

Court File No. 47959 CP

**ONTARIO  
SUPERIOR COURT OF JUSTICE**

BETWEEN:

JOHN DOUGLAS McKITTRICK

Plaintiff

- and -

THE GREAT-WEST LIFE ASSURANCE COMPANY and  
GREAT-WEST LIFECO INC

Defendants

**FURTHER AMENDED AMENDED STATEMENT OF DEFENCE**

*Proceeding commenced under the Class Proceedings Act, 1992*

1. The defendants admit that the plaintiff is a participating policyholder ("par policyholder") of The Great-West Life Assurance Company ("GWL") and currently holds the policies listed in paragraph 2 of the fresh as amended statement of claim (the "statement of claim").
2. The defendants further admit the allegations in paragraph 3 of the statement of claim that the defendant GWL is an insurance company that carries on business, among other things, as a life and health insurer in Canada with its head office in Winnipeg, Manitoba, and is a wholly-owned subsidiary of the defendant Great-West Lifeco Inc. ("Lifeco").
3. The defendants deny all of the remaining allegations in the statement of claim except as expressly admitted in this statement of defence.
4. The defendants further deny that the plaintiffs are entitled to any of the relief claimed in paragraph 1 of the statement of claim.

## Overview

5. At issue in this proceeding is a transaction involving the participating account (“par account”) of GWL (referred to below as the “Par Account Transaction”) that arose in the course of the 1997 acquisition by Lifeco and GWL of London Insurance Group Inc. (“LIG”)(and, indirectly, London Life Insurance Company) (the “Acquisition”).

6. The Par Account Transaction was beneficial to the par account, and fair to par policyholders. Prior to proceeding with the Par Account Transaction, fairness opinions were given by:

- (a) the Appointed Actuary for GWL;
- (b) an external actuary; and
- (c) an Independent Actuary.

7. The Par Account Transaction was also reviewed by the Office of the Superintendent of Financial Institutions (“OSFI”), in the course of its approval of the Acquisition.

8. Contrary to the allegations in the statement of claim, the Par Account Transaction did not contravene the *Insurance Companies Act (“ICA”)*, nor was there a breach of any other alleged obligation, by the GWL Board of Directors or otherwise.

## Acquisition of LIG

9. In the summer of 1997, Lifeco announced a bid to acquire LIG (including London Life). Ultimately, Lifeco (and GWL) acquired LIG for approximately \$2.9 billion in cash and securities.

## Par Account Transaction

10. The concept of the Par Account Transaction was based upon the savings that would result from the integration of the businesses of London Life and GWL. Anticipated reductions in the cost of administrative functions would represent extraordinary long term benefits to the par account.

11. As ultimately implemented, the Par Account Transaction had the following elements:
  - (a) in the par account, cash was exchanged for a prepaid expense asset of the same amount;
  - (b) in the shareholder account, the cash was received and offset by a deferred revenue liability of the same amount; and
  - (c) the cash in the shareholder account was used in the financing of the Acquisition.
12. The amount, ultimately \$40 million, was based upon the estimated savings in the first 25 years after the closing of the Acquisition, with an experience rating mechanism to adjust for any material deviations between estimated savings and actual savings.
13. The Par Account Transaction was beneficial to the par account. It incorporated interest at an appropriate rate of return – 6.91 percent – which was determined based on the Government of Canada long term bond rate in late July 1997 of 6.66 percent, plus a margin of 0.25 percent. The Par Account Transaction therefore provided for a beneficial rate of return for the par account. The defendants deny any other entitlement to interest, contrary to the allegations in paragraphs 1 and 30 of the statement of claim.
14. There were other anticipated benefits to the par account since the business combination gave the companies a leading position in markets in which they competed, enhancing the market presence of the par account. In addition, long-term savings accrued to the benefit of the par account.
15. The Par Account Transaction did not affect the total assets or surplus of the par account. Nor did it adversely affect the dividend expectations of par policyholders.
16. Contrary to the allegations in paragraph 6 of the statement of claim, the Par Account Transaction did not contravene either section 458 or 462 of the *ICA*.

**External review of proposed transaction**

17. Before proceeding with the Par Account Transaction, OSFI was consulted, and external and independent actuarial opinions were obtained, as set out below.

***External Actuarial Opinion***

18. In July of 1997, before moving forward with the concept of a Par Account Transaction in connection with the proposed Acquisition, GWL sought an external actuarial opinion from Tillinghast-Towers Perrin regarding the general concept.

19. On July 30, 1997, Tillinghast-Towers Perrin provided its opinion, concluding, among other things, that:

- (a) the overall principle of assessing the financing costs of the Acquisition to the par account in an amount equal to the value of the gains expected to be received was reasonable and equitable to par policyholders;
- (b) the proposed method was reasonable, and would result in a fair and equitable allocation, and hence the par policyholders would not be adversely affected by the transaction; and,
- (c) the particular method and assumptions proposed would generate a fair and reasonable value of the future expected gains to the par account.

***OSFI / Independent Actuary's Opinion***

20. GWL and Lifeco needed OSFI's approval for numerous aspects of the Acquisition before it could close. OSFI is the primary regulator of federal financial institutions, including federally regulated insurance companies such as the defendant GWL.

21. Although the proposed Par Account Transaction did not itself require a specific statutory approval by OSFI, GWL and Lifeco drew it to OSFI's attention in connection with OSFI's review of the Acquisition.

22. At OSFI's request, GWL sought an opinion from an Independent Actuary regarding the proposed Par Account Transaction. The defendants deny the allegation in paragraph 25 of

the statement of claim that no independent actuarial advice regarding the Par Account Transaction was obtained. The defendants further deny the allegations in paragraph 28 of the statement of claim that OSFI failed to protect the interests of the par policyholders.

23. In August of 1997, with the approval of OSFI, the actuarial firm William M. Mercer Limited was engaged to act as Independent Actuary and provide the requested opinion. The Independent Actuary's mandate required, among other things, the following:

- (a) that it opine on the fairness of the proposed Par Account Transaction as it affected the par policyholders of GWL, including,
  - (i) the rationale for a portion of the financing being provided by the par account;
  - (ii) the rationale used to determine the amount of such financing;and,
- (b) that it opine on the continuing outlook for the reasonable expectations of the par policyholders.

24. The Independent Actuary conducted its review of the proposed Par Account Transaction, and concluded, among other things, that:

- (a) it was fair for the par account of GWL to contribute towards the purchase price in the Acquisition;
- (b) the proposed amount of financing to be provided by the par account was reasonable;
- (c) the par policyholders would see their long-term policy expectations maintained or enhanced by the Acquisition; and
- (d) the par policyholders would see the continuing outlook for their financial security maintained or enhanced by the Acquisition.

25. In September of 1997, Lifeco and GWL issued their Offer to Purchase LIG. Contrary to the allegations in paragraphs 15 and 25 of the statement of claim, the Offer did disclose the potential involvement of the par account in the Acquisition.

26. The Acquisition closed on November 13, 1997, following receipt of the requisite OSFI approvals.

#### **Internal Approval of the Par Account Transaction**

27. In November of 1997, the GWL Appointed Actuary gave an opinion to the GWL Board of Directors that the proposed Par Account Transaction was fair and equitable to par policyholders of GWL.

28. On November 26, 1997, the Par Account Transaction was approved by the Board of Directors of GWL, which noted, among other things, the following:

- (a) that as a result of expected annual savings GWL's par account would realize an extraordinary long-term benefit;
- (b) that the external actuary opined that the actions proposed to be taken were fair and reasonable;
- (c) that the Independent Actuary opined that actions proposed to be taken were fair and reasonable; and
- (d) that it was appropriate that the par account contribute and that a prepaid expense asset be established in the par account in the same amount.

29. The GWL Board of Directors resolved among other things:

- (a) that GWL's par account contribute an amount as determined by the Company's Appointed Actuary, of up to \$44 million after the anticipated after tax cost of any restructuring charges to be allocated to the par account, to assist in the Acquisition;

- (b) that a prepaid asset in the same amount be established in GWL's par account, to be depreciated in accordance with the principles referred to in the external actuary's opinion and the Independent Actuary's Opinion; and,
- (c) that an experience rating mechanism be implemented to adjust for material deviations between the estimated amount and the actual savings and the actual restructuring charges allocated to the par account, in connection with the Acquisition.

30. The defendants deny the allegations in paragraphs 7 and 23 of the statement of claim alleging a breach by GWL of s. 518 of *ICA*. The defendants further deny the allegations in paragraph 7 of the statement of claim that the GWL Directors contravened their duties under the *ICA*, specifically the requirement in section 212 of the *ICA* to abstain from voting. The obligation relied on by the plaintiffs is expressly inapplicable to contracts with affiliates under section 212(1)(d) of the *ICA*, and the Par Account Transaction was not, in any event, a material contract or proposed material contract within the meaning of section 211 of the *ICA*.

31. The Directors of GWL were therefore not subject to, or in breach of, the alleged obligations under section 211 and 212 of the *ICA*, contrary to the allegations in paragraph 24 of the statement of claim.

32. Contrary to the allegations in paragraph 20 of the statement of claim, all of the members of the Board of Directors of GWL were not affiliated with Lifeco under s. 170 of the *ICA*.

33. The defendants further deny that the Par Account Transaction unfairly disregarded the interests of the GWL par policyholders, or violated the alleged corporate law principles. Nor does the *ICA* provide for a statutory claim of oppression, and no such cause of action exists at common law, contrary to the allegations in paragraph 25 of the statement of claim. The defendants further deny the alleged non-compliance with Generally Accepted Accounting Principles, and the allegations in paragraph 31 of the statement of claim including the allegation that there was a breach of section 492 of the *ICA*.

### **Implementation of the Par Account Transaction**

34. After the Par Account Transaction was approved, it was implemented, in the amount of \$40 million, not \$47 million as alleged in paragraphs 6, 16 and 19 of the statement of claim.

35. The \$40 million amount was the estimated present value of the savings for the first 25 years after the Acquisition, on an after tax basis, net of the par account's integration costs. The amount was arrived at by estimating those savings using a present value calculation that had regard for an appropriate rate of inflation and an appropriate rate of investment return. Margins for conservatism (acting to reduce the amount) were included in the amount of the expenses, the inflation rate, and in the interest rate.

36. Contrary to the allegations in paragraphs 6, 16 19 and 22, the Par Account Transaction did not include any "conversion" of funds, or "transfer" within the meaning of section 462 of the *ICA*.

37. The prepaid expense asset depreciates over the period of 25 years, with the depreciation in each year being an expense of the par account allocated and debited under section 458 of the *ICA*. Contrary to the allegations in paragraphs 13, 18 and 22 of the statement of claim, the annual expense was within GWL's expense allocation method, and met the requirements of section 458 of the *ICA*.

### **Amended claims are statute-barred**

38. The claims added by the amendments granted by order dated April 8, 2008 are statute-barred. The defendants plead and rely on the *Limitations Act*, R.S.O. 1990, c. L.15, and the *Limitations Act*, 2002, S.O. 2002, c. 24, Sched. B.

### **No breach of the *Insurance Companies Act***

39. The Par Account Transaction was done in accordance with, not in breach of, the *ICA*:

(a) it was not a prohibited transfer under s. 462 of the *ICA*;

- (b) the annual amortization of the prepaid expense asset was a proper debit from the par account, expressly permitted by section 458 of the *ICA*;
- (c) as set out above, a number of the other *ICA* provisions relied on by the plaintiffs are inapplicable, on their own express terms, and cannot be said to have been breached; and
- (d) to the extent that the remaining *ICA* sections alleged by the plaintiff do apply, there was no breach.

40. The defendants deny all the allegations of improper conduct in the statement of claim and put the plaintiffs to the strict proof thereof.

41. The defendants plead and rely on the *ICA*, and the *Office of the Superintendent of Financial Institutions Act*.

### **Remedies**

42. The defendants deny that the plaintiff is entitled to any of the relief sought in paragraphs 1, and 29 to 33 of the statement of claim.

43. There has been no breach calling for an order for compliance under section 1031 of the *ICA*. Nor does the plaintiffs' claim give rise to a right to a restraining order or an order for rescission, contrary to the allegations in paragraph 1 of the statement of claim.

44. As set out above, the Par Account Transaction incorporated a beneficial interest rate in favour of the par account. There is no basis for a claim for further interest, or for unjust enrichment, contrary to paragraphs 1 and 30 of the statement of claim.

45. Nor is the plaintiff entitled to any of the declaratory relief sought in paragraph 1 of the statement of claim.

46. Lastly, the defendants deny the claim for damages or other payments to par policyholders, claimed in paragraphs 1 and 33 of the statement of claim. On the contrary,

even if there had been a breach, which is denied, there would be no entitlement to any such relief.

### **Not a Proper Class Action**

47. The defendants deny that the plaintiff is entitled to the relief sought in paragraphs 1 and 34 to 36 of the statement of claim in relation to the requested certification of this action as a class action under the *Class Proceedings Act*, 1992, S.O. 1992, c. 6.

### **Dismissal with costs**

48. The plaintiff is not entitled to the relief they have claimed. The defendants therefore request that this action be dismissed, with costs.

September 12, 2008

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Proceeding commenced at London

**FURTHER AMENDED AMENDED  
STATEMENT OF DEFENCE**

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