

Court File No. 1056/10 CP

**ONTARIO
SUPERIOR COURT OF JUSTICE**

BETWEEN:

**THE ONTARIO FLUE-CURED TOBACCO GROWERS' MARKETING BOARD,
ANDY J. JACKO, BRIAN BASWICK, RON KICHLER
and ARPAD DOBRENTEY**

Plaintiffs

- and -

JTI-MACDONALD CORP.

Defendant

STATEMENT OF DEFENCE

1. The defendant JTI-MacDonald Corp. ("JTIM") admits the allegations contained in paragraph 8, 14, the second sentence of paragraph 15 and paragraph 16 (subject to supplementary agreements dated December 16, 1990, and February 6, 1991, and an addendum to the 1992 agreement dated November 9, 1992) of the statement of claim.
2. JTIM denies all other allegations in the statement of claim except as may be expressly admitted in this statement of defence and puts the plaintiffs to the strict proof thereof.
3. JTIM specifically denies that the plaintiffs are entitled to any of the relief claimed in paragraph 2 of the statement of claim.

The Parties

4. JTIM is incorporated under the laws of Canada with its head office in Mississauga, Ontario. At times material to the action, JTIM operated as RJR Macdonald Inc. and was primarily in the business of the manufacture, marketing, distribution and sale of Canadian-blend cigarettes and other tobacco products.

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5. The plaintiff Ontario Flue-Cured Tobacco Growers' Marketing Board (the "Board") is a local board within the meaning of the *Farm Products Marketing Act*, R.S.O. 1990, c. F-9. At the relevant time it was responsible for the control and regulation of the production and marketing of tobacco within Ontario.

6. The remaining plaintiffs are individuals with whom JTIM had no contractual relationship as set out below.

The Agreements

7. During the period January 1, 1986 to December 31, 1996, JTIM and other Canadian manufacturers of tobacco products agreed to purchase tobacco grown in Ontario under annual written agreements with the Board for each crop year (collectively the "Agreements").

8. The Agreements were between JTIM, other Canadian manufacturers and the Board, and not any individual grower, as the plaintiffs have admitted in paragraph 3 of the statement of claim.

9. The Agreements stipulated the minimum quantity and price of tobacco leaf purchased for use in products sold by JTIM and other manufacturers in Canada ("Domestic Accounts"). The Agreements also provided that JTIM and the other manufacturers would purchase specified quantities of tobacco for use in products sold outside of Canada for duty free and export ("Domestic Export Accounts" or "DFX Accounts") at or above stipulated minimum prices.

No Breach of the Agreements

10. JTIM denies the plaintiffs' allegations that it breached the Agreements. At all times material to the action, JTIM paid to the Board the amounts properly owing under the Agreements for the tobacco purchased under the Agreements, according to their terms.

11. JTIM also made the required disclosure to MacGillivray, contrary to the plaintiffs' allegations. JTIM duly disclosed to MacGillivray Partners its export sales, by category, and provided the auditors with full access to sales invoices and other records disclosing customers, shipment destinations, and quantities of shipments.

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12. JTIM therefore denies any liability for the alleged breach of the Agreements, or at all.

Tobacco Taxes Create Contraband Market

13. Beginning in 1987, the Canadian Federal and Provincial governments substantially increased taxes and duties on domestic tobacco products only. Those taxes and duties were not imposed on tobacco products for export. This created a significant difference in prices, which in turn resulted in tobacco products that had been exported from Canada being re-imported illegally and sold for less than the domestic tobacco products.

14. By 1990, the widespread availability of contraband tobacco products had become common knowledge in the Canadian public. The Board, the other plaintiffs, tobacco farmers and MacGillivray knew that DFX tobacco products were being illegally re-imported and sold in Canada.

15. The Agreements, including the pricing and volume of tobacco, were negotiated in the context of a known and increasing market for contraband DFX products containing DFX tobacco.

16. Under the Agreements, the Board sold increasing volumes of DFX tobacco to JTIM and the other manufacturers, knowing that a significant portion of DFX tobacco was being illegally re-imported into Canada and sold in Canada. The fact that some DFX tobacco was being sold in Canada through the market for contraband DFX tobacco products was considered and factored into the Agreements.

17. Despite actual knowledge of the smuggling, neither the Board, nor the other plaintiffs, made any complaint to JTIM alleging that the Board was entitled to be paid any additional amounts in respect of the tobacco sold to the DFX Accounts. On the contrary, the Board continued to sell increasing volumes of tobacco to JTIM for the DFX Accounts knowing that increasing volumes of that tobacco was being smuggled back into Canada for resale.

18. Each year, the Board negotiated and accepted the prices in the Agreements for domestic and DFX tobacco, with knowledge that DFX tobacco was used in contraband tobacco products. In doing so, it ratified the alleged breach of the Agreements, which breach is in any event denied.

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19. The plaintiffs wrongly suggest that they are entitled to effectively change the price now, for quantities of DFX tobacco purchased decades ago on the basis of the price in the Agreement. On the contrary, the plaintiffs cannot retroactively change the price, yet allege that the annually negotiated prices and quantities would have remained the same. Had the Board complained at the relevant time that it was entitled to receive a higher price for the tobacco sold to the DFX accounts, JTIM would have negotiated a commensurately lower price for the tobacco sold to Domestic Accounts, or chosen to purchase less tobacco.

20. Thus, even if the Board had a claim for breach of contract, which is denied, by its conduct it waived the claim, a waiver on which JTIM detrimentally relied. Further, as a result of the Board's conduct, the plaintiffs are estopped from now pursuing this claim.

No Damages

21. JTIM denies the plaintiffs have suffered any of the damages alleged in the statement of claim and puts them to the strict proof thereof. Further, to the extent the plaintiffs have suffered any damage, which is denied, such damages are excessive, remote and not foreseeable, and are not recoverable at law.

Claim is Statute Barred

22. The plaintiffs' knew or ought to have known of the claim by at least some 20 years before the claim was initiated, and likely much earlier. The action is therefore barred by the provisions of the *Limitations Act*, R.S.O. 1990, c. L.15, or alternatively, the provisions of the *Limitations Act, 2002*, S.O. 1990, c. 24.

Claim is Released

23. By agreement dated April 12, 2010, JTIM entered into a Comprehensive Settlement Agreement with Her Majesty the Queen in right of Canada and certain provinces and territories, including Ontario and Her Majesty the Queen in right of Ontario. The Comprehensive Settlement Agreement resolved any liability the JTIM may have in relation to the illegal contraband tobacco products at issue in this action.

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24. The Comprehensive Settlement includes a release of JTIM by Ontario and its Crown Agents for any and all claims in any way relating to contraband tobacco products, or any conduct relating to smuggling, exportation, transshipment, importation or re-importation of tobacco to and from Canada during the period January 1, 1985 to December 31, 1999. The plaintiffs' claim is captured by the release.

25. The Board, as a part of the Ontario government, is bound by the Comprehensive Settlement Agreement. In addition or in the alternative, the Board was at all material times an agent of the Crown and bound by the Comprehensive Settlement Agreement and its release.

26. JTIM therefore pleads and relies on the release as a complete defence to this claim and an estoppel to this claim.

27. Pursuant to its agreement with the Board, by pleading and relying on the release, JTIM does not waive its rights to require arbitration of any other issues under the Comprehensive Settlement Agreement.

Not a Proper Class Action

28. JTIM denies that the claim is properly a class action. If the action is certified, however, JTIM reserves the right to amend its statement of defence to address the class claims.

Action Should be Dismissed

29. JTIM asks that this action be dismissed, with substantial indemnity costs plus H.S.T. payable to JTIM.

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May 3, 2013

Torys LLP
Suite 3000
79 Wellington St. W.
Box 270, TD Centre
Toronto, Ontario
M5K 1N2 Canada

Wendy Matheson LSUC#: 28548T
Tel: 416-865-8133

Patrick D. Flaherty LSUC#: 34661L
Tel: 416-865-8113

Fax: 416-865-7380
Lawyers for the Defendant

TO: SUTTS, STROSBURG LLP
Lawyers
600 - 251 Goyeau Street
Windsor, ON N9A 6V4

HARVEY T. STROSBURG, Q.C.
LSUC#: 1264000
WILLIAM V. SASSO
LSUC# 121341
Tel: 519.561.6228
Fax: 519.561.6203

Lawyers for the Plaintiffs

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MARKETING BOARD et al

- and -

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Proceeding commenced at LONDON

STATEMENT OF DEFENCE

Torys LLP
Suite 3000
79 Wellington St. W.
Box 270, TD Centre
Toronto, Ontario
M5K 1N2 Canada

Wendy Matheson LSUC#: 28548T
Tel: 416-865-8133

Patrick D. Flaherty LSUC#: 34661L
Tel: 416-865-8113
Fax: 416.865.7380

Lawyers for the Defendant

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