

CANADA / JUDGMENT

Pestano v. Wong

2019 BCCA 141

COURT

British Columbia Court of Appeal

DECIDED

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2019 BCCA 141 Pestano v. Wong

COURT OF APPEAL FOR BRITISH COLUMBIA

Citation:

Pestano v. Wong,

2019 BCCA 141

Date: 20190425

Dockets: CA44831, CA44839

Docket: CA44831

Between:

Matthew Pestano, by his litigation guardian,

Kevin Pestano

Respondent

(Plaintiff)

And

Mildred Wong

Appellant

(Defendant)

And

Vancouver Coastal Health Authority

John Doe #1, John Doe #2

Respondents

(Defendants)

Docket: CA44839

Between:

Matthew Pestano, by his litigation guardian,

Kevin Pestano

Respondent

(Plaintiff)

And

Mildred Wong

Respondent

(Defendant)

And

Vancouver Coastal Health Authority

Appellant

(Defendant)

Before:

The Honourable Madam Justice Saunders

The Honourable Madam Justice Fenlon

The Honourable Madam Justice Dickson

On appeal from: An order of the Supreme Court of British Columbia, dated September 20, 2017 (Pestano v. Wong, 2017 BCSC 1666, Vancouver Docket S111428).

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Place and Date of Hearing:

Vancouver, British Columbia

March 22, 2018

Place and Date of Judgment:

Vancouver, British Columbia

April 25, 2019

Written Reasons by:

The Honourable Madam Justice Dickson

Concurred in by:

The Honourable Madam Justice Fenlon

Concurring Reasons by:

The Honourable Madam Justice Saunders (Page 31, Para. 77)

Summary:

Three days after his birth, the respondent M suffered a brain injury secondary to a hypoglycemic episode that resulted in his need for lifelong care. M, by his litigation guardian, commenced a medical malpractice action. The parties resolved most of the claims by way of settlement, but required judicial determination on issues related to fund and investment management fees and gross-up calculations. The judge concluded that Level 4 investment management assistance would be reasonable throughout the entire period of M's life expectancy and accepted the method of M's expert used to calculate gross-up awards. On appeal, the appellants submit the judge erred in awarding Level 4 investment management assistance for the duration of M's life expectancy and in accepting the expert's method of calculation. Held: Appeal allowed in part: the judge's finding that Level 4 investment management assistance for the duration of M's life expectancy was required to achieve a rate of return equal to the statutory discount rate was based on a misunderstanding of the expert evidence, findings unsupported by evidence and erroneous conclusions. The judge made no error in accepting the expert's method of calculation, which was well supported on the evidence. Concurring reasons (per Justice Saunders): the guiding principles for the investment of trust property are compliance with the trust instrument and reasonable prudence as viewed in the context of the particular trust. In this case, there is no statutory direction compelling diversification. The fact of trusteeship for investing money is not

material to the outcome of the issue on appeal.

Reasons for Judgment of the Honourable Madam Justice Dickson:

Introduction

- [1] This appeal concerns the legal principles and methods of calculation to be applied in assessing trustee and investment management fees and tax gross-up awards. The central issue involves the extent of a defendant's obligation, if any, to pay for additional investment management services when a trustee is charged with managing an incapable plaintiff's award for future pecuniary loss.

Background

- [2] The respondent, Matthew Pestano, was born on March 15, 2009. Three days later he suffered a brain injury secondary to a hypoglycemic episode, leading to cerebral palsy, epilepsy, autism spectrum disorder and global developmental delay. As a result of his injuries, Matthew will need lifelong care and he will never be competitively employable. His life expectancy is to age 61.8 years.
- [3] Kevin Pestano is Matthew's father and litigation guardian. He commenced a medical malpractice action against the appellants on Matthew's behalf. The parties were able to resolve most of the claims by way of a \$5,850,000 settlement that later received court approval. However, they required judicial determination on a range of unresolved issues, including issues related to fund and investment management fees and gross-up calculations.
- [4] The settlement sum included allocations of \$4,000,000 for the cost of future care and \$1,200,000 for future income loss based on the present value of Matthew's lifetime care needs and lost earnings. Due to his injuries, Matthew will never be able to manage his estate or person or manage or invest his settlement fund personally. Although the parties agreed that Matthew is entitled to an award for lifelong assistance from a trustee to manage the fund, they disagreed on the extent, if any, of his entitlement to additional investment management assistance. They also disagreed on the appropriate method for calculating the income tax gross-up and management fees.

The Discount Rate, Fund and Investment Management Services and Calculation Methodology

The Discount Rate

- [5] In most serious personal injury cases, damages for future pecuniary loss are awarded or agreed in the form of a one-time lump sum payment. The lump sum is determined by discounting projected future costs and lost income to their present day value, adjusting for inflation and assuming the amount paid will be invested in low-risk long-term investments and earn interest before being used in the contemplated timeframe. In *Lewis v. Todd*, [1980] 2 S.C.R. 694, a fatal accident case, Justice Dickson explained the theory of the discount factor (at 710):

the dependants receive immediately a capital sum roughly approximating the present value of the income they would have received had the deceased survived. They are able to invest this capital sum and earn interest thereon. A proportion of the interest received may be offset by the effect of inflation. To the extent that the interest payments exceed the rate of inflation, there is conferred on the dependants, through payment today of a stream of future income, a benefit which can be expressed as the "real rate of return". There would clearly be enrichment of the plaintiff at the expense of the defendant if the court did not take this benefit into account in making an award. Accordingly, the court applies a so-called "discount factor", i.e. the real rate of return which the plaintiff can expect to receive on the damage award

- [6] The purpose of applying a discount factor to determine a lump sum award for future loss is to afford full and fair compensation by restoring the plaintiff to the status quo ante, to the extent reasonably possible, without requiring the defendant to overpay: *Townsend v. Kroppmanns*, 2004 SCC 10 at para. 5; *Andrews v. Grand & Toy Alberta Ltd.*, [1978] 2 S.C.R. 229 at 241.
- [7] In the absence of legislation, complex expert economic and actuarial evidence is adduced to establish the appropriate discount rate. However, in *British Columbia s. 56 of the Law and Equity Act*, R.S.B.C. 1996, c. 253 empowers the Chief Justice of the British Columbia Supreme Court to prescribe mandatory discount rates to be used in calculating the present value of future pecuniary damages. Under s. 56(2)(a), the prescribed discount rate is the deemed future difference between the investment rate of interest and the rate of increase of earnings due to inflation and general increases in productivity. Under s. 56(2)(b), it is the deemed future difference between the investment rate of interest and the rate of general price inflation. These statutory discount rates are predicated on the assumption that awards for income loss and other future losses will be invested in low risk fixed-income securities which will produce the required annual payments from a fund that is self-liquidating in nature: *West v. Cotton* (1995), 10 B.C.L.R. (3d) 73 at para. 30 (C.A.). In *Cherry v. Borsman* (1992), 70 B.C.L.R. (2d) 273 (C.A.), this Court held that the statutory discount rate must be assumed to reflect reality as a matter of law.
- [8] On April 30, 2014, Chief Justice Hinkson reduced the statutory discount rate to reflect investment and economic reality. In particular, he reduced the discount rate under s. 56(2)(a) from 2.5% to 1.5% for loss of future earnings or dependency under the *Family Compensation Act*, R.S.B.C. 1996, c. 126 and the discount rate under s. 56(2)(b) from 3.5% to 2.0% for all other future damages, including future care costs: B.C. Reg. 74/2014. The previous rates had been in place since 1981, when the provisions were first added to the *Law and Equity Act*. The effect of the recent reduction in the statutory discount rate is to increase the size of pecuniary damages awards to ensure that plaintiffs have sufficient funds to provide the requisite future income stream through investment in low risk fixed-income securities.

Fund and Investment Management Services

- [9] Because the law recognises that future loss awards must be invested to provide sufficient funds for the future income stream in respect of which they are made, an additional sum may be needed to cover fund management. As explained in The Law Reform Commission of British Columbia, Report on Standardized Assumptions for Calculating Income Tax Gross-up and Management Fees in Assessing Damages (Vancouver: Ministry of Attorney General, 1994) (the "LRC Report"), the rationale for awarding fees for fund management services, investment management services or both is that the fund will be exhausted prematurely if the plaintiff is unable to perform these functions and, therefore, must pay others to do so. In other words, the purpose of including fund and investment management fees in a future loss award is to ensure that the value of the award is maintained over time and thus to adhere to the principle of awarding the plaintiff full and fair compensation: Townsend at paras. 5-6.
- [10] However, as Justice Sopinka explained in *Mandzuk v. I.C.B.C.*, [1988] 2 S.C.R. 650, an award for fund or investment management fees is not automatic. Entitlement to an award for such fees is a question of fact to be resolved based on the evidence in every case (at 651):

A plaintiff seeking to recover either a management fee or an investment counselling fee should provide a factual basis to the trier of fact, including:

- i. evidence that management assistance is in fact necessary;
- ii. evidence that investment advice is in fact necessary in the circumstances;
- iii. evidence as to the cost of such services.

- [11] The question of whether fund and investment management services are "necessary" and, if so, at what cost relates to what services are required to achieve a rate of return equal to the statutory discount rate: *Lines v. W & D Logging Co. Ltd.*, 2009 BCCA 106 at paras. 109, 117. Where the plaintiff is entitled to an award for investment management services, the defendant cannot go behind the deemed statutory discount rate to prove that greater returns will be achieved and claim a share of any excess benefit. As Justice Deschamps stated in Townsend at paras. 12-16, the legislature sought to avoid the need for complex actuarial evidence on inflation and rates of return in personal injury litigation by adopting a mandatory deemed discount rate. This goal could be indirectly defeated, she said, if such evidence is admitted when the plaintiff has established entitlement to management fees for services required to meet the discount rate.
- [12] In *West*, Justice Taylor explained that the low risk fixed-income securities that will produce the requisite annual payments can typically be purchased without a fee or professional investment assistance. However, he said, if the recipient of the award wishes to secure a greater return through diversification the cost of investment advice for that purpose should not be charged to the defendant:

- [30] The important factors in this regard are: (i) that the discount rates adopted by regulation under the Law and Equity Act, R.S.B.C. 1979 c. 224, s. 51, are predicated on the investment of awards for future care and loss of future earning capacity in interest-bearing government bonds, or similar secure bank or trust company investment certificates, and do not contemplate the need for dividends or capital gain in order to achieve the required annual payments from the assumed self-liquidating fund; (ii) that for the purchase of such interest-producing securities no brokerage house advice is required, but only the assistance of a bank or trust company officer, which is generally available without fee; (iii) that if the recipient of such an award wishes to secure a greater return than that contemplated in establishing the modest statutory discount rates, this involves the operation of an investment business for the profit of the recipient, and the costs of any investment advice required for that purpose cannot properly be charged to the defendant; (iv) that there will, however, be a need in many cases for the recipient of such an award to have accounting advice in order to ensure that investment terms are appropriate to produce the required annual income, and for this an appropriate allowance should be made; but (v) that a result of assuming investment wholly in interest-bearing securities will, of course, be a higher requirement for income-tax gross-up, on that portion of the award provided for future care, than would be the case were a more conventional "portfolio mix" presumed...
- [13] The third question in *Mandzuk* concerns service costs and requires assessment of the level of services needed to protect an award by producing a rate of return equal to the statutory discount rate. The authors of the LRC Report recommended a standardized four-level classification system in this regard. They also considered whether a nominal amount for management fees should be made in every case in which damages for future loss are awarded, but decided against recommending abolition of the evidentiary requirement. In doing so, they noted that the overwhelming majority of plaintiffs will need at least a minimum level of investment advice and that proving entitlement to such services will not be difficult.
- [14] The LRC Report classification system provides (at 52):
- Level 1 - The plaintiff requires only a single session of investment advice and the preparation of an investment plan at the beginning of the period the award is to cover.
- Level 2 - The plaintiff will require an initial investment plan and a review of the investment plan approximately every five years throughout the duration of the award.
- Level 3 - The plaintiff will need management services in relation to custody of the fund and accounting for investments on a continuous basis.
- Level 4 - The plaintiff will require full investment management services on a continuous basis, including custody of the fund, accounting, and discretionary responsibility for making and carrying out investment decisions. Such a plaintiff is likely to be mentally incapacitated or otherwise incapable of managing personal financial affairs.

- [15] The LRC Report classification system has never been legislated. Nevertheless, it has been referred to with approval repeatedly in the jurisprudence, including by Justice Deschamps in *Townsend*. In *Cikojevic v. Timm*, 2012 BCSC 1688 at para. 81, Justice Brown described the classification system as a "useful analytical tool" for judges in the assessment of claims for fund and investment management, although, he said, it does not represent a set of rigid categories into which every plaintiff will fit neatly. In my view, this was an accurate statement, particularly where, as here, continuous fund management by a professional trustee is contemplated and external investment management advice, if any, is to be provided separately.

Calculation Methodology

- [16] Investment income earned on the capital sum awarded for future care costs is subject to taxation. Where an evidentiary foundation is laid, the law recognises that an additional allowance is required to ensure the fund is not eroded prematurely by the tax liability. This is the so-called tax gross-up: *Watkins v. Olafson*, [1989] 2 S.C.R. 750. Like an award for management fees, the purpose of a gross-up award is to adhere to the compensatory principle. Three principles are particularly relevant to their calculation: i) damages are assessed, not calculated; ii) damages are awarded in a lump-sum to respect the principle of finality; and iii) the plaintiff has property of the award: *Townsend* at paras. 5-6, 17-21.
- [17] Calculation methodology is highly complex and technical. It involves multiple steps and a wide range of facts and assumptions, including factors such as tax and inflation rates, the nature and mix of the plaintiff's investment portfolio and the amount of other income that the plaintiff receives: *Scarff v. Wilson* (1988), 33 B.C.L.R. (2d) 290 (C.A.), rev'd in part [1989] 2 S.C.R. 776. In consequence, in selecting an appropriate methodology, the court inevitably depends heavily on expert economic and actuarial evidence. As occurred here, this often means that expert opinions on competing methodologies are placed before the court.

At Trial

- [18] At trial, the parties relied on an Agreed Statement of Facts regarding the nature and results of Matthew's injuries, Matthew's life expectancy and possible fee options for long-term fund management. As to the latter, the Agreed Statement of Facts outlined fee schedules that would apply if a private trust company, Solus Trust, is retained to act as a trustee, Investors Group is retained to act as an investment manager or ScotiaTrust is retained to act as both a trustee and an investment manager. As noted, the appellants conceded that comprehensive trustee services were required.

Evidence Regarding Trustee and Investment Management Services

- [19] Matthew's parents testified that they wish to be involved in making healthcare decisions but not in managing the settlement fund, which will be invested and spent to meet his needs until it is depleted. The judge heard that options for long-term management include trustee

services and investment management services provided by the Public Guardian and Trustee or, subject to court approval, appointment of a private trustee, appointment of an investment manager (possibly Solus Trust and Investors Group working together) or appointment of a private trustee providing both trustee and investment management services (possibly ScotiaTrust). He also heard that the non-negotiable fees of the Public Guardian and Trustee are set by regulation and, for combined trustee and investment services, would exceed those of Solus Trust/Investors Group or ScotiaTrust. Mr. Pestano testified that his preferred choice is Solus Trust working together with Investors Group.

- [20] John Blackmer is the president and CEO of Solus Trust. A lawyer and MBA graduate, he founded Solus Trust in 2005. Mr. Blackmer testified that Solus Trust is not affiliated with any financial institution, provides only fiduciary services and is not licensed or registered under the Securities Commission to give investment advice. If retained to act as Matthew's trustee, he explained, Solus Trust would administer the trust on a day-to-day basis and charge specified fees, but it would not make investment decisions on its own. Rather, he said, when managing funds the size of the settlement fund, Solus Trust's practice is to retain an external investment manager.
- [21] Mr. Blackmer went on to explain that, after consulting with Solus Trust concerning a trust, an external investment manager develops proposed parameters for prudent fund management. If Solus Trust agrees to the proposal and associated fees, the investment manager manages the fund, buying and selling within the agreed range, reporting back to Solus Trust regularly and sometimes making periodic payments to the trust. According to Mr. Blackmer, an investment manager typically invests a fund in a range of investments, with 30% to 70% of the portfolio invested in equities.
- [22] Counsel for Matthew asked Mr. Blackmer whether Solus Trust would be willing to work with an investment manager who assesses fund investments on a five-year basis and provides guidance to Solus Trust once in every five-year period. He replied that would not be appropriate because Solus Trust would not be meeting its fiduciary obligations as a prudent investor and, therefore, "we would not be prepared to - to take on the role if we were limited to an investment review every five years". He said nothing about the level of investment management assistance that Solus Trust needs to achieve a rate of return equal to the 2% discount rate, or any rate of return. Nor did any other witness.
- [23] For their part, the appellants called an economist, Douglas Hildebrand, who gave evidence on historical rates of return for fixed-income and mixed investment portfolios. He testified that, assuming a real rate of return of 5% per year based on historical averages rather than the prevailing 2% discount rate and depending on the calculation methodology employed, the predicted fund balance at the end of Matthew's life expectancy would be between approximately \$3,600,000 and \$5,000,000. Mr. Hildebrand confirmed on cross-examination that rates of return for short-term bonds are substantially smaller than for long-term bonds, that bond yields have been low since 2010 and that current short-term bond returns are below the 2% discount rate. He also agreed that it is possible historical bond yields may not

be the same as future yields.

- [24] In an exchange premised on active fund management, Mr. Hildebrand stated that an investment manager would presumably be "opportunistic" and move funds in advance to avoid losses caused by selling bonds before maturity in order to meet withdrawal needs. In the context of that exchange, he described the investment manager's job as including consideration of Matthew's needs, projecting what might happen in the market at any time and making related decisions on an ongoing basis.

Evidence Regarding Calculation Methodology

- [25] Mr. Hildebrand also testified regarding his recommended method for calculating income tax gross-ups and management fees. Robert Carson, an economist called by Matthew, testified regarding a different method that he recommends and actuarial experts critiqued both proposed methods. For present purposes, a detailed description of this complex evidence is unnecessary. However, an overview of its key points assists in contextualizing the judge's reasons and the appeal issues.
- [26] Prior to calculating the gross-ups, Messrs. Carson and Hildebrand prepared underlying income loss and cost of care valuations based on future care recommendations and an expert opinion on Matthew's life expectancy. Mr. Carson testified that, at the cost of care valuation stage, their calculations were based on the probability of Matthew living or dying in each year and not on the theory that he would need the specified amounts with certainty each year prior to death. These underlying valuations were used by both experts to calculate the gross-ups. In performing their calculations, both experts assumed a mixed investment portfolio.
- [27] Pierre Banville, an actuary, testified there are three main methods for calculating gross-ups to compensate plaintiffs for income tax and fees to be paid in respect of a future care cost award and thus to avoid its premature depletion. These methods were identified and discussed, he said, in an authoritative paper by a leading actuary, Brian Burnell. The first is the Life Certain Method, the second is the Probability of Survival Method and the third is the Probability of Death Method.
- [28] Mr. Banville explained that the Life Certain Method calculates the gross-up as the difference between the lump sum award (i.e., the capital sum required to cover future care costs) and the capital sum required to cover future costs of care, taxes and fees should the plaintiff live with certainty to the year the award is depleted, generally around the plaintiff's life expectancy. The Probability of Survival Method calculates the gross-up as the difference between the award and the capital sum required to cover future costs of care, taxes and fees should the plaintiff survive in accordance with the survival probabilities indicated in his or her mortality table. The Probability of Death Method calculates the gross-up as a weighted average of sub gross-ups, each of which is the difference calculated between the capital sum required to cover the future costs of care and the capital sum required to cover the future

costs of care, taxes and fees should the plaintiff survive to a specified number of years (between one year and the number of years until the plaintiff reaches age 110, which is the maximum in the life expectancy tables). The number of sub gross-ups depends on the plaintiff's age and mortality table and is calculated as 110 less the plaintiff's age plus one.

- [29] The Burnell paper was appended to an expert report written by Mr. Carson. In it, Mr. Burnell described the Life Certain Method as more easily explainable to a non-actuary, but expressed the view that its continued use was not reasonable because it includes a possible inherent invalidating distortion. He also described the Probability of Death Method as more complex and time-consuming than the Probability of Survival Method, although, he said, it is more theoretically correct where a low tax rate is concerned and it is the preferred method in cases involving a single tax rate.
- [30] In addition to the Burnell paper, the court was provided with evidence on the strengths and weaknesses of the three main calculation methods via witness testimony. Mr. Banville testified that none of them is perfect and all have issues. For example, according to Mr. Banville the Life Certain Method tends to have a fund deplete before the expected date of death, the Probability of Survival Method has an issue with first dollar income and tax credits and the Probability of Death Method tends to undervalue or overvalue the gross-up when there are mathematically progressive or regressive tax and fee schedules.
- [31] Mr. Hildebrand testified that his calculation method does not correspond precisely to any of the three main methods identified in Mr. Burnell's paper. Rather, he said, he starts with investment of the lump sum award from which annual withdrawals are made in accordance with care recommendations and he calculates the annual income from investment, taxes and fees based on the investment amount. In other words, to this point his fund simulation model is the same as the Life Certain Method. However, he explained, he goes on to apply the mortality table to each sub gross-up scenario and totals the mortality-adjusted calculations to deal with the probability of death. Mr. Hildebrand conceded that, under his approach, the fund would deplete approximately five years before the year of Matthew's expected death.
- [32] Mr. Banville characterized Mr. Hildebrand's method as an adjusted version of the Life Certain Method. He testified that it is not a generally accepted method, it systematically undervalues the gross-up and, for two reasons, it is mathematically incorrect. First, he said, the Hildebrand method applies the mortality assumption twice because the starting amount of the lump sum cost of care award is already reduced for the probability of death and then a subsequent mortality adjustment is applied when the tax gross-up and fees are calculated. Second, he said, the Hildebrand method makes the duration of the expected cost of care withdrawals approximately five years too short given Matthew's life expectancy.
- [33] Mr. Hildebrand acknowledged that his method "decouples" calculation of the present value for cost of care and lost income from calculation of income tax gross-up and fees because he starts with a lump sum assumed to be invested at the outset. In response to Mr. Banville's

criticisms, he provided an adjusted version extending the duration of care withdrawals to the equivalent of Matthew's life expectancy by reducing the projected withdrawal pattern and he testified that the second mortality adjustment is equivalent to an 8.3% reduction in the overall number.

- [34] Mr. Carson testified that his method corresponds to the Probability of Death Method. He said that, in Matthew's case, given his age, this meant running 97 hypothetical scenarios covering the potential range of life expectancies using the projected cost of care payment stream, then adjusting the amounts by incorporating the probability of death in each scenario based on the mortality table. He also testified that, while he did not base his calculations on the amount invested in the fund at any particular moment, he did base them on the actual lump sum agreed, which sum matched the cumulative present value of his model's computations. He testified further that he used a consistent valuation method in his underlying valuations and gross-up calculations and that under his method the fund runs out at Matthew's projected life expectancy.
- [35] According to Mr. Banville, the Carson method was reasonable and appropriate in this case, albeit not perfect. He acknowledged that in his report he stated the Probability of Death Method would not be appropriate if a gross-up calculation is deemed to take place after the award has been determined where, as here, taxes or fees are progressive or regressive. However, he testified, the potential problem is only "a slight issue". He testified further that when the problem arises the overvaluation and undervaluation typically offset one another quite well and the overall estimate is reasonable.

Reasons for Judgment

- [36] The judge began his reasons by summarizing the facts and the issues for determination. After addressing the first three issues, he turned to Matthew's claim for paid investment management assistance. He outlined the guiding principles for awarding management or investment counselling fees, then identified what he saw as the "real question":
- [17] The defendant acknowledges that neither the plaintiff nor his parents are in a position to manage the settlement funds themselves. This was a reasonable concession
- [18] Hence the real question is not whether the plaintiff needs paid investment management assistance, rather, it is what level of assistance is required.
- [19] The defendant suggests Level 2, while the plaintiff proposes assistance at Level 4.
- [37] The judge noted that the appellants accepted retaining a trust company such as Solus Trust to hold the settlement funds would be reasonable. He characterized the nature of the parties' dispute as whether additional support from an investment manager is required. Before reaching a conclusion on the point, he emphasized that, for calculation purposes, Mr. Hildebrand assumed the funds would be invested in a mixed portfolio. He also described his understanding of some of Mr. Hildebrand's testimony:

[22] Notably, the defendant's economist Mr. Hildebrand assumed that the funds would be invested in a mixed portfolio in his calculations (as did Mr. Carson). He also testified that if long term bonds were purchased, there would be a risk of losses if the bonds had to be sold before maturity. As such, he agreed that any manager would need to be "opportunistic" to guard against this outcome. He agreed that a professional investment manager would be required to look at what care needs are projected, and what might need to happen with the investments over the necessary timelines.

[23] It is difficult to see how Level 2 assistance would be consistent with this assumed need for more active management. Indeed, the defendant agreed that it would be reasonable for Solus Trust to hire an outside investment manager, but submitted that the defendant should not be required to pay for this assistance. However, as a basic starting point, neither the plaintiff nor any custodial trustee would have had any need to hire an investment manager to perform the work contemplated by Mr. Hildebrand absent the assumed negligence of the defendant: *Yeung (Guardian ad Litem of) v. Au*, 2007 BCSC 175 at para. 45.

[Emphasis added.]

[38] The judge went on to note that Solus Trust was not willing to provide investment advice on its own, nor was it licensed to act as an investment advisor. He referred to Mr. Blackmer's testimony that Solus Trust's "prudent investor" rules require it to obtain outside assistance in this situation and that its proposed fees were based on acting solely as trustee. He described this evidence as "supportive of the need to hire an external investment manager in order to achieve the requisite rate of return" (at para. 24) and said a similar debate was considered in *Cikojevic*, quoting extensively from that decision (at paras. 25-27). He also reviewed several other authorities that involved claims for investment management services (at paras. 28-37).

[39] According to the judge, the appellants' position that they should only have to fund Solus Trust to do investment management on its own was inconsistent with Mr. Blackmer's evidence that hiring a professional at Level 2 of the classification system in the LRC Report would not be prudent. He also questioned the import of Mr. Hildebrand's evidence regarding historical rates of return:

[39] The defendant offered some evidence on historical levels of return in order to support its submission that outside investment assistance beyond Solus Trust was unnecessary to obtain the required rates of return. However, as any investor knows, "past performance is no indication of future results". Furthermore, Mr. Hildebrand's review of investment returns fails to appropriately acknowledge that:

1. over the most recent decade, S&P/TSX returns have been below long term historical averages;
2. there have been wild swings year over year within that time horizon;

3. historical S&P/TSX returns would likely have been achieved, at least in part, with the assistance of professional investment managers, whom the defendant suggests are unnecessary here; and
 4. Government of Canada 10 year bond yields are presently below the discount rate and have been since 2010, meaning that there is a legitimate concern that a simple passive and conservative investment strategy will not get the plaintiff the required rate of return over the important early years.
- [40] The judge concluded that Level 4 investment management assistance would be reasonable throughout the entire period of Matthew's life expectancy. In doing so, he described the appellants' argument as "perilously close to a suggestion that with the reduction in the discount rate to 2%, no one will ever require Level 4 assistance" (at para. 41). He also found Matthew's fee proposal was reasonable for gross-up purposes and the appellants' concern, namely, that with assistance from Investors Group, Matthew may be in a surplus position was irrelevant "[o]nce the court concludes that investment management services are necessary to achieve the discount rate" (at para. 46). The judge stated:
- [40] In this case, I find that investment assistance in line with the LRC Report's Level 4 would be the most reasonable, for the following reasons:
1. The plaintiff has put forward sufficient evidence that neither he, nor his parents, nor the proposed custodial trustee, can achieve the required rate of return assumed by the statutory discount rate on their own.
 2. Even the defendant's expert assumed the need for portfolio management in excess of Level 2.
 3. This is an extremely large award, in excess of \$5 million. As such, even small errors or gaps in the required investment results could yield significant shortfalls for the plaintiff in absolute terms.
 4. This award must last an extremely long period of time, with the plaintiff having a life expectancy of 56 years from trial. As such, even slight dips below the necessary level of return for short periods of time could yield outcomes that fall far short of the settlement's intended results, given the unfortunate power of negative compounding. This is particularly so at the front end of the investment horizon.
 5. If Solus Trust is accepted as a reasonable custodian of the settlement funds, the evidence before me is that it would require active outside investment management assistance. It is only with such assistance that the plaintiff could be expected to achieve the discount rate of return, given that Solus Trust will not make investment decisions on its own.
- [41] It is difficult to imagine a fact pattern that would require Level 4 assistance if this case does not. The plaintiff is a catastrophically injured infant who will never be able to make his own decisions, and is presently cared for by parents without material investment expertise

[42] As to duration, I see no basis to cut off this assumed level of investment management assistance at a specific point in time. There is sufficient evidence to assume Level 4 is required, and there is not sufficient evidence before me, unlike in Cikojevic, that there will be a specific point at which the investments will be able to enter a more passive pattern, or that the current market uncertainty supporting active management can be expected to cease as of a particular date.

[Emphasis added.]

[41] After dealing with the claim for investment management fees, the judge dismissed Matthew's claims for committee of the person fees and a contingency award for the risk that the Public Guardian and Trustee may need to assume trustee and investment management responsibilities in the future. Then he turned to the appropriate methodology for calculating gross-up awards.

[42] The judge began by referring to the historical debate regarding the Life Certain Method and Probability of Survival Method and the judicial consensus that emerged favouring the latter. He said the evidence at trial represented the second generation of that historical debate. In particular, he said, while both Messrs. Carson and Hildebrand accepted that the mortality tables must be factored into gross-up calculations the debate is now about "how and when within the order of operations that should occur" (at para. 55). He went on to summarize the Carson and Hildebrand methods, the critiques of the other expert witnesses and the applicable legal principles.

[43] Based on the evidence and applicable principles, the judge concluded that the Carson method should guide the calculation of the gross-up in this case. In reaching his conclusion, he cited Mr. Banville's evidence that the Carson method is preferable to the Hildebrand method because it aligns more closely with the development of the lump sum present values of the cost of care and income loss at the base of the gross-up calculations. He described the calculation path of the Carson method and found that it eventually yields a cumulative net present value sum which matches the cost of future care and income loss awards. He also noted that the Carson method is consistent with the Probability of Death Method whereas the Hildebrand method is outside any of the three main methods identified in Mr. Burnell's paper.

[44] The judge recognised there were issues of concern with respect to both the Carson and Hildebrand methods:

[58] Mr. Banville concedes that even the Probability of Death method has a problem, in that when management fees are regressive (in other words, when the percentage of fees go up if you are only investing smaller amounts), the method does not yield a perfect mathematical outcome if the calculation is deemed to occur after an award has been determined. The proposed fees here do have a regressive element. However, Mr. Banville clarified during his testimony that the global net effect of this problem is limited. While the regressive fees can cause the amounts to be undervalued, this is offset in whole or in part by the fact that the

progressive nature of our tax system can cause the amounts to be overvalued. The problem is also negated if the gross-up calculation is deemed to take place at the same time as the award is determined.

[59] As such, Mr. Banville's testimony was that the Probability of Death method is the most appropriate when compared to the other two approaches, which suffer from more fundamental difficulties

[61] Mr. Banville's critique of Mr. Hildebrand's approach is that:

1. It yields outcomes that are even lower than those that would be provided by the generally rejected "life certain" approach, by effectively using the "life certain" method to begin, and then applying the mortality risk to reduce the amounts further. Mr. Hildebrand did not dispute this.
2. It yields outcomes that would have the funds expiring earlier than the average expected life expectancy, even after factoring in the relevant discount rate. Mr. Hildebrand described that result as "regrettable", but said it was required by the mathematical formula.
3. It essentially discounts for the mortality risk twice. The withdrawals and their duration are made with certainty in a situation where the potential duration of those withdrawals has already been limited by the mortality assumptions used in the cost of care calculations, but then Mr. Hildebrand's method provides net amounts of taxes and fees that are again reduced for the risk of death. Or, as Mr. Carson puts it:

"The problem with Mr. Hildebrand's method is that if withdrawals are made with certainty, the implicit assumption is that the risk of death in each year is zero until the life expectancy age is reached, and that it is then 100% when the life expectancy age is reached. If the risk of death is 100% at the predicted age of death, then it is incorrect to apply mortality risks in the years prior to the expected age of death. This double counts death."

As noted above, Mr. Banville responds to the fundamental concern about the illustration of so-called unrealistic scenarios in Mr. Carson's method by noting that this is simply an intermediate step in the calculation. The final outcome is designed to yield amounts which match the agreed amounts.

[Emphasis added.]

[45] Next, the judge reviewed several case authorities. Based on this review, he rejected the appellants' argument that the Probability of Death Method violates the principle of finality because, he said, it is ultimately derived in a way that respects the final fixed amount of an award. He also held that, to the extent possible, gross-up methodology should provide funds at a level that will meet projected expenses throughout a plaintiff's lifetime and should be consistent with the methodology used for the underlying awards upon which the gross-up is based. Then he applied these general principles to the competing Carson and Hildebrand methods:

- [77] I find that these principles favour Mr. Carson's Probability of Death method, in that this method is more closely aligned to the probabilistic approach used to derive the cost of care and future income lost. By way of contrast, Mr. Hildebrand admits that his approach "decouples" the gross-up calculations from the underlying calculations. Furthermore, the Probability of Death method is more likely to yield a stream that matches the plaintiff's average expected life expectancy. Finally, Mr. Hildebrand accepted that the Burnell paper, from which the Probability of Death method was derived, is a recommended resource for actuaries
- [78] In terms of the defendant's critiques of the Probability of Death method, the concern about certain illustrated scenarios being unrealistic is overstated, since they were simply a step along the road of a longer mathematical calculation that eventually adjusts in such a way that the final expected outcome matches the award. Furthermore, this complaint overlooks that the interim scenarios in the early years vastly underutilize the agreed amount. This only highlights the need to assess the approach in its totality, not on the basis of what is illustrated half-way through the order of mathematical operations

[Emphasis in original.]

- [46] The judge concluded by stating that tax gross-up and management fees are assessed, not calculated, citing *Tucker (Public Trustee of) v. Asleson* (1991), 62 B.C.L.R. (2d) 78 (S.C.), *aff'd* in part (1993), 78 B.C.L.R. (2d) 173 (C.A.). However, he held, calculations consistent with his reasons should be performed before the assessment was finalized given the magnitude of the amounts in issue. Following completion of this process, based on those calculations he awarded \$1,738,400 for management fees and \$190,600 for tax gross-up. The award for management fees was comprised of \$997,060 for investment management fees and \$741,340 for trustee fees on invested funds of \$5,200,000.

On Appeal

Position of the Appellants

- [47] The appellants contend that the judge erred in law in assessing entitlement to paid investment management assistance from Matthew's standpoint rather than from the professional trustee's standpoint. In their submission, where a trustee manages a plaintiff's financial affairs, if investment management fees are claimed the focus should be on the abilities of the trustee, not on the abilities of the injured plaintiff. However, the judge simply assumed that investment management assistance was required and Level 4 was appropriate based on the catastrophic nature of Matthew's injuries. According to the appellants, this was a legal error because Matthew's injuries were irrelevant once they conceded that he was entitled to the services of a trustee.
- [48] The judge also erred, they say, in failing to consider whether paid investment management assistance was needed to achieve a rate of return equal to the 2% discount rate and thus whether entitlement was established. While the appellants acknowledge that it would be

reasonable for the trustee to retain professional investment management assistance to secure the best possible rate of return, they argue this does not mean they should have to pay for it, which point the judge failed to appreciate. In addition, they say, the judge erred in finding that investment management services were needed despite the presumption that the 2% discount rate will be achieved by purchasing fixed-income securities with the (typically unpaid) assistance of a bank or trust company officer and in the absence of any evidence to the contrary. The judge erred further, they say, by misinterpreting Mr. Hildebrand's testimony that he assumed a mixed portfolio in his calculations and active fund management, which assumptions pertained only to the gross-up calculation and not to the alleged need for paid investment management assistance in order to achieve the 2% discount rate.

- [49] Alternatively, the appellants contend, the judge erred in awarding Level 4 investment management assistance for the duration of Matthew's life expectancy. In doing so, they say, he ignored Mr. Hildebrand's evidence regarding historic long-term bond returns and the lack of evidence that active fund management at the maximum level is required for a period of over 50 years. He also shifted the burden of proof to them to disprove a long-term need for ongoing and active investment management assistance. At most, they say, an award of \$50,000 representing Level 2 investment management services for the duration of the fund would be appropriate. The appellants concede that where a plaintiff's entitlement to investment management assistance is predicated on fixed income investments, then income tax gross-up calculations should also be based on fixed income investments, thereby potentially increasing the award for income tax.
- [50] The appellants go on to contend that the judge also erred in awarding income tax gross-up and management fees based on the Carson method of calculation. In their submission, the Carson method is inconsistent with the principles articulated in leading authorities, including West and Townsend. According to the appellants, these authorities require that the starting point for gross-up calculations is the lump sum award and that the fund be self-extinguishing. However, they say, the Carson method bears no relation to the reality of the starting lump sum of \$5,200,000 and the judge erred in law when he used a calculation method that grossed up 97 hypotheticals rather than the lump sum the parties agreed upon.
- [51] The appellants submit further that, although the judge recognised the undervaluation and overvaluation problem with the Carson method, he failed to make a specific finding on its actual effect in this case and ignored Mr. Banyville's evidence that the Carson method was inappropriate in circumstances such as these. This, too, was an error, they say, particularly because the overvaluation in this case actually exceeded the undervaluation by approximately \$60,000. Accordingly, they submit, the judge committed a palpable and overriding error when he found the undervaluation and overvaluation were offsetting and he erred in principle in relying on an inherently flawed calculation method without first confirming the existence of an offset.

- [52] The appellants do not seek an order for a new trial on the gross-up calculation due to the judge's alleged errors. Rather, given the state of the record, they ask that we make our own assessment based on the Hildebrand method, extended for the duration of care withdrawals and adjusted for the treatment of mortality.

Position of Matthew

- [53] Matthew submits that the judge made no factual or legal error regarding entitlement to or level of investment management services. Accordingly, he says, appellate intervention is not justified. In support of this position, he emphasizes the factual nature of the judge's assessment and its foundation in the evidence. He also emphasizes the underlying purpose of the award, namely, to ensure that the sum for future care costs is not exhausted prematurely and thus that the appellants fund full and fair compensation.
- [54] In Matthew's submission, his abilities were the proper subject of the judge's inquiry into whether and what level of investment management services was required for his life expectancy. A trustee had not yet been appointed by the court, Solus Trust could not and would not act if a professional investment manager is not retained and, unless a trustee is appointed, the funds will be paid to the Public Guardian and Trustee to be managed at a significantly higher cost than the combined costs of Solus Trust and Investors Group. Without assistance, Matthew says, he cannot generate any investment earnings, nor will he ever be able to do so. In these circumstances, he submits, the judge correctly assessed entitlement to and level of investment managements services from his standpoint.
- [55] However, even if the judge should have considered these matters from the proposed trustee's standpoint, Matthew contends that he did not err in his assessment. In his submission, the uncontradicted evidence was that Solus Trust could not achieve the requisite discount rate, or any other, because it is not licensed under the Securities Act, R.S.B.C. 1996, c. 418, to provide investment advice. Therefore, he says, Solus Trust is also permanently unable to earn investment returns without professional management assistance. In addition, he submits, as provided in Townsend, he was not obliged to lead evidence regarding the level of services required to achieve a particular rate of return on fund investment. On the contrary, he says, in Townsend the Court stated that the parties in personal injury litigation should be discouraged from adducing such evidence.
- [56] Matthew says further that the judge did not misinterpret Mr. Hildebrand's evidence on the need for ongoing active investment management assistance. As he correctly understood, Mr. Hildebrand accepted that putting the fund entirely into bonds would be inappropriate and there would be negative risks for Matthew if bonds had to be sold at an inopportune time, which risks would be mitigated by the professional investment manager. Matthew submits the judge also correctly understood Mr. Hildebrand's evidence regarding current low bond yields, which he considered in finding that future rates of return may not predictably be as positive as historic returns. And, he says, the judge properly treated Mr. Hildebrand's evidence on the possible creation of a surplus estate as irrelevant, as provided in Townsend,

Cherry and Bystedt v. Hay, 2007 BCCA 84.

- [57] As to calculation methodology, Matthew submits that we must not retry this highly technical and complex factual matter on appeal, as requested by the appellants. The judge heard and considered the evidence of two economists, two actuaries and one tax accountant on the proposed methods of calculation, including evidence that both were imperfect but, as between the two, the Carson method was preferable. According to Matthew, the judge's decision to rely on the Carson method was well-supported on the evidence, consistent with governing legal principle and, in any event, ultimately an assessment, not a calculation. It was also fully explained by the judge in his reasons. In these circumstances, Matthew submits, there is no basis for appellate intervention.

Discussion

Standard of Review

- [58] The applicable standard of review depends on the nature of the issue under consideration. On questions of law, the standard is correctness and, where legal error is shown, this Court may replace the judge's opinion with its own. As to questions of fact or mixed fact and law, however, the standard is deferential. The judge is in a privileged position regarding the facts and this Court will interfere with his or her factual conclusions only if there is an obvious (palpable) and material (overriding) error: *Housen v. Nikolaisen*, 2002 SCC 33 at paras. 5-6, 8, 10.
- [59] In *Toneguzzo-Norvell (Guardian ad litem of) v. Burnaby Hospital*, [1994] 1 S.C.R. 114, the Supreme Court of Canada considered the standard of review for a judge's factual findings based on inferences drawn from conflicting testimony of expert witnesses. Justice McLachlin, as she then was, explained that appellate intervention on factual findings and conclusions is justified only if the judge has made a "manifest error, has ignored conclusive or relevant evidence, has misunderstood the evidence, or has drawn erroneous conclusions from it": *Toneguzzo-Norvell (Guardian ad litem of)* at 121. However, if a finding of fact is unsupported by any evidence this gives rise to a legal error: *Thunderbird Entertainment Ltd. v. Greater Vancouver Transportation Authority*, 2012 BCCA 294 at para. 39.
- [60] The assessment of damages is a factual finding, subject to a deferential standard: *Gregory v. Insurance Corp. of British Columbia*, 2011 BCCA 144 at para. 14. In particular, the question of whether a management fee or investment counselling fee should be awarded is a fact-specific inquiry, as is the requisite degree of any such assistance: *Mandzuk* at 651; *Lines* at para. 116. The same is true of a gross-up assessment: *Townsend* at para. 6.

Did the judge err in awarding Level 4 investment management fees for the duration of Matthew's life expectancy and, if so, how?

- [61] I am not persuaded that the judge assessed Matthew's entitlement to investment management fees from his standpoint rather than from the intended trustee's standpoint. Had he done so, I agree with the appellants that it would have been an error. Where a trustee is or predictably will be responsible for fund management on behalf of an incapable plaintiff the focus of analysis shifts from the plaintiff's ability to achieve a rate of return equal to the statutory discount rate to the trustee's ability to do so: *Cikojevic*. This is because the involvement of a trustee is a key aspect of a plaintiff's circumstances for purposes of answering the second and third questions in *Mandzuk*, namely, whether investment advice is necessary and, if so, at what level and cost: see, for example, *Li (Guardian ad litem of) v. Sandhu*, 2006 BCSC 949 and *Yeung (Guardian ad litem of) v. Au*, 2007 BCSC 175.
- [62] Nor am I persuaded that the judge failed to consider whether investment management assistance was needed to achieve a rate of return equal to the 2% statutory discount rate. Again, had he done so, it would have been an error: *Lines*. Although certain passages in the reasons do suggest this possibility, when they are read as a whole it is clear the judge concluded that neither Matthew nor Solus Trust could achieve the requisite rate of return without Level 4 assistance for the duration of Matthew's life expectancy. The real question is whether there was a basis in the evidence to support this factual conclusion. In my view, there was not.
- [63] This was not a case like *Cikojevic* where there was evidence that even a knowledgeable trustee would have difficulty achieving a rate of return equal to the statutory discount rate without investment management assistance. When *Cikojevic* was decided the prevailing discount rate was 3.5% and evidence was adduced to the effect that the trustee would likely need continuous external professional assistance to achieve the requisite returns by investing outside the range of low risk fixed-income bonds. In other words, in *Cikojevic* there was evidence establishing that the plaintiff was entitled to awards for both trustee and investment management fees in order to satisfy the compensatory principle. Contrary to Matthew's submission, the admission of such evidence is not inconsistent with *Townsend*, in which Justice Deschamps discouraged the presentation of evidence on the prospect of achieving rates of return over and above the statutory discount rate with investment advice when that advice is also required to achieve the statutory discount rate.
- [64] As noted, the judge relied heavily on *Cikojevic* in his analysis, stating that it involved "a similar debate" to the debate in this case. However, in my view, this was not an accurate statement. In this case, unlike *Cikojevic*, there was no evidence that Solus Trust, or any other possible trustee, required active investment management to achieve a rate of return equal to the statutory discount rate or that there was a realistic risk that investing in low risk long-term fixed-income securities would produce returns below the 2% statutory discount rate. In particular, Mr. Blackmer did not testify that Solus Trust would require active investment management of a mixed portfolio to achieve a rate of return equal to the statutory discount rate. Nor did any other witness.

- [65] Messrs. Carson and Hildebrand did testify that they assumed the fund would be invested in a mixed portfolio rather than entirely in secure long-term fixed-income securities. However, their assumptions related to the gross-up calculation, not to a purported need for active and continuous investment management of a mixed portfolio in order to achieve the requisite rate of return. In any event, the experts' assumptions were not evidence from which a need for Level 4 investment assistance for over 50 years could be assumed or inferred and, to the extent he found otherwise, the judge fell into error. Nor did Mr. Hildebrand's testimony regarding recent economic conditions or low short-term bond yields support such an inference. The statutory discount rate is based on long-term historic rates, it is assumed to reflect reality and there was no evidence which displaced that assumption.
- [66] Further, Mr. Blackmer's testimony that Solus Trust would not make investment decisions on its own or act as trustee if it is limited to five-year investment reviews did not support the judge's conclusion that Matthew requires Level 4 investment management services for an over 50 year period. Mr. Blackmer did not testify that Solus Trust would only act as trustee if the appellants funded the intended investment management assistance. While Solus Trust's intention to retain external investment assistance to maximize returns is in Matthew's best interests, accords with its fiduciary obligations and is undoubtedly prudent, unless those services are needed to achieve rates of return equal to the 2% statutory discount rate it would violate the compensatory principle to require the appellants to pay for them. To repeat, as Justice Taylor stated in *West* (at para. 30):
- if [the respondent or his trustee] wishes to secure a greater return than that contemplated in establishing the modest statutory discount rates, this involves the operation of an investment business for the profit of [the respondent or his trustee], and the costs of any investment advice required for that purpose cannot properly be charged to [the appellants]
- [67] In sum, in my view, the judge's finding that Level 4 investment management assistance for the duration of Matthew's life expectancy was required to achieve a rate of return equal to the statutory discount rate was manifestly erroneous. In making the award, he misunderstood some of Mr. Hildebrand's evidence, made findings unsupported by evidence and drew erroneous conclusions. As a result, I would set aside the order.
- [68] However, given the inability of the proposed trustee to provide any form of investment advice, the magnitude and duration of the award and the low threshold for establishing entitlement to a modest award based on the statutory discount rate, I would substitute an award of \$50,000 for investment management fees. This award is predicated on the assumption that the fund will be invested in low risk fixed-income securities and represents Level 2 investment management services for its duration.

Did the judge err in accepting the Carson method of calculation?

- [69] In my view, the judge's conclusion that the tax gross-up and management fees should be calculated using the Carson method was free of error. It was also well supported on the evidence. Accordingly, his conclusion should not be disturbed on appeal.
- [70] I do not accept the appellants' submission that the Carson method is not based on the actual lump sum award and thus conflicts with the finality principle articulated in Townsend. As outlined above, Messrs. Carson and Banville clearly explained that, in fact, Mr. Carson's calculations were based on the lump sum amount and they supported their testimony by referring to his reports, in which those calculations were set out in detail. They also testified that the fund would run out at the end of Matthew's life expectancy, which accords with the principles articulated in West. The judge accepted their evidence. That was his prerogative.
- [71] Nor do I accept the appellants' submission that Mr. Banville testified the Carson method was inappropriate, which the judge ignored when he accepted the Carson method. As outlined above, while Mr. Banville acknowledged stating in his report that the Probability of Death Method would not be appropriate where, as here, taxes or fees are progressive or regressive, he characterized the problem as "a slight issue" and testified the resulting overvaluation and undervaluation typically offset one another. Most importantly, he also testified that, despite the overvaluation/undervaluation issue, the Carson method was reasonable, appropriate and preferable to the Hildebrand method. The judge accepted Mr. Banville's evidence. Again, that was his prerogative.
- [72] Finally, I do not accept the appellants' submission that the judge found the undervaluation and overvaluation associated with progressive taxes and regressive fees actually offset one another in this case, which finding is mathematically inaccurate and thus unsupportable. The judge made no such finding of fact, nor was he obliged to do so. Rather, the judge found that the Carson method was imperfect and described the offset as being "in whole or in part", but he also found the Hildebrand method had more fundamental difficulties. As a result, he chose to assess the awards based on the Carson method. These conclusions were all supported on the evidence.
- [73] It follows that I would not give effect to this ground of appeal.

Conclusion

- [74] I have had the benefit of reading in draft the concurring reasons for judgment of Madam Justice Saunders and I agree with her additional comments.
- [75] I would allow the appeal in part, set aside the award for investment management fees and substitute an award of \$50,000. I would also remit the question of the income tax gross-up award to the trial court for recalculation in accordance with the appellants' concession and these reasons in the event the parties are unable to agree.

[76] Absent further submissions from the parties, as success was divided I would order that each side bear their own costs of the appeal. If the parties wish to address the issue of costs they may make arrangements with the registry to file written submissions by no later than May 31, 2019.

"The Honourable Madam Justice Dickson"

I AGREE:

"The Honourable Madam Justice Fenlon"

Reasons for Judgment of the Honourable Madam Justice Saunders:

[77] I have had the benefit of reading in draft the reasons for judgment of Madam Justice Dickson. I agree that the appeal should be allowed to the extent she describes, for the reasons she explains.

[78] In these additional comments I address the recovery of investment management fees as part of the damages award, in the context of the trustee's fiduciary obligation. Two aspects of the evidence suggest that the fiduciary duty of a trustee requires the fund to be invested in a more diverse way than is attainable by anything less than Level 4 advice. The first is the testimony of Mr. Blackmer to the effect his firm would not take on the role of a trustee unless provision is made for full investment advice. The second is the following paragraph in the Public Committee Handbook of the Public Guardian and Trustee:

The Patients Property Act says that, for the purposes of investing, all committees are trustees under the Trustee Act. The Trustee Act (Section 15) establishes the standard of care for trustees. This standard of care is known as that of a "prudent investor". Therefore, committees are required to exercise the care, skill, diligence, and judgment that a "prudent investor" would when making investment decisions. As a prudent investor, you are required to develop an investment plan or strategy and you should put it in writing. The definition of the prudent investor has generally evolved to mean:

- making necessary investments that a prudent investor would make to protect capital and provide income;
- developing risk and return objectives that are reasonable and suitable, given the size of the overall portfolio, and the circumstances of the investor;
- ensuring reasonable diversification of the type and class of investments;
- acting with prudence when delegating investment authority to an agent;
- incurring only reasonable and appropriate costs; and
- adopting a balanced approach to management investments.

[Emphasis added.]

[79] The proposition that a trustee's fiduciary obligation influences the recoverability of those fees as part of a damages award starts from Matthew's undoubted need for a committee, since by virtue of s. 15(2) of the Patients Property Act, R.S.B.C. 1996, c. 349, a committee is a trustee for the purposes of investing money. Matthew's need for a committee, in turn, arises from the grave brain injury that engendered this sizeable fund. In the event the committee/trustee's fiduciary duty to manage the fund requires a degree of diversification in the type and class of investments, arguably the costs of doing so are recoverable.

[80] The Public Committee Handbook correctly recognizes that the standard of the prudent investor has evolved in jurisprudence and is not particularized in the Trustee Act, R.S.B.C. 1996, c. 464. The Act provides:

15.1 (1) A trustee may invest property in any form of property or security in which a prudent investor might invest, including a security issued by an investment fund as defined in the Securities Act.

(2) Subsection (1) does not authorize a trustee to invest in a manner that is inconsistent with the trust.

15.2 In investing trust property, a trustee must exercise the care, skill, diligence and judgment that a prudent investor would exercise in making investments.

15.3 A trustee is not liable for a loss to the trust arising from the investment of trust property if the conduct of the trustee that led to the loss conformed to a plan or strategy for the investment of the trust property, comprising reasonable assessments of risk and return, that a prudent investor would adopt under comparable circumstances.

[81] The issue of investment diversification was discussed by Madam Justice Levine in *Miles v. Vince*, 2014 BCCA 289:

[53] The appellant argues that a prudent investor would not place all of the Insurance Trust's assets into one investment, but instead, would have a diversified portfolio of investments. The respondent says that she was under no statutory obligation to diversify the investment portfolio or invest the trust funds in any particular manner.

[54] In *Fales v. Canada Permanent Trust Co.*, [1977] 2 S.C.R. 302, the Supreme Court of Canada held that the primary duty of a trustee is to preserve trust assets. This principle applies despite broad discretionary powers given to the trustee in the trust document. Justice Dickson (as he then was) articulated this standard (at 316):

This standard, of course, may be relaxed or modified up to a point by the terms of a will and, in the present case, there can be no doubt that the co-trustees were given wide latitude. But, however wide the discretionary powers contained in the will, a trustee's primary duty is preservation of the trust assets, and the enlargement of recognized powers does not relieve him of the duty of using ordinary skill and prudence, nor from the application of common sense.

..

[58] Section 15.2 of the Trustee Act enacted in statutory form the standard of care for trustees investing trust property. As noted above, it requires an investor to exercise the care, skill, diligence and judgment of a prudent investor.

[59] The "prudent investor" is also referred to in s. 15.3 of the Trustee Act

[60] Professor Donovan Waters discusses the development of the "prudent investor" standard in Canada in Donovan W.M. Waters et al., *Waters' Law of Trusts in Canada*, 4th ed. (Toronto: Thomson Reuters Canada Limited, 2012) at 1006-1009.

[61] Professor Waters notes (at 1008) that in 1997 the Uniform Law Conference of Canada promulgated the Uniform Trustee Investment Act, 1997, which imposed an obligation for trustees to diversify investments and provided a list of factors which a trustee may consider in making investment decisions.

[62] He describes the "prudent investor" standard as used in the B.C. Trustee Act, (at 1018):

The reference to the "prudent investor" is intended to bring into the picture the requirements of modern portfolio theory, which teaches that one must first decide what is the level of appropriate level of risk, and then seek to maximize the return within that constraint.

[63] He points out that diversification is implicit in the prudent investor standard, based on modern portfolio theory (at 1019-1020):

It is true that in some jurisdictions, particularly those retaining the prudent man standard, there is room for argument as to whether the trustee has the duty to diversify. The new prudent investor standard, based on modern portfolio theory, leaves less room for argument; diversity is inherent in modern portfolio theory. Even so, the circumstances of a trust might be inconsistent with diversification. For example, if a trustee expected to hold property only for a few weeks, it might not be prudent to expose the assets to the volatility which inheres in equity investments.

[64] Unlike other jurisdictions in Canada, B.C.'s Trustee Act does not expressly impose a duty on trustees to diversify investments in accordance with modern portfolio theory (see *The Trustee Act*, 2009, S.S. 2009, c. T-23.01 s. 26; *Trustee Act*, R.S.O. 1990, c. T. 23 s. 27(6); *Trustee Act*, R.S.N.S. 1989, c. 479 s. 3B; *Trustee Act*, R.S.P.E.I. 1988, c. T-8 s. 3.1).

[65] As Professor Waters suggests, however, the "prudent investor" standard implicitly brings modern portfolio theory into play, and thus requires the trustee to assess the level of appropriate risk and whether diversification is required.

[Emphasis in original.]

[82] Thus, the guiding principles for investment of trust property are compliance with the trust instrument and reasonable prudence as viewed in the context of the particular trust.

- [83] Madam Justice Dickson correctly notes in her para. 7 that the fund is predicated upon the assumption that it "will be invested in secure fixed income securities which will produce the required annual payments from a fund that is self-liquidating in nature". As there is no statutory direction compelling diversification, I do not consider the fact of trusteeship for investing money is material to the outcome of the issue before us, given the context of this fund's creation as a settlement of a personal injury claim, the design of the fund to be self-liquidating, and the absence of evidence that the discount rate cannot be achieved by investing solely in high-quality interest-bearing instruments by means of Level 2 advice.
- [84] For these additional reasons, I concur with Madam Justice Dickson in the reasons and result.

"The Honourable Madam Justice Saunders"

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