of the Trust Agreement and Health and Welfare Plan up to the date of the Notice of Termination**. The Trustee shall also determine upon a sound actuarial basis, the amount of money necessary to pay and satisfy **all future benefits and claims to be made under the Plan in respect to benefits and claims up to the date of the Notice of Termination**. The Corporation and the designated affiliated or subsidiary corporations shall be responsible to pay to the Trustee sufficient funds to satisfy all such expenses, claims and obligations, and such future benefits and claims. The final accounts of the Trustee shall be examined and the correctness thereof ascertained and certified by the auditors appointed by the Trustee. Any funds remaining in the Trust Fund after the satisfaction of all expenses, claims and obligations and future benefits and claims, arising under the terms of the trust Agreement and the Health and Welfare Plan shall revert to the Corporation.

(emphasis added)

19. The Nortel HWT was structured and has been operated such that Paid as Incurred Plan employee benefits, such as medical and dental costs, or active and LTD employees' life insurance premiums, have been paid by Nortel directly on a "pay-as-you-go" basis and paid through the HWT as an administrative matter only. Other benefits, referred to as "Reserved Plans", such as disability and survivor income benefits, have had employer contributions placed into the trust for the purpose



of accumulating trust assets in order to pay for the incurred claims with legal obligations beyond the current year.

20. Only the Reserved Plans had reserve assets notionally allocated in the HWT as reflected by the HWT financial statements; however, assets were not segregated in the HWT for each Reserved Plan and no separate bank accounts were established. As a result, all of the HWT assets were commingled in one common trust account.

21. In addition to having to comply with the *Income Tax Act* and related CRA Interpretation Bulletins and Rulings, as well as the contractual terms of the Trust Agreement, the Nortel HWT is a true, irrevocable trust subject to classic trust law principles, as well as applicable trust legislation. The irrevocable nature of the HWT meant that once contributions were made into the trust, trust assets could not be withdrawn or permitted to be removed by the Trustee except to pay for benefits in respect of the Health and Welfare benefit plans for which the funds were intended. Importantly, HWT reserve assets for the Reserved Plans could not be withdrawn to pay for other benefits in the Paid as Incurred Plans that – while Nortel may have had a contractual obligation to pay – the HWT had no obligation or reserve assets to pay.

**b) The Appointment of the Defendants as Trustees and the Breaches of Trust**

22. Northern Trust became the trustee of the HWT upon the signing of an Appointment of Successor Trustee and Acceptance of Appointment of Successor Trustee dated as of December 1, 2005 (the “Appointment”). Northern Trust succeeded the Defendant, Royal Trust, who was removed as trustee by the plan sponsor, Nortel.

23. Concurrent with the Appointment, and as a condition of Northern Trust's acceptance of the appointment to act as trustee, Nortel entered into a letter agreement with Northern Trust which, *inter alia*, purported to clarify and limit the trustee's responsibilities ("Northern Trust Letter Agreement"). Nortel further agreed to indemnify Northern Trust for any liability associated with employer contributions not being made on a sound actuarial basis by Nortel into the HWT despite the obligations otherwise contained in the Trust Agreement. This letter agreement provides as follows:

Notwithstanding anything to the contrary in the health and welfare trust and for the avoidance of any doubt, we agree that you shall have no responsibility for determining, reviewing or monitoring the amounts of Nortel Networks Limited's contributions required in order to fund adequately the health and welfare plan ("Contribution Amounts") nor to advise and carry out administrative procedures in accordance with the health and welfare plan and the eligibility requirements.

Nortel Networks Limited agrees that it shall be solely responsible for determining said contribution amounts on a sound actuarial basis and administering the Health and Welfare Plan and agrees to indemnify and hold you harmless for any and all costs, losses, damages, claims, actions, suits, liabilities, expenses or other charges (including attorneys' fees) that you incurred directly or indirectly arising out of the contributions made (or not made) by Nortel to the Health and Welfare Trust or out of the administration of the Health and Welfare Plan.

This indemnification shall survive the termination of the Health and Welfare Trust. To the extent necessary, this letter shall constitute an amendment to the Health and Welfare Trust.

24. This letter agreement did not change or alter in any respect the fiduciary and trust duties of the Defendant Trustees to the Trust. In particular, its beneficiaries did not relieve the duty of the Defendant Trustees to ensure that there was a sound actuarial basis for maintaining the Trust Funds at a level necessary to meet the requirements of the claimants under the Health and Welfare Plan.

24-25. Despite the obligation to fund the HWT in accordance with sound actuarial practice, as confirmed by disclosures made by the court appointed monitor in Nortel's insolvency proceedings, at the time Nortel filed for CCAA protection, the Defendants knowingly, intentionally, recklessly and wilfully breached their fiduciary duties and trustee duties (or alternatively, were wilfully blind) in that the HWT was significantly underfunded relative to the actuarial liabilities of the various Reserved Plans, including most notably the Long-term Disability Plan. That is to say, the HWT assets were not even sufficient to pay incurred claims that could be "asserted against the Trust Fund".

25-26. The significant funding shortfall arose in at least two material ways. First, Royal Trust improperly and fraudulently withdrew approximately \$18 million from the assets of the HWT from the Long-term Disability Plan notional asset reserve between May 2005 and September 30, 2005. An additional \$14 million was also withdrawn by the Defendants from the assets of the HWT from October 2005 to April 2006. There was no actuarial basis or justification for the withdrawal of these funds and neither the Trustee nor Nortel had any belief that the HWT would have sufficient funds on an actuarial basis to fund existing Reserved Plan claims, including existing Long Term Disability claims after those funds were removed. The defendants knew, based on discussions with Nortel and their own analysis that the funds in the Trust were inadequate to meet the needs of Health and Welfare claimants and that there was a real and substantial risk that Nortel would not be able to, and would not, repay the withdrawn funds.

26-27. The \$32 million withdrawn from the HWT was used unlawfully by Nortel to pay for benefits in the Paid as Incurred Plans, including active, LTD and pensioner medical and dental

benefits, and active and LTD life insurance premiums, that Nortel was obligated to pay directly from its own operations and funds. There were no assets in the HWT whose purpose was to pay out such pay-as-you-go benefits in the Paid as Incurred Plans. As such, the removal of monies from an irrevocable trust was improper, unlawful and fraudulent as trust assets were used for purposes other than for which the funds were intended, namely, the Reserved Plans. Furthermore, the removal of \$32 million in trust assets occurred at a time when the HWT was in a position of significant deficit in respect of the actuarial liabilities of the Reserved Plans. In such circumstances, irrevocable trust funds could not be removed in order for an employer to take a contribution holiday with respect to obligations owed to beneficiaries of different benefit plans. Nortel had no right to withdraw funds from the HWT to pay for benefits in the Pay as Incurred Plan, especially with the knowledge or being reckless to the fact that the HWT was underfunded. The defendants knew, or were reckless about knowing that there was a significant risk that Nortel would be unable on an actuarial basis to meet existing Reserved Plans claims.

27,28. Second, despite the fact that the Trust Agreement required employer contributions in amounts sufficient to pay claims that could be “asserted against the Trust Fund” and to ensure that the HWT was funded on a sound actuarial basis annually, the Defendants accepted contributions in the form of “Due From Sponsoring Company” (“Due”). The Due was an accumulation of annual amounts of required employer contributions not paid in cash. Required employer contributions should have been paid in cash and, if not in cash, at least the recorded “IOU” should have had security and paid interest.

~~28-29.~~ The Due did not contribute to an HWT investment return since there was no interest charged and further failed to provide for preservation of HWT capital since no security was ever provided by Nortel.

~~29-30.~~ The Due or IOU from Nortel was booked as a long-term receivable and appeared as an asset on the HWT financial statements. The Due was effectively a varying loan from the HWT by the trust grantor in favour of Nortel.

31. Nonetheless, the Defendants granted increases to the Due in 2005 and 2006 despite their knowledge of Nortel's financial distress during this period of time and their knowledge of, or recklessness about, the fact that this created a significant risk for Class Members facilitated through the underfunding of the HWT by Nortel, especially when combined with the unlawful withdrawal of HWT funds as described, would result in the HWT being unable to meet Class Members' LTD and other Reserved Plan claims.

~~30-32.~~ In addition, the Defendants had a fiduciary and trust obligation to collect upon the outstanding "Due From Sponsoring Company" as the company's financial condition continued to deteriorate as Nortel still had sizeable cash assets from which the Defendants could have demanded Nortel repay the IOUs. In particular, Northern Trust had an obligation to collect upon the outstanding "Due From Sponsoring Company" prior to Nortel's CCAA filing at January 14, 2009. Northern Trust knowingly chose not to fulfil its fiduciary and trust obligation to do so with knowledge that this was a breach of its trust duties and increased the risk that the HWT would be unable in the future to pay Class Members' LTD claims and other Reserved Plan claims.

~~31.33.~~ The amount of the Due increased from \$20.290 million in 2004 to a high of \$42.518 million in 2006, before decreasing to \$28.343 million prior to its partial write-off in the period ending December 31, 2009. The Due was written off by Nortel in 2009 by \$26.985 million.

**c) Northern Trust's Silence During Nortel's CCAA Filing, the Settlement Agreement Approval Hearing and HWT Wind-Up Distribution**

~~32.34.~~ Nortel applied for and was granted protection from creditors under the CCAA pursuant to an Initial Order dated January 14, 2009. At the time it filed for protection under the CCAA, Nortel had cash assets of approximately \$2 billion. The amount outstanding in respect of the "Due From Sponsoring Company" at the time was \$37.064 million. Although it had the assets to do so, Nortel did not repay this outstanding loan to the HWT and Northern Trust knowingly failed and knowingly and fraudulently chose not to collect on this loan in the years and months prior to the CCAA filing as Nortel's financial condition continued to deteriorate to the point of insolvency. Northern Trust was aware that there was a significant and increasing risk that Nortel would be unable or unwilling to reimburse the Trust for the \$32 million of assets wrongfully removed from the Trust but deliberately and fraudulently refrained from pursuing its duties as Trustee to collect these amounts.

~~33.35.~~ Despite the improper removal of \$32 million in trust assets, the \$37.064 million outstanding loan (as at December 31, 2008), as well as the fact that the HWT was in a significant deficit position, initial court filings prepared by the Monitor suggested that there were no issues with respect to the level of funding in the HWT and, in fact, that the HWT was in "surplus". For example, the Monitor's Pre-Filing Report stated that the funding payments into the HWT would be suspended post-filing as "it [was] forecast that the H & WT has sufficient surplus assets to sustain

itself during the forecast period”. Further, the Thirty Third Report of the Monitor states: “funding continues in the ordinary course for the H & W Trust”. The Thirty Fifth Report of the Monitor further states: “funding continues in the ordinary course for the H&WT”. The Trustee, in furtherance of its fraudulent conduct, took no steps to ensure that these amounts were claimed against Nortel and/or brought to the attention of the Monitor and claimed against the estate.

34-36. Thus, the factual foundation on which the Initial Order was obtained appears to have been incorrect, or at a minimum, unclear or misleading. Yet, Northern Trust knowingly, or pursuant to its course of fraudulent conduct, chose not to correct or clarify this information which it knew to be incorrect, unclear, or misleading.

35-37. The Initial Order provided that Nortel was “entitled but not required” to make payments in respect of, among other things, employee benefits, after the CCAA filing.

36-38. After the Initial Order, Nortel continued to make employer contributions to pay for pensioner and LTD medical and dental benefits, and LTD life insurance benefits on a pay-as-you-go basis. LTD income benefits and survivor income benefits, as well as Pensioner Life insurance benefits, were paid from the Nortel HWT assets without fresh employer contributions being made into the HWT. However, Nortel advised stakeholders that, absent a settlement or special arrangements being made, it would cease making the continued payment of benefits on March 31, 2010.

37-39. On February 8, 2010, leveraging the threatened cutting off of benefits, Nortel was able to achieve an agreement with the Former Employees’ Representatives, the LTD Representative, the

Settlement Representative Counsel and the CAW principally involving matters related to Nortel's pension plans, the HWT and employment related issues. In exchange for the limited extension of certain benefits to December 31, 2010, the settlement agreement provided broad releases in relation to HWT funding matters and precluded claims of priority with respect to HWT related claims ("HWT Claims"). The settlement agreement included the following key terms:

- a) ***Treatment of HWT Claims.*** HWT Claims related to the funding deficit in the HWT or any HWT related claims in these proceedings or in any other proceedings shall not advance, assert or make any claim that any HWT Claims are entitled to any priority or preferential treatment over unsecured claims, or are the subject of a constructive trust or trust of any nature or kind in respect of the property and assets of Nortel or any Nortel entity, and such claims, to the extent allowed against Nortel pursuant to any claims adjudication procedure established in these proceedings, shall rank as ordinary unsecured claims on a *pari passu* basis with the claims of the ordinary unsecured creditors of Nortel;
- b) ***Release of HWT Claims.*** Broad releases provided in favour of the Releasees (including the trustees of the HWT) in respect of any claims related to the HWT, including without limitation, the administration of the HWT, the funding of the HWT, any obligation to contribute to the HWT and the investment of the HWT assets. Limited exceptions are provided with respect to claims against directors of Nortel referred to in subsection 5.1(2) of the CCAA or with respect to fraud on the part of any Releasee, with respect to that Releasee only (the "Release");
- c) ***Release related to priority of HWT Claims.*** Additional releases provided in respect of claims that the HWT Claims rank as a preferential or priority claims over the claims of ordinary unsecured creditors of Nortel.

40. Although the settlement agreement sought to significantly compromise HWT Claims, including potential claims held by the Beneficiaries against the Defendants, very limited information was disclosed in the CCAA proceedings, including information within the knowledge of the Defendants, at that time with respect to the operation and funding of the HWT, as well as the significant funding shortfall of the Reserved Plans. In fact, the only financial



information involving the HWT consisted of *unaudited* financial statements of the HWT for one year (for the period ending December 31, 2008) which comprised seven pages.

38-41. Neither Nortel nor the defendants advised the Class Members of the fact of the fraudulent withdrawal of \$32 million from the Trust in 2005-2006 as pleaded, or of the course of their fraudulent conduct which permitted and acquiesced in the deliberate underfunding of the Trust by virtue of the scheme described in paragraphs 30 to 33.

39-42. The 2008 HWT financial statements indicated that the HWT had net assets of approximately \$123 million, of which \$37 million consisted of the “Due from Sponsoring Company”. Given Nortel’s insolvency, the assets actually available to pay claims in respect of the Reserved Plans for which the HWT held assets were approximately \$86 million (as of December 31, 2008). However, the estimated actuarial liability for these Reserved Plans was \$258.2 million (as of December 31, 2008).

40-43. Despite objections being advanced on behalf of some 40 dissenting LTD Beneficiaries with respect to the level of (non-)disclosure of financial information provided, as well as questions raised as to the possibility that funds may have been improperly removed from trust, Northern Trust, standing in a position of clear conflict of interest given its efforts to secure a release of potential claims against it, knowingly failed and chose not to provide any level of information to the trust beneficiaries. As subsequent court disclosures were to confirm, the concerns raised by the dissenting LTD Beneficiaries with respect to possible misappropriation of trust assets were, in fact, legitimate.

41.44. On March 31, 2010, an amended Settlement Agreement was approved by the Court.<sup>1</sup> The Release (as contained in the order approving the Settlement Agreement dated March 31, 2010) specifically provides as follows:

**THIS COURT ORDERS AND DECLARES** that the Releasees, the trustee and custodian of the Pension Plans, CAW, the Representatives... are hereby released, discharged and remised from any and all direct and indirect claims (contingent, liquidated or unliquidated, proven or unproven, known or unknown, in the nature of damages or otherwise, whether or not asserted whether arising by contract, agreement (whether written or oral), under statute, civil law, common law, or in equity, or otherwise in any jurisdiction) related to... (ii) the HWT, including without limitation, the administration of the HWT, the funding of the HWT, any obligation to contribute to the HWT and the investment of the HWT assets, provided that nothing herein shall release a director of Nortel from any matter referred to in subsection 5.1(2) of the CCAA or with respect to fraud the part of any Releasee, with respect to that Releasee only.

42.45. The Settlement Agreement further provides that the settlement parties would work towards a court approved distribution of the HWT corpus in 2010.

46. On August 27, 2010, the Monitor delivered its 51<sup>st</sup> report which disclosed for the first time a lengthy list of documents. These documents were not in the knowledge of the plaintiff class and could not have been known prior to this date. This list of documents led to the discovery of various facts, including:

(a) the HWT has a -66% deficit between the estimated HWT assets and actuarial liabilities for the Reserved Plans at December 31, 2010. The Reserved Plans with HWT legal obligations are identified by the Court Monitor on August 27, 2010 and then endorsed by J. Morawetz on November 9, 2010. These Reserved Plans with HWT legal obligations are the LTD Income Benefit and LTD Life Insurance Benefit, the Survivors Income Benefit and Survivors Transition Benefit and the Pensioners' Life Insurance Benefit

(b) the HWT deficit is inflated by the following

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<sup>1</sup> The amendment did not relate to any of the terms of the initial settlement agreement related to HWT Claims.

- 1) the estimated \$32 M of HWT assets used to pay claims in the Paid as Incurred Plans during May 2005 to April 2006, when Nortel took an employer contribution holiday for these plans in order to materially improve its own cash flow. The HWT assets had the purpose to fund the Reserved Plans, were irrevocable, and were not to be used for the benefit of Nortel.
- 2) the estimated final \$28 M Due from Sponsoring Company allowed to be created and then not collected from Nortel before the CCAA filing.
- 3) the loss of investment income relating to the above amounts.

47. The report did not disclose the fraudulent basis of the scheme carried on by Nortel and the defendants which subsequently involved the fraudulent withdrawal of \$32 million from the Trust and the underfunding of the Trust as described herein.

43-48. On August 30, 2010, the Monitor delivered materials in support of a motion for an order approving a methodology for the allocation of the corpus of the HWT. The allocation scenario recommended by the Monitor contemplates a *pro rata* distribution between beneficiaries whose claims are “in pay”, namely, those with income claims presently being paid, including LTD income benefits, and those whose claims are said to be “certain to be payable at some future date” which, according to the Monitor, included claims for Pensioner Life insurance benefits.

44-49. By order dated November 9, 2010, the Court approved a distribution of the HWT assets on the basis of the allocation scenario proposed by the Monitor. The proposed class definition corresponds with the participating beneficiaries that would receive funds under the court-approved allocation scenario. Several interim distributions of HWT assets were thereafter made to the participating beneficiaries. As of the termination date of the HWT<sup>2</sup>, the total assets

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<sup>2</sup> The termination date of the HWT was deemed by the November 9, 2010 HWT allocation order to be December 31, 2010.

available for distribution were approximately \$80 million. However, the most recent estimated actuarial liability for these Reserved Plans was approximately \$223 million (as of December 31, 2010).

## CAUSES OF ACTION

### A. The Defendants as Fiduciaries

50. As noted above, the Trust Agreement requires that the trustee determine, on a sound actuarial basis no less than once every calendar year, the level of contributions to the HWT necessary to adequately fund the Health and Welfare Plan. In addition to the obligations set out under the Trust Agreement, the Defendants are subject to statutory and common law fiduciary duties and obligations to the beneficiaries of the HWT assets, namely the beneficiaries of the Reserved Plans. To the extent the Trust Agreement (and in the case of Northern Trust, the Northern Trust Letter Agreement) purports to limit the trustee's mandate, such contractual terms in no way affect the Defendants' statutory and common law fiduciary duties and obligations to the trust beneficiaries.

51. Notwithstanding any contractual terms purportedly limiting the trustee's obligations and in addition to their contractual duties provided in the Trust Agreement, the Defendants had overarching fiduciary obligations to act in the best interests of the Beneficiaries. The scope of a trustee's duties extend to ensuring that employer contributions are appropriately made based on a sound actuarial analysis and not discontinued and to take appropriate measures when contributions are inappropriately terminated, when trust assets are proposed to be used to pay for benefits that are not the purpose of the reserve assets in the trust, or when significant, unsecured IOUs are given in

lieu of cash contributions. As trustees, the Defendants had obligations of prudence to protect not just the body of the trust, but also the interest of the Beneficiaries during the ongoing operation of the Fund and of the Health and Welfare Plan. They had a duty to ensure that the trust assets were not withdrawn and/or maintained through required contributions in circumstances where they were taking risks with the trust assets to the prejudice of Class Members, which risks were known to them to be contrary to their duties as Trustees and which they had no right to take.

**B. Fraudulent Breach of Trust**

52. As discussed herein, the Defendants not only knowingly and fraudulently failed to protect the interests of Beneficiaries but they violated one of the hallmarks of trust law by knowingly failing to protect the corpus of the trust from revocation and exposed the Beneficiaries to unconscionable risk. As noted below, the breaches of trust committed by the Defendants were so egregious in the circumstances so as to constitute fraud.

53. In addition, the Defendants knowingly consulted with and worked with Nortel to facilitate and actively participate in the fraudulent breach of trust through the unlawful use of the trust funds by Nortel to fund its ongoing benefits payment and other obligations. The Defendants did this to protect their financial and business arrangements, including their current and future trust and benefits business relationship with Nortel, a major Canadian business client.

54. As described herein, the defendants have engaged in unlawful and fraudulent conduct in their capacity as Trustee which has facilitated a fraudulent breach of trust. They have done so in concert with Nortel and with knowledge of, or with wilful blindness and recklessness as to, Nortel's

intervention and use of trust assets or funds, that it was obligated to contribute to the Trust in order to fund the Health and Welfare Plan, to unlawfully fund Nortel's other business obligations.

55. The defendants facilitated and acquiesced in this fraudulent breach of trust by fraudulently paying \$32 million of Trust fund assets to Nortel in 2005-2006, contrary to their fiduciary duties as Trustee, by permitting and acquiescing in Nortel's failure to make proper and required contributions to the Trust, by accepting unsecured promises to pay from Nortel in lieu of contributions based on sound actuarial analysis and by unlawfully failing to claim payment of trust funds from Nortel, either prior to or during the CCAA process.

45-56. The defendants' fraudulent conduct as pleaded herein put the trust funds at risk of loss to the prejudice of Class Members' rights, the risk of which the Defendant Trustees knew was contrary to their fiduciary duties as Trustee, was unconscionable and which they had no right to take.

**B. — Liability of the Defendants**

**C. Actual or Constructive Fraud**

57. Despite the strict responsibilities and requirements delineated by the Trust Agreement, as well as the fiduciary duties owed by the Defendants to the Beneficiaries under common law and relevant trust legislation, the Defendants engaged in fraud (actual or constructive) and their actions constituted fraudulent breaches of trust or fraudulent misrepresentation in a number of respects.

58. The plaintiff repeats the facts pleaded herein and pleads that those facts, including the facts pleaded below constitute actual and/or constructive fraud.

46.59. First, the Defendants knowingly and fraudulently assisted Nortel in improperly removing approximately \$32 million from the HWT trust assets to pay for Nortel's benefits under Paid as Incurred Plans, which Nortel was obligated to pay annually directly from its own operational funds. This intentional removal of monies from an irrevocable trust was improper as trust assets were knowingly and fraudulently used for purposes other than for which the funds were intended, namely, the Reserved Plans. They knew, or were reckless and wilfully blind to the prospect that Nortel was in financial distress and would be unable to repay the trust funds and that there was a significant risk of prejudice to Class Members if the HWT was and remained underfunded, especially with the increasing prospect of Nortel's insolvency.

47.60. Second, the Defendants knowingly accepted "Due From Sponsoring Company" from Nortel instead of cash employer contributions and intentionally failed to collect on or secure this loan as Nortel's financial condition deteriorated. At a minimum, the Defendants should not have accepted increased IOUs in 2005 and 2006 when they knew of Nortel's financial distress. In addition, Northern Trust egregiously breached its fiduciary obligation, constituting fraudulent behaviour, by knowingly failing to collect upon or secure the outstanding and impaired "Due From Sponsoring Company" from as early as 2005 (when it knew Nortel's financial condition was deteriorating) to no later than Nortel's CCAA filing at January 14, 2009. The Defendants knew, or were reckless and wilfully blind that the Class Members would be at risk if the Trust was not funded on a sound actuarial basis and they permitted, acquiesced to, and fraudulently facilitated the underfunding by Nortel.

~~48-61.~~ As of May 2005, when the \$32 million began to be withdrawn, the Reserved Plans were in deficit. Similarly, as of 2005, when the Due increased from \$20.29 million to \$31.121 million, the assets of the HWT were far below the actuarial liability of the Reserved Plans. As a result, the Defendants (including Royal Trust up to December 5, 2005) took a risk they were not entitled to take, and which was contrary to the best interests of the trust Beneficiaries, with respect to their knowingly permitting and facilitating the removal of trust funds during 2005-2006, and in knowingly accepting an increase in the Due and not requiring Nortel to repay the Due prior to Nortel's CCAA filing at January 14, 2009.

~~49-62.~~ Third, beyond knowingly participating in these fraudulent breaches of trust, the Defendants knowingly and fraudulently failed to advise the trust Beneficiaries and the Monitor of the misappropriation of trust assets and of the existence of the Due which was to become impaired, as well the fact that the fund was insufficient to pay for benefits in respect of the Reserve Plans on claims that had already been incurred. In this way, the Beneficiaries and, in particular, the LTD Beneficiaries suffered extreme prejudice when Nortel became insolvent.

63. Finally, the Defendants further committed fraud through their fraudulent concealment of the above described fraudulent breaches of trust, of which they had full knowledge, from the Beneficiaries and the Monitor. In particular, Northern Trust, in a position of conflict of interest, knowingly failed to advise the Beneficiaries of these breaches and further failed to provide any meaningful financial disclosure relating to the HWT during Nortel's CCAA proceedings until after it had secured the benefit of a third party release contained in a Settlement Agreement addressing employee-related claims.



64. The third party release released all HWT Claims except claims with respect to fraud. Northern Trust's concealment or silence during the period leading up to the Settlement Agreement was particularly unconscionable given the very troubling questions raised by some of the Beneficiaries regarding the significant funding shortfall in the HWT in respect of the Reserved Plans and their concerns that money may have been misappropriated from the trust. Disclosures made in Nortel's CCAA proceedings subsequent to the Settlement Agreement validated these concerns: there was in fact a significant funding shortfall in the HWT in respect of the Reserved Plans and funds were misappropriated from the trust.

50-65. The Defendants in their position as Trustees, took risks that would prejudice the rights of the Beneficiaries, without having any right to take those risks by allowing trust funds to be removed from the HWT and not informing the Beneficiaries of such withdrawal and the resulting shortfall in the HWT. The Defendants knew or ought to have known that their conduct would prejudice the Beneficiaries since the HWT would no longer be able to meet its obligations to the Beneficiaries.

## **DAMAGES**

51-66. As noted above, the net assets of the HWT distributed or to be distributed to Beneficiaries is approximately \$80 million whereas the actuarial liability in respect of the participating benefits is \$223 million. As a result of the fraudulent conduct described herein, the Beneficiaries have suffered damages of \$60 million plus accrued interest.

52-67. Given the nature of the interests that the Defendants have disregarded, and their high-handed and oppressive conduct towards the Beneficiaries, an award of aggravated or punitive damages is warranted.

53-68. The Plaintiff pleads and relies on the *Income Tax Act*, RSC, 1985, c. 1., the *Trustee Act*, RSO 1990, c. T.23, the *Variation of Trusts Act*, RSO 1990, c. V.1 (including predecessor legislation and as may be amended), as well as similar applicable trust legislation in other provinces, including the *Civil Code of Québec*, S.Q., 1991, c. 64 and *An Act Respecting Trust Companies and Savings Companies*, RSQ, c. S-29.01.

54-69. The Plaintiff proposes that the trial of this action be in the City of Toronto.

55-70. The Plaintiff will serve a jury notice.

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Court File No: CV-12-462273CP

**ONTARIO**  
**SUPERIOR COURT OF JUSTICE**

Proceeding commenced at TORONTO

**AMENDED STATEMENT OF CLAIM**

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