

COURT OF APPEAL OF ALBERTA

COURT OF APPEAL FILE NUMBER **2001-0216AC**

TRIAL COURT FILE NUMBER / ESTATE NUMBERS 2001-05630

REGISTRY OFFICE CALGARY

APPLICANT DIAVIK DIAMOND MINES (2012) INC.

STATUS ON APPEAL PROPOSED APPELLANT
STATUS ON APPLICATION APPLICANT

RESPONDENTS DOMINION DIAMOND MINES ULC, DOMINION DIAMOND DELAWARE COMPANY LLC, DOMINION DIAMOND CANADA ULC, WASHINGTON DIAMOND INVESTMENTS, LLC, DOMINION DIAMOND HOLDINGS, LLC AND DOMINION FINCO INC.

STATUS ON APPEAL PROPOSED RESPONDENTS
STATUS ON APPLICATION RESPONDENTS

DOCUMENT **APPLICATION TO SEEK LEAVE TO APPEAL PURSUANT TO SECTION 13 OF THE COMPANIES' CREDITORS ARRANGEMENT ACT**

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AND TO: THE BALANCE OF THE SERVICE LIST**WARNING**

If you do not come to Court either in person or by your lawyer, the Court may give the applicant what it wants in your absence. You will be bound by any order that the Court makes. If you want to take part in this application, you or your lawyer must attend in Court on the date and at the time shown at the beginning of the form. If you intend to give evidence or prepare a memorandum in response to the application, you must file and serve those documents in compliance with the Rules. (Rule 14.41 and 14.43)

NOTICE TO RESPONDENT(S)

You have the right to state your side of this matter before the Court.

To do so, you must be in Court when the application is heard as shown below:

Date:	As determined by the Court
Time:	As determined by the Court
Where:	Court of Appeal of Alberta, TransCanada Tower
Before:	Single judge of the Court (Rule 14.37)

Nature of Application and Relief Sought:

1. The Applicant, Diavik Diamond Mines (2012) Inc. ("**DDMI**"), seeks an Order:
 - (a) granting leave to appeal the order of the Honourable Madam Justice K.M. Eidsvik, granted November 4, 2020 (the "**November 4th Order**") that has the effect of requiring DDMI, a senior secured creditor, to return a portion of its collateral to the debtor in the midst of a liquidation and prior to the satisfaction of its senior secured claim;
 - (b) staying the operation of the November 4th Order pending the determination of DDMI's appeal;
 - (c) directing that, if leave to appeal is granted, the resulting appeal shall be heard on an expedited basis in accordance with a litigation schedule to be agreed between the parties or set by this Honourable Court under Rule 14.37;
 - (d) such further and other relief as DDMI may advise.

Grounds for making this application:

2. This application for leave to appeal is made under s. 13 of the *Companies' Creditors Arrangement Act*, RSC 1985 c. C-36, as amended (the "**CCAA**") and Rules 14.5(1)(f) and 14.44 of the *Rules of Court*, Alta Reg 124/2010 (the "**Rules**").

The JVA

3. DDMI and Dominion Diamond Mines ULC ("**Dominion**") are successors in interest (in this capacity, each a "**Participant**") to the Diavik Joint Venture Agreement, dated March 23, 1995, as subsequently amended (collectively, the "**JVA**").

4. Pursuant to the JVA, DDMI holds a sixty percent (60%) interest in, and Dominion holds a forty (40%) interest in, a diamond mine site and various surrounding exploration properties (collectively, the "**Diavik Mine**") located approximately 300 kilometers northeast of Yellowknife, Northwest Territories.

5. The JVA provides that, in the event that either Participant defaults in its obligation to pay a cash contribution required by the JVA, the non-defaulting Participant is permitted to make such contribution on behalf of the defaulting Participant (each such payment is referred to as, a "**Cover Payment**"). The Cover Payment obligation is secured by a senior security interest in the defaulting Participant's interest in the Diavik Mine, including Dominion's share of production from the Diavik Mine (the "**Diamonds**").

Dominion's CCAA Filing

6. On April 22, 2020 (the "**Filing Date**"), Dominion applied for and was granted creditor protection under the CCAA. Dominion subsequently obtained: (i) an amended and restated initial order, granted on May 1, 2020; and (ii) a second amended and restated initial order, granted on June 19, 2020 (the "**SARIO**"). On November 4, 2020, Dominion obtained an extension of the stay of proceedings up to December 15, 2020.

Dominion's Post-Filing JVA Defaults

7. Dominion commenced its CCAA proceedings with the express intention of not paying its post-filing JVA obligations. As of October 19, 2020, Dominion is indebted to DDMI for Cover Payment obligations in the amount of \$119.52 million CAD, plus interest (presently estimated to be in the amount of \$2.37 million CAD) and legal fees, costs and expenses (the "**CP Indebtedness**"). All of the CP Indebtedness, other than a portion in the amount of approximately \$16 million relating to a Cash Call initially issued on April 9, 2020 and deferred to the week of April 15, 2020 to April 22, 2020 at Dominion's request, has been incurred since the Filing Date and is a post-filing obligation of Dominion.

8. Pursuant to paragraph 16 of the SARIO, DDMI is authorized to hold a portion of the Diamonds in an amount equal to the total value of the Cover Payments made by DDMI, at the production splitting facility in Yellowknife, Northwest Territories (the "**PSF**"). The value of the Diamonds that DDMI is entitled to hold is determined based on gross royalty valuations performed from time to time at the PSF by the Government of the Northwest Territories (the "**DICAN Valuation**").

Dominion's Failed SISP Procedures

9. Dominion elected to pursue a sale transaction with a related party through a stalking horse bid made by an affiliate of its parent company in its CCAA proceedings. The SARIO issued in June 2020 authorized Dominion to enter into the Stalking Horse Bid and directed that Dominion carry out the SISP Procedures (as such terms are defined in the SARIO).

10. The Stalking Horse Bid assigned no value to Dominion's interest in the Diavik Mine. The Stalking Horse Bid provided that the transaction contemplated thereunder was subject to reaching an agreement, acceptable to the bidder, with DDMI and the Government of the Northwest Territories in relation to timing and quantum of Cash Calls and reclamation liabilities (the "**Rio Condition**"). Pursuant to the Stalking Horse Bid, if the Rio Condition was not satisfied: (i) the Diavik Mine would be excluded from the transaction; and, (ii) the cash purchase price under the bid would not be reduced.

11. The SISP Procedures have concluded and Dominion's shareholder has elected not to complete the Stalking Horse Bid. Dominion's interest in the Diavik Mine did not attract any binding bids under the SISP Procedures.

The September 25 Order

12. The Chambers Justice issued an order on September 25, 2020 suspending the operation of paragraph 16 of the SARIO such that DDMI was not required to deliver any Diamonds to Dominion, pending further order of the Court.

13. Subsequently, on November 4, 2020, the Chambers Justice approved a process that allowed DDMI to recover on the CP Indebtedness (the “**Monetization Process Order**”). The recovery of the CP Indebtedness is being effected through a liquidation. Notwithstanding that the Chambers Justice approved a liquidation of the Diamonds through the Monetization Process Order, the Chambers Justice refused to continue the suspension on the delivery of Diamonds to Dominion. Rather, the November 4th Order was issued, with the result that DDMI will be required to deliver a portion of the Diamonds to Dominion if the value ascribed to the Diamonds by the DICAN Valuation exceeds the value of the CP Indebtedness.

The Errors of the Chambers Justice

14. The Chambers Justice made the following errors:

- (a) the Chambers Justice erred in law by requiring DDMI to return Diamonds, prior to the satisfaction of its senior secured claim. The law is that senior secured creditors are entitled to be paid from the proceeds of the sale of their collateral in full and prior to the release of such collateral, or resulting proceeds, to subordinate secured creditors, unsecured creditors and the debtor. Consistent with this basic principle, the Chambers Justice ordered the collateral over which DDMI holds the first-lien position to be liquidated to cash and that the proceeds be distributed in accordance with the agreed upon priority scheme. The law further provides that either subordinate creditors or the debtor may redeem DDMI’s security by payment of the obligations owed by Dominion to DDMI. That did not occur in this case.

The Chambers Judge erred in law in ordering DDMI's collateral to be returned to the debtor, which would make it available to other creditors, before DDMI's secured debt is fully satisfied. The order jeopardizes the rights of DDMI as the first secured creditor, contrary to the law;

- (b) the Chambers Justice erred in fact by making findings of fact that are entirely contrary to the uncontroverted evidentiary record. The Chambers Justice stated that "...the DICAN evaluation [sic] was proposed by DDMI" and that this was "...likely because it is the method that has been used for years between the parties to divide the diamond production." The Chambers Justice was then unconvinced that a change was required "...since the parties both agreed to this method a few months back." All of these facts are incorrect. DDMI never proposed that its right to hold Diamonds be based on the DICAN Valuation; this method was determined and ordered by the Chambers Justice as part of DDMI responding to Dominion's earlier stay extension application. The division of production from the Diavik Mine is based on an agreement between the parties that is entirely independent from, and does not involve, the DICAN Valuation. Finally, there never been an agreement on the usage of the DICAN Valuation as previously ordered by the Chambers Justice; and,
- (c) the Chambers Justice erred in principle in connection with the alternative relief sought by DDMI in the event the Court was not inclined to permit it to retain all of the Diamonds by failing to address the fact that the DICAN Valuation is a gross valuation and if Diamonds are to be returned it would

be just and equitable to allow DDMI to deduct from the gross DICAN Valuation at least 11% on account of fees and expenses. The Chambers Justice failed to consider uncontested and unconflicting evidence relating to the effect of sale, marketing, royalty and other fees and expenses on the sale recoveries of the Diamonds. The evidence on the application established, at a minimum, that such fees: (i) would be in the amount of 11%; and (ii) were not accounted for in the DICAN Valuation. Despite accepting the evidence on the point, the Chambers Justice did not account for the fact that DICAN provides a gross (not net) valuation and did not modify the DICAN Valuation as provided for in paragraph 16 of the SARIO.

Leave to Appeal

15. Leave to appeal under the CCAA is warranted:

- (a) the prospective appeal is more than *prima facie* meritorious. The decision subject to appeal is contrary to basic and well-established principles pertaining to the rights of creditors and debtors. The Chambers Justice authorized a liquidation on a manner that is inconsistent with the law and made findings of fact without an evidentiary basis. Further, the Chambers Justice accepted that realization costs should be accounted for in the DICAN Valuation but then failed to give any consideration to that finding in the resulting decision;
- (b) the issues raised by the appeal are significant to the practice. The reasoning of the Chambers Justice suggests that a CCAA-sanctioned

liquidation can be conducted in a manner that does not accord with the priorities established in federal bankruptcy legislation. In doing so, the Chambers Justice has sown doubt about the proper scheme of distribution in insolvency proceedings;

- (c) the issues raised by the appeal are significant to this CCAA proceeding specifically, as it will affect DDMI's priority position; potentially enrich subordinate creditors to DDMI's corresponding deprivation; and, potentially impact the sole operating business within Dominion's CCAA proceedings, the Diavik Mine. While it is trite that parties only seek leave in respect of decisions that are significant to the action, the CP Indebtedness currently exceeds \$120 million. Given Dominion's decision not to pay JVA obligations after the Filing Date, the CP Indebtedness will continue to be incurred. The Stalking Horse Bid did not ascribe value to the Diavik Mine and the Diavik Mine did not attract any bids under the SISP Procedures. The sale of the Diamonds is, at present, the only way that DDMI can effect recovery on the CP Indebtedness. The Diavik Mine employs over 1,100 persons and its continued operation is placed at risk by the decision; and,
- (d) there will not be undue or prejudicial delay, particularly if an order is granted to expedite the prospective appeal as sought by DDMI.

Stay of Proceedings

16. A stay of proceedings is required to prevent the prejudice that would result if DDMI is required to surrender any of the Diamonds pending the hearing of the appeal:

- (a) there is a serious question to be determined. The appeal involves a decision that does not accord with well-established legal principles and a failure to account for uncontested evidence on the written record;
- (b) not granting the stay would place DDMI at risk of surrendering a portion of the Diamonds to its insolvent counterparty prior to its debt being repaid in full, which constitutes irreparable harm; and,
- (c) the balance of convenience favours DDMI. The most recent Monitor's Report, dated October 27, 2020, establishes that Dominion has cash on hand of \$53.8 million and (other than its JVA obligations, which it has elected not to pay despite having the ability to do so) is able to meet its obligations in the ordinary course.

12. Such further and other grounds as the Applicant may advise and this Honourable Court may permit.

Material or evidence to be relied on:

17. The Affidavit of Katie Doran, sworn November 10, 2020.

18. Such further and other evidence as DDMI may advise of and as this Honourable Court may permit.

Applicable Acts, regulations and rules:

19. CCAA, including ss. 5.1, 14 and 22.

20. Rules, including 14.5, 14.37, 14.40 and 14.44.