CITATION: Dundee Oil and Gas Limited (Re), 2018 ONSC 6376
COURT FILE NO.: CV-18-591908-00CL
DATE: 20181024

SUPERIOR COURT OF JUSTICE – ONTARIO
(COMMERCIAL LIST)

RE: IN THE MATTER OF THE COMPANIES' CREDITORS ARRANGEMENT ACT, R.S.C. 1985, C. C-36 AS AMENDED

AND IN THE MATTER OF A PLAN OF COMPROMISE OR ARRANGEMENT OF DUNDEE OIL AND GAS LIMITED, (Applicant)

BEFORE: S.F. Dunphy J.

COUNSEL: *Grant Moffat and Rachel Bengino*, for the Monitor

Aubrey Kauffman for National Bank of Canada

Richard Swan for Lagasco Inc.

Adam Mortimer for MNRF

Victoria Yang for MacLeod Energy

Matthew Gottlieb and Andrew Winton for Canadian Overseas Petroleum Limited

HEARD at Toronto: October 24, 2018

REASONS FOR DECISION

[1] The Monitor has come before me asking for the court's advice and directions in relation to a further proposed extension of the closing date for an Asset Purchase Agreement previously approved by the court. This is not the first extension and the ground beneath this transaction has moved sufficiently far since my original approval of it that the Monitor thought it advisable to seek my advice and directions before moving forward any further with it. The Monitor has also discovered what appear to be various serious and material breaches of the confidentiality obligations of the purchaser under the APA for which the court's direction is also sought.

[2] In the circumstances of this case, I have been persuaded that a further three-week extension (to November 16, 2018) is justified and am authorizing the Monitor to proceed to agree to an extension providing it is satisfied as to the precise terms proposed and that such terms are reasonably in line with the proposal described to me in court (and referred to below).

Background Facts

[3] These proceedings began as a Notice of Intention to Make a Proposal of Dundee Oil and Gas Limited pursuant to the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3. On February 13, 2018, I approved an application to continue the proposal proceedings under the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36.

[4] On April 4, 2018, Dundee entered into an Asset Purchase Agreement with Lagasco Inc. as buyer. The APA came before me for approval on June 11, 2018. I approved the proposed transaction at that time and granted a number of requested vesting orders.

[5] Among other items of relief sought and granted at that time was an order pursuant to s. 11.3 of the *CCAA* assigning certain executory contracts. Prior to agreeing to that requested order, I had required the purchaser (Lagasco) to provide further evidence of its fitness as a proposed assignee. I also received information from the Monitor regarding a cash flow modelling exercise that had been performed on the proposed purchaser.

[6] This evidence was placed before me for two purposes. First, I needed to be satisfied that the purchaser would be a fit and proper assignee (and the evidence initially supplied to me suggested that the purchaser might have a high degree of leverage post-closing). Second, the Ministry of Natural Resources and Forestry would be required to consent to the transfer of Dundee's well licences under the APA and had a similar concern regarding the proposed assignee from the perspective of ensuring that capping and de-commissioning obligations related to exhausted wells would be attended to. MNRF has an obvious concern that operators not be permitted to extract all of the revenue from a well while leaving the de-commissioning costs of exhausted wells to be funded by the general public.

[7] The APA contemplated an outside date for closing of July 30, 2018 – only six weeks following court approval. It also contemplated that extensions to the outside closing date required the agreement of National Bank of Canada and the Monitor. I was advised in July that an initial extension of the closing date from July 30, 2018 to August 31, 2018 was required in order to provide time for the MNRF to complete its review and approval process.

[8] It was then the first material obstacle to closing emerged. Although not part of its initial financing plans, Lagasco reached an agreement with MacLeod Energy Limited to purchase some of the assets to be purchased by Lagasco at closing. It turned out that MacLeod (or an affiliate) was bound by an agreement with Canadian Overseas Petroleum Limited, itself an unsuccessful bidder for the Dundee assets to be purchased by Lagasco (and MacLeod). COPL learned of MacLeod's role and sought an injunction blocking MacLeod from purchasing any of the Dundee assets.

[9] The evolution of Lagasco's business plans had caused some delay in closing at all events because the monitor and MNRF now needed to re-evaluate the prior cash flow models to assess the future stability of two potential buyers instead of one. As the review

process continued in tandem with the scheduling of the injunction hearing, the parties agreed to a number of short-term extensions to the outside closing date – from August 31, 2018 until October 12, 2018. It emerged during this process that, while Lagasco had no financing condition in its favour in the APA and had represented that its financing was in place, it was no longer clear that Lagasco would be in a financial position to close absent the expected funds from the MacLeod sale. Some of the short extensions in September were directed at firming up alternative financing.

[10] On September 28, 2018, the second unexpected obstacle to closing exploded. Lagasco was dependent upon a commitment from PACE Savings and Credit Union Limited for the lion's share of its financing. The Monitor and National had both sought and obtained firm confirmations from PACE that its financing was in place when consenting to the closing extensions that were granted in late September. On September 28, 2018, PACE was placed in Administration by the Deposit Insurance Corporation of Ontario for reasons having no connection to the Dundee transaction.

[11] At first it appeared that PACE might nevertheless be prepared to honour its funding commitment notwithstanding the administration proceedings. On October 10, 2018, a Third Amending Agreement was reached whereby consent to a further extension of the outside date for closing from October 12, 2018 to October 26, 2018 was granted. To secure the consent of the Seller, Lagasco agreed to pay a non-refundable extension fee of $300,000 as well as a non-refundable professional cost fee of $150,000.

[12] Lagasco tried and failed to secure the consent of the administrator to the completion of the committed PACE financing. The reasons for that failure are not material – I am fully satisfied that Lagasco tried and that it reasonably believed that its efforts were not doomed to failure. However, that door is now closed.

[13] Patience of stakeholders on the seller's side has understandably worn thin. Including the Third Amending Agreement, a total of five extensions have been granted to the outside closing date. It is now clear that the transaction will not be able to close by October 26th either. PACE will not provide the needed funding.

[14] Lagasco has not thrown in the towel. It has secured a Term Sheet from a lender whom the Monitor acknowledges to be serious and credible. The Term Sheet appears to the Monitor to be credible as well. Lagasco has secured the agreement of PACE to allow its counsel to work for the new proposed lender, thereby shortening the learning curve and thus the time needed to close any financing to be provided under the Term Sheet. The proposed lender is bringing the Term Sheet to its credit committee in the morning of October 26th and is hopeful that the Term Sheet will secure the necessary approval to evolve into a full Commitment at that time.

[15] If these problems were not enough, a third bombshell emerged in the past few days. The Monitor has learned that Lagasco and its financial advisor have both established data rooms to enable potential investors in and lenders to Lagasco to assess the Dundee assets. Lagasco's reasons for doing so are clear enough – it is in need of

investors or lenders or both. It has had to scramble to deal with the consequences of the loss of the MacLeod transaction and then the PACE financing. However, Lagasco did not seek the Monitor's approval to take these steps, the parties who have accessed the data rooms have not been screened or approved by the Monitor and it seems clear that at least one party has received confidential information without agreeing to any confidentiality agreement at all, let alone one approved by the Monitor. The Monitor is of the view that there were agreements in place to prohibit all of this.

[16] Lagasco points out that these revelations have come about through the interventions of COPL, a party who it characterizes as a "bitter bidder" without standing who has nevertheless pulled out all of the stops to undermine the APA and prevent Lagasco from purchasing the Dundee assets.

[17] Lagasco's objections are beside the point. COPL may well be a bitter bidder, its standing may be dubious and it may have an obvious self-interest in having a second opportunity to acquire the Dundee assets, at an advantageous price if possible. None of this excuses breaches of solemn confidentiality obligations by Lagasco. The motives of the whistleblower are not the issue here.

[18] Before leaving the topic of COPL, I will make these observations. I see no utility or basis to cast aspersions upon COPL. While they may have had only a thin case for standing, and what standing they have had has been on sufferance, they have been resolutely straightforward in expressing and defending their interest. COPL's intervention may have sunk the MacLeod transaction, but Lagasco's APA was never contingent on that transaction and it was not even initiated until *after* court approval of the APA was granted. The Monitor has also satisfied itself that COPL did not cause the leak of confidential information that came to the Monitor's attention.

[19] If Lagasco has had its share of troubles, it cannot blame COPL for acting in its own self-interest where COPL has done so honestly and without underhanded dealings.

[20] The Monitor has outlined the evidence it has assembled of breaches of confidentiality obligations in its Sixth Report. The investigation is not complete and there are open questions. Some preliminary conclusions do emerge:

a. Lagasco appears to have been of the view that it was within its rights to do what it did – I have not heard argument on the point nor have I yet seen the underlying confidentiality and non-disclosure agreements that would need to be examined and thus am reaching no conclusion as to the merits of the claim one way or the other;

b. Lagasco has been fully co-operating with the Monitor to identify exactly what information went to whom and to contain the problem as fully as can be done;

c. Lagasco has been able to contact all but one of the parties who received such information.

[21] While the Monitor has been able to be satisfied that the genie is *mostly* back in the bottle, it is also clear that at least some information has gone to a party subject to no NDA and managed to make its way into the hands of COPL (who did not themselves procure anyone's breach of obligation). When confidential information from even one recipient makes its way into the public domain, the genie will be fully out of the bottle regardless of how much co-operation has been shown by all of the other recipients. We may not be there yet, but it seems we are perilously close to that point.

[22] In short, there appear to be potentially serious breaches of solemn confidentiality obligations. These breaches could have serious consequences to any future efforts of the Monitor to market the Dundee assets should the APA fail to close. The ability of the Monitor to control access to confidential information and to manage a process designed to maximize value may be seriously impaired. There is at least some evidence that Lagasco's actions might be characterized as an intentional breach of those confidentiality obligations regardless of what position Lagasco takes.

[23] I express all of these conclusions regarding breaches of confidentiality obligations with the utmost care because matters are only at a preliminary stage. However, CCAA cases evolve in real time and it is in real time that I must determine what directions to give. The Monitor must decide whether to extend the time for completing an APA where the Monitor has concluded that the purchaser has engaged in what appears to the Monitor to be significant and grave breaches of confidentiality obligations that may have far-reaching implications. The integrity of the entire sales process must be examined in light of this information.

Issues

[24] There are two related issues to be considered. Firstly and most immediately, I must consider whether the APA has passed the point of no-return or whether the Monitor ought to be advised by me to consent to a further extension of time. Secondly, I must consider what steps if any ought to be taken in light of the information contained in the Monitor's Sixth Report regarding breaches of confidentiality obligations.

Discussion and analysis

(a) Extension of the APA

(i) Position of the parties

[25] National Bank of Canada is by no means the only party with an economic interest in the APA, but it clearly has a very significant interest. National's secured loans will not be repaid in full should the transaction close. It will suffer a significant shortfall.

[26] National has reached two conclusions. First, it has negotiated a three-week extension (until November 16, 2018) on terms that include a payment of an extension fee to compensate the estate for some of the extensive costs that have been incurred by reason of the various extensions that have been required to date as well as the costs required to deal with the potential changes to the deal structure. The fee will be $300,000 per week of the extension in addition to an agreement to help defray additional professional fees over the same time frame ($75,000 per week). Second, National has now clearly drawn the proverbial line in the sand beyond which it is not prepared to go. If there is to be an extension, this is the last chance for this deal to be closed. If it does not close, National supports starting a new process and moving on. It will not consent to a further extension.

[27] There are other significant economic stakeholders who have a vital interest both in a closing and in the viability and stability of the purchaser going forward. These include landowners who have granted drilling and extraction rights, employees, the MNRF in respect of potential future liabilities for capping and those of Dundee's employees who would be kept on by the purchaser.

[28] The MNRF has played an active role in negotiations aimed at closing the APA and supports the extension proposal negotiated by National Bank. The other "going-forward" stakeholders have not been engaged to the same degree as MNRF and have not retained counsel or taken a formal position on the motion. I am however satisfied that their interests are reasonably aligned with MNRF's interest and thus attach significant weight to MNRF's position.

[29] Dundee at this stage is playing a somewhat passive role. It will not emerge intact from this transaction – its assets will all be sold and it will continue to have significant unpaid debt. It is trying to minimize the harm to its stakeholders and has indicated a willingness to abide by whatever directions the court provides.

[30] Finally I turn to Lagasco's submissions. Lagasco initially filed its own Notice of Motion seeking a mandatory extension of the closing date under the APA for its benefit as purchaser. That motion – which should have faced very considerable obstacles in terms of standing and jurisdiction had it proceeded – became moot by reason of the understanding reached with National shortly before the hearing. It was not proceeded with. Lagasco obviously supports me advising the Monitor to agree to a further extension on the terms of the agreement it has negotiated with National.

[31] Lagasco asks me to consider the following factors:

a. Lagasco has been acting in good faith. The delays that have occurred were both unexpected and unwanted. Lagasco had expected to have access to asset sales to fund its acquisition and did not count on the MacLeod transaction being effectively stymied by COPL's injunction application. Similarly, Lagasco did not anticipate that its principal lender, PACE, would be placed into administration on September 28, 2018 thereby knocking the

legs out from underneath its financing. While none of these problems are the seller's responsibility under the APA, these have been serious and unanticipated blows to Lagasco who has had to scramble on relatively short notice to cobble together alternatives.

b. Lagasco has invested a lot in the APA and is very heavily incented to see it to a successful closing. In addition to the devotion of a very considerable amount of time and energy to moving this transaction towards closing, Lagasco has paid a very significant deposit (10% of the cash purchase price), has paid a $300,000 extension fee already and is proposing to commit to paying more than a million dollars in further fees and expenses towards the transaction. These committed amounts are all before considering the professional fees incurred by Lagasco in bringing the transaction along this far. Lagasco's principals have been required to provide personal guarantees as well. Lagasco and its principals are heavily committed.

c. Lagasco has secured credible alternative financing, which financing is being submitted for credit committee approval on October 26, 2018. Lagasco has also secured the permission of PACE Credit Union to permit its former counsel to represent the proposed replacement lender – assuming approval of the credit is received – which will shorten the time needed to proceed from credit approval to closing.

(ii) Position of the Monitor

[32] The Monitor clearly plays an especially important role in cases such as this. The Monitor is always the eyes and ears of the court, but never more so than where some of the natural checks and balances of a multi-party restructuring transaction begin to wear down or lose their effectiveness.

[33] This is a liquidating CCAA. The debtor will not emerge and unsecured creditors with no on-going dealings with the purchased business will not receive anything. Creditors and stakeholders with an interest in the continuing business are numerous but diffuse – none have played a continuing and active role in this case, each of their interests being individually small relative to the costs of on-going participation and engagement.

[34] In cases such as this, the day to day supervisory and advisory role played by the Monitor acquires a particularly high level of importance and our courts rightly place a great deal of reliance and faith in the skill and integrity that our Monitors bring to the process.

[35] The Monitor has frankly and ably placed before me a host of concerns that are serious ones. I shall deal with the issue of the breaches of confidentiality undertakings below. Apart from that issue, the transaction is one that has morphed fairly significantly from the time of initial approval by me. These may be conveniently considered under the headings of timing, conditionality and structure.

Timing

[36] The APA is dated as of April 4, 2018 and was approved by me on June 11, 2018. It contemplated an outside closing date of July 30, 2018. The proposal negotiated by National and agreed to by Lagasco would see the outside closing date moved to November 16, 2018. The extent of the resulting delay in closing – regardless of the reasons for each such delay – is a prejudice in and of itself. Apart from the time value of money and the prejudice creditors suffer from further delay in receiving payment on their claims, this delay subjects the debtor's business to additional running costs and risk and inevitably entails the incurring of very significant costs relative to the continued operation of a debtor company in CCAA proceedings and the professional and other costs incurred in moving towards closing. Some of these costs – and indeed a very significant portion of these costs – would be offset by the extension fee already paid and the extension fees proposed to be paid pursuant to the tentative arrangement negotiated by National.

Conditionality

[37] Conditionality is another area of concern. Among the major selling points of the transaction as approved by me on June 11, 2018 was its unconditional nature. The buyer agreed to a substantial deposit and imposed relatively few conditions of closing. In particular, there was no financing condition. I cannot now speculate as to how attractive the Lagasco APA would have appeared in April 2018 had an accurate picture of the fragility of the buyer's financing been fully appreciated.

Structure

[38] The initial motion to approve the APA was deferred until June 11, 2018 in order to provide the parties with a further opportunity to satisfy me with appropriate evidence that the buyer was a fit and proper assignee of the executory contracts I was being asked to approve the assignment of pursuant to s. 11.3 of the CCAA. Lagasco as purchaser had provided evidence of the stability of the emerging business that enabled me to acquire a sufficient degree of comfort to exercise my discretion under s. 11.3 of the CCAA and approve the assignment of executory contracts. One of the factors in that approval was a cash flow forecast that considered the ability of the post-closing purchaser to service debt while meeting its rent and environmental responsibilities in relation to safe shut-down of exhausted wells. Lagasco's plans have been evolving since June 2018, largely in response to the various unexpected problems it has faced in its internal financing – problems that are not and never have been the responsibility of Dundee as vendor. The current plan is for a division of the business into two parts – one part holding off-shore wells and one part holding on-shore wells. The cash flow forecasts that underpinned my approval – and will be needed to secure the monitor's and MNRF approval – will need to be re-worked to reflect these changes and re-assessed to see whether there is a material difference that requires re-visiting.

[39] The Monitor is concerned – and rightly so – that the cumulative effect of these is to cast a shadow upon the integrity of the process it has run under my supervision and

the impact of the proposed extension on the integrity of the process ought to be an important consideration. While the Monitor has expressed these concerns, the Monitor has not reached the point where it is prepared to recommend that the APA be allowed to expire in accordance with its terms. Objectively, the Monitor views the transaction as being a valuable one. However, the Monitor was of the view that the integrity of the process concerns have acquired sufficient weight to warrant fresh consideration.

(iii) My conclusions

[40] While this case is not *Royal Bank of Canada v. Soundair Corp.*, 1991 CanLII 2727 (ON CA), I consider the *Soundair* principles are a good guideline to consider in cases where significant challenges have arisen to the integrity of the process. The interests of all of the parties – including that of the creditors in receiving the highest price – is by no means the only consideration to be weighed. The efficacy and integrity of the process and any unfairness in the working out of the process must also be considered. No one criterion is necessarily paramount.

[41] I consider the following factors material to my decision:

a. I have no basis at this point to conclude that a new process would likely deliver a higher or better price for the benefit of stakeholders. The efforts of the Monitor and the process to secure the highest and best offer have not been called into question by subsequent events. If this transaction is able to be nursed to the finish line, bandages and all, there is every reason to expect that it remains the best economic outcome viewed from the perspective of existing creditors and is a good outcome viewed from the perspective of on-going creditors.

b. The economic interests of the parties is not disregarded in the *Soundair* analysis and I do not disregard it here. The very significant losses suffered by creditors with the most at stake entitles them to a very sympathetic and attentive hearing. National's recommendation is a reasoned one and comes from the perspective of a frank acknowledgement of the possibility that it may have to take its lumps and start the process all over again. The MNRF also remains engaged in the transaction and its concern for the potential future capping and abandonment costs is a good proxy for the concerns of stakeholders with an on-going interest in the business.

c. The efficacy and integrity of the process is of course a matter of great concern here. The courts must always be vigilant to weed out parties who would abuse a court-supervised sales process to attempt a "bait and switch": promising high and delivering low when competition has packed its bags and gone home. Had I the sense that the purchaser has been manipulating the process with a view to seeking its own advantage, my approach might be quite different. The purchaser has not sought to lever uncertainty into a lower price. It is at least fair to observe that the purchaser

cannot be said to have deliberately provoked either the loss of the MacLeod transaction or the failure of the PACE financing. The purchaser has been dealing with adversity that it did not plan for and it has not sought to shirk its responsibility for dealing with it. The purchaser has made a very large investment in this transaction that it stands to lose should it fail to close. All of these factors persuade me that this purchaser has not set out to abuse the court's process or otherwise undermine the integrity of the sales process undertaken with the court's supervision.

d. For many of the reasons expressed in the preceding sub-paragraph, I cannot find that there has been unfairness in the working out of this process of a sort that would suggest that a termination of the APA is a desirable outcome at least where there is some reasonable basis to believe that this "last chance" option might succeed.

[42] The Monitor will be authorized to consider and if thought advisable to agree to an extension of the outside closing date under the APA to November 16, 2018 having regard to my reasons expressed above.

(b) Breach of Confidentiality Obligations

[43] I remain very, very concerned with the information I have received regarding possible breaches of solemn confidentiality obligations.

[44] One of the greatest attributes of the CCAA and the genius of the Canadian approach to the restructuring process generally is the flexibility and pragmatism that informs its procedures. Properly used, this can translate to swifter and better outcomes for stakeholders. Abused, this advantage can quickly become the Achilles heel of our system.

[45] While flexibility and pragmatism as operating principles free the system from the weight of rules and procedures that add no tangible value to stakeholder outcomes, these same principles impose a corresponding responsibility on the stakeholders to respect the integrity of the process. There are a large number of very vulnerable parties in restructuring proceedings. A debtor company's financial affairs are of great concern to its creditors but are also of great interest to its competitors if for different reasons. Every buyer of assets is looking for an edge and would like to eliminate competitive bids. Confidentiality agreements and NDA's have evolved as a critical tool to enable the court to protect a vulnerable estate and its stakeholders from being unduly put at risk by those with a vested interest in doing so. The entire process relies for its smooth functioning on the faith one and all can have in the integrity of the process. Unheralded and laden with boilerplate though they may be, NDA's play a critical role in maintaining that integrity.

[46] Receiving news that a purchaser has established unsanctioned data rooms and that parties unscreened by the Monitor have had wholesale access to sensitive commercial information stored there is unsettling in the extreme. We cannot permit our

system to degrade to one of parties cynically breaching obligations when it suits them with the intention of asking for forgiveness instead of permission. The end will not justify the means.

[47] The unexpected degree of pressure this purchaser has found itself under does not excuse these alleged breaches of confidentiality obligations even if it begins to offer the germ of an explanation. I cannot find on the evidence thus far uncovered that there was an intention to take advantage of the debtor or the debtor's stakeholders so much as an attempt to prevent the considerable losses that would be visited upon the purchaser by a collapse of this deal. There is some mitigation to be found in that negative fact.

[48] I have by no means reached a conclusion as to what consequences ought to follow from the breaches of confidentiality that have been outlined to me. The evidence is incomplete and there has been no time for considered argument by either side. However, I am satisfied that whatever has happened has not been actuated by an intention to undermine the integrity of the sales process even if the purchaser appears to have shown a considerable degree of disregard for it.

[49] I am therefore satisfied that the question of what breaches if any have occurred and what consequences ought to flow from them is one that can be addressed separately from the question of whether the APA ought to be given one last chance to close.

Disposition

[50] In summary then the following advice and directions are given to the Monitor:

a. The Monitor will be authorized to consider and if thought advisable to agree to an extension of the outside closing date under the APA to November 16, 2018 having regard to my reasons expressed above;

b. In considering any such extension agreement, the Monitor should be satisfied both as to the terms provided and that the extension is without prejudice to any rights arising from the breaches of confidentiality raised in the Monitor's Sixth Report;

c. The Monitor is authorized to arrange a hearing before me at 8:30 a.m. (maximum 90 minutes) on November 13, 14 or 15 through the Commercial List office to deal with any clean-up issues necessary to facilitate closing of the APA should this occur and, at such time, to report to me further regarding the breaches of confidentiality and any proposed actions to be taken in consequence as well as regarding the re-modelled cash flow dealing with the final transaction structure and the financial stability of the operator of the Dundee assets going forward; and

d. The Monitor is directed to take such steps as it deems necessary to be in a position to resume the sales process at a running start should this

transaction fail to close on November 16, 2018. It must be clear to all that this is the LAST chance to salvage this APA.

S.F. Dunphy J.

Date: October 24, 2018