CITATION: GrowthWorks Canadian Fund Ltd. (Re), 2019 ONSC 1659
COURT FILE NO.: CV-13-10279-00CL
DATE: 20190321

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 PROPOSED PLAN OF COMPROMISE OR ARRANGEMENT WITH RESPECT TO GROWTHWORKS CANADIAN FUND LTD.

BEFORE: Conway J.

COUNSEL: *Geoff R. Hall*, for GrowthWorks Canadian Fund Ltd.

Lawrence Ritchie and *Evan Thomas,* for Newbury Equity Partners II L.P.

Duncan C. Boswell, for GWC Limited Partnership and 2638475 Ontario Inc.

Caitlin Fell, for the Monitor, FTI Consulting Canada Inc.

HEARD: March 13, 2019

REASONS FOR DECISION

[1] GrowthWorks Canadian Fund Ltd. (the "**Fund**") brings a motion seeking the following relief:

(a) an order directing GWC Limited Partnership (the "**Partnership**") to pay deferred proceeds of $1 million to the Fund pursuant to s. 2.04 of the share purchase agreement between the Fund and the Partnership dated December 31, 2012 (the "**Share Purchase Agreement**"); and

(b) an order declaring that the purported removal by Newbury Equity Partners II L.P. ("**Newbury**") of the general partner of the Partnership contravened the stay of proceedings in the Amended and Restated Initial Order for the Fund dated October 1, 2013 (the "**Amended and Restated Initial Order**") and is null and void.

Background

[2] The Fund is a labour-sponsored venture capital fund. It has been under *Companies' Creditors Arrangement Act*[1] protection since October 2013.

[3] In 2012, the Fund began marketing certain of its portfolio investments in order to address serious liquidity issues that it was facing. Newbury, a Delaware limited partnership, expressed its interest in purchasing certain of the Fund's assets.

[4] On October 29, 2012, Newbury delivered a letter of intent to purchase various portfolio investments of the Fund, including securities of BTI Systems Inc. and OneChip Photonics Inc. (the "**BTI securities**" and "**OneChip securities**"). The purchase price consisted of an up-front payment of $20 million on closing, with a profit sharing mechanism for the Fund to receive additional proceeds if Newbury subsequently disposed of the purchased securities for an amount exceeding 150% of its invested capital. Newbury wanted to retain the current management team of the Fund to manage the portfolio investments going forward. The Fund accepted the letter of intent on November 1, 2012.

[5] After the letter of intent was accepted, Newbury discovered that there were potential significant Canadian tax issues with the BTI and OneChip securities, which were Canadian controlled private corporations. Newbury was concerned that on a subsequent disposition of the BTI and One/Chip securities, it could face both capital gains taxes in Canada and withholding taxes on any distribution of proceeds to Newbury in the United States. Given the significance of these tax issues, Newbury was prepared to walk away from the deal.

[6] Newbury came up with a proposal to address these potential tax Canadian issues. It proposed that the up-front payment to the Fund on closing would be reduced to $18 million, and that the Fund would receive the additional $2 million if Newbury was able to exit its BTI and OneChip investments free of Canadian taxes. This deferred payment structure would provide an incentive to the Fund (whose subsidiary would be managing the portfolio investments) to ensure that Newbury could exit the BTI/OneChip investments without incurring any Canadian taxes.

[7] Newbury prepared a revised letter of intent on December 4, 2012 incorporating these changes,[2] which the Fund accepted the next day. The parties proceeded to document and structure the transaction, which closed on December 31, 2012.

[8] The transaction was structured through a limited partnership (the Partnership) of which Newbury was the sole limited partner. The general partner of the Partnership was GWC GP Inc. (the "**GP**"), a wholly-owned subsidiary of the Fund. Pursuant to the Share Purchase Agreement,

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[1] R.S.C. 1985, c. C-36

[2] Newbury also changed the calculation for the profit sharing mechanism to be on an after-tax basis.

the Fund sold the portfolio investments (collectively, the "**Purchased Securities**") to the Partnership.[3]

[9] Pursuant to s. 2.02 of the Share Purchase Agreement, the up-front payment of the purchase price on closing was $18,409,824.[4] Section 2.03 of the Share Purchase Agreement contains the profit sharing mechanism, in which the Fund is entitled to receive additional consideration if Newbury subsequently disposes of the Purchased Securities for more than 150% of its invested capital.

Deferred Proceeds Clause

[10] Section 2.04 of the Share Purchase Agreement provides for the payment of $2 million in "Deferred Proceeds" by the Partnership to the Fund, if the Partnership disposes of the BTI or OneChip securities and distributes (or could distribute) the proceeds to Newbury without incurring any applicable Canadian Exit Tax. The clause reads as follows (my emphasis added):

> Section 2.04. **Deferred Proceeds**
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> If either:
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> (1) the Partnership or GWC III or any successor thereof, in one or more transactions (including pursuant to any amalgamation, winding-up or dissolution), disposes of the Underlying BTI Securities and/or the GWC III ULC Shares and any Follow-on Securities of BTI or GWC III held by it to a third party, or
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> (2) the Partnership or GWC IV or any successor thereof, in one or more transactions (including pursuant to any amalgamation, winding-up or dissolution), disposes of the Underlying OneChip Securities and/or the GWC IV ULC Shares and any Follow-on Securities of OneChip or GWC IV held by it to a third party,
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> (each disposition referred to in (1) or (2) a "**Disposition Event**"), in either case without any applicable Canadian Exit Tax being incurred by the Partnership or, in the case of Section 2.04(1), GWC III or, in the case of Section 2.04(2), GWC IV, as applicable, or any successor thereof and either (a) the Partnership, GWC III or GWC IV, as applicable, or any successor thereof distributes the proceeds from such disposition or dispositions (whether or not the amount so distributed is net of any costs (other than applicable Canadian Exit Tax) or expenses incurred in connection therewith or otherwise) to the Limited Partner without any applicable Canadian Exit Tax being incurred, or (b) the Partnership, GWC III or GWC IV, as applicable,

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[3] The Fund first transferred the BTI and OneChip securities to two British Columbia unlimited liability corporations (ULCs) and then sold the shares of those ULCs to the Partnership, along with the shares of the other portfolio investment companies.

[4] An additional $750,000 was paid for the Cytochroma Warrants, for a total purchase price of $19,159,824.

> or any successor thereof could, at the time of the completion of such disposition or dispositions, have made such a distribution to the Limited Partner without any applicable Canadian Exit Tax being incurred, then the Partnership will, within two (2) Business Days of the occurrence of a Disposition Event, concurrently give written notice of such occurrence to the Vendor and pay to the Vendor or as the Vendor may in writing direct the sum of $1,000,000 (the "**Deferred Proceeds**"), such amount to be payable in immediately available funds to an account specified by the Vendor or as the Vendor may in writing direct. For greater certainty, (i) the Deferred Proceeds, if any, can only be paid once in respect of a disposition of the Underlying BTI Securities and/or the GWC III ULC Shares and subsequent distribution of proceeds and once in respect of a disposition of the Underlying OneChip Securities and/or the GWC IV ULC Shares and subsequent distribution of proceeds, and (ii) the obligations of the Partnership under this Section 2.04 to pay Deferred Proceeds are not contingent on a Disposition Event occurring in respect of an event described in both Sections 2.04(1) and 2.04(2).

[11] The definition of "Canadian Exit Tax" reads as follows:

> "**Canadian Exit Tax**" means, without duplication, (i) the Taxes, if any, imposed under the laws of Canada and the provinces thereof on taxable capital gains or income realized by the Partnership on the sale of any ULC Shares, Underlying Securities or any Follow-on Securities and by the Corporations on the sale of any Underlying Securities or any Follow-on Securities, and (ii) withholding Taxes under Part XIII of the Tax Act imposed on any holder of limited partnership interests in the Partnership, non-voting securities of the Corporations, or a successor thereof in respect of any amounts paid or credited by Corporations, or any successor thereof, to the Partnership or to any holder of limited partnership interests in the Partnership or non-voting securities of a Corporation.

[12] The Partnership disposed of the BTI securities on April 1, 2016. On April 5, 2016, Timothy Lee, who was managing the Partnership's investments, sent an email to the Fund's legal counsel advising that the Partnership had sold the BTI securities for a loss. The Partnership distributed the proceeds from the sale of the BTI securities to Newbury on July 7, 2016. No Canadian Exit Tax was incurred on the disposition of the BTI securities by the Partnership or the distribution of proceeds to Newbury.

[13] On May 15, 2018, the Fund sent a letter to the Partnership demanding that it comply with its obligation to pay $1,000,000 in Deferred Proceeds to the Fund in respect of the disposition of the BTI securities. The Partnership refused to make the payment, taking the position that since it had sold the BTI securities at a loss, the requirement to pay Deferred Proceeds did not apply.

[14] On June 5, 2018, Newbury gave notice to the Fund that the GP was being removed as the general partner of the Partnership and being replaced by 2638475 Ontario Inc. On June 8, 2018, the Fund advised Newbury that the attempt to replace the GP as the general partner of the Partnership was stayed by the Amended and Restated Initial Order.

Issue #1 – Payment of Deferred Proceeds on the sale of the BTI securities

[15] The first issue is whether the Partnership is required to pay $1 million in Deferred Proceeds to the Fund in respect of the disposition of the BTI securities.

Positions of the Parties re s. 2.04 of the Share Purchase Agreement

[16] Newbury's position is that the Deferred Proceeds are payable under s. 2.04 only if the Partnership sells the BTI/OneChip securities for a gain or profit. Since the BTI securities were sold for a loss, the Fund is not entitled to receive the $1 million in Deferred Proceeds. Newbury submits that the definition of Canadian Exit Tax, which refers to taxes on capital gains and income, supports its position. Newbury argues that s. 2.04 was designed to create an incentive for the Fund to maximize the proceeds that Newbury would receive from the sale of the BTI/OneChip securities and to do so on a tax-free basis. Its position is that the parties never intended for the Fund to receive the $2 million payment if the BTI/OneChip securities were sold at a loss. The Partnership supports Newbury's position.

[17] The Fund's position is that it is entitled to receive the $1 million in Deferred Proceeds upon the sale of the BTI securities because the three conditions of s. 2.04 have been met, namely (i) the Partnership disposed of the BTI securities; (ii) the Partnership distributed the proceeds of such disposition to Newbury; and (iii) no applicable Canadian Exit Tax was incurred by the Partnership or Newbury on the disposition or distribution. The Fund submits that Newbury is trying to insert a fourth condition that is not included in s. 2.04, namely that the Deferred Proceeds are payable only if Newbury sells the BTI securities for a gain or profit. The Fund's position is that the deferral of $2 million of the purchase price was intended only to address Newbury's Canadian tax issues and had nothing to do with whether Newbury realized a gain or loss on its investment. Since Newbury has exited the BTI investment free of Canadian Exit Tax, the Fund is entitled to receive $1 million in Deferred Proceeds.

[18] Each side argues that its interpretation is supported by the language of the Share Purchase Agreement, properly interpreted in the context of the surrounding circumstances (or factual matrix) in which it was entered into.

Applicable Legal Principles

[19] The following principles of contract interpretation are set out in the Supreme Court of Canada case of *Sattva Capital Corp. v. Creston Moly Corp.*, 2014 SCC 53, at paras. 46 to 58:

- The overriding concern is to determine the intent of the parties and the scope of their understanding.

- The contract must be read as a whole, giving the words used their ordinary and grammatical meaning, consistent with the surrounding circumstances known to the parties at the time of formation of the contract.

- Evidence of surrounding circumstances must never be allowed to overwhelm the words of that agreement. The goal of examining such evidence is to deepen a decision-maker's understanding of the mutual and objective intentions of the parties as expressed in the words of the contract.

- The interpretation of a written contractual provision must always be grounded in the text and read in light of the entire contract. Courts cannot use surrounding circumstances to deviate from the text such that the court effectively creates a new agreement.

- The evidence of surrounding circumstances that can be relied upon consists only of objective evidence of the background facts at the time of the execution of the contract, that is, knowledge that was or reasonably ought to have been within the knowledge of both parties at or before the date of contracting.

[20] While evidence of negotiation and prior drafts of agreements is generally not admissible as part of the factual matrix, antecedent agreements such as a memorandum of understanding which has been agreed to by the parties may constitute objective evidence of background facts.[5] Evidence of a party's subjective intentions in entering into the contract, however, is inadmissible.[6]

Analysis

[21] I agree with the Fund's interpretation of s. 2.04. It is supported by the clear language of the section, read in the context of the agreement as a whole and in light of the surrounding circumstances known to both parties at the time they entered into the Share Purchase Agreement.

[22] I first turn to the wording of s. 2.04. The section provides that if the Partnership disposes of the BTI/OneChip securities "without any applicable Canadian Exit Tax being incurred" by the Partnership and distributes the proceeds to Newbury "without any applicable Canadian Exit Tax being incurred" by Newbury, then the Fund is entitled to receive $2 million in Deferred Proceeds.[7]

[23] The wording of s. 2.04 is clear and unambiguous. It focuses only on whether the Partnership/Newbury incurs Canadian Exit Tax on a disposition of the BTI/OneChip securities and distribution of proceeds to Newbury. If no such taxes are incurred, the Fund is entitled to receive $2 million in Deferred Proceeds ($1 million for each of BTI and OneChip).

[24] There is nothing in s. 2.04 stating that the Fund can only receive the Deferred Proceeds if the Partnership/Newbury realizes a profit or gain on the disposition of the BTI/OneChip

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[5] *IFP Technologies (Canada) Inc. v. EnCana Midstream and Marketing*, 2017 ABCA 157, at paras. 84-85.

[6] *Sattva*, at para. 59

[7] Newbury placed some emphasis on the use of the word "applicable" in s. 2.04. I do not see how that word assists Newbury's interpretation. The clause provides that the Deferred Proceeds are payable unless the Partnership/Newbury incurs any Canadian Exit Tax, if applicable.

securities.[8] There is nothing that ties payment of the Deferred Proceeds to the sale of the BTI/OneChip securities at any particular price. There is nothing that relieves the Partnership/Newbury from paying the Deferred Proceeds if the BTI/OneChip securities are sold at a loss. As long as the securities are sold, at whatever the price, and the proceeds distributed free of Canadian Exit Tax, the Fund is entitled to receive the Deferred Proceeds.

[25] Newbury argues that the words "capital gains or income" in the definition of "Canadian Exit Tax" support its position that Newbury must only pay the Deferred Proceeds if it sells the BTI securities for a profit or gain. I disagree. The definition of "Canadian Exit Tax" merely identifies the taxes that, if payable by the Partnership/Newbury on a disposition, would disentitle the Fund from receiving the Deferred Proceeds under s. 2.04. However, if the Partnership/Newbury disposes of the BTI/OneChip securities without incurring any of these taxes, the Fund is entitled to receive the Deferred Proceeds.

[26] Newbury submits that the Deferred Proceeds mechanism in s. 2.04 was designed to create an incentive for the Fund (through the GP) to maximize profits on the sale of the BTI securities. I disagree. Section 2.03 of the Share Purchase Agreement contains the profit sharing mechanism that creates the incentive for the Fund to maximize profits. The incentive to the Fund in s. 2.04 is restricted only to ensuring that Newbury receives any proceeds of disposition for the BTI/OneChip securities free of Canadian Exit Tax.

[27] The factual matrix in which the Share Purchase Agreement was entered into supports this interpretation and sheds light on the purpose for which the Deferred Proceeds mechanism was included. Newbury was prepared to purchase the Purchased Securities for $20 million. That was the value it placed on the Purchased Securities and reflected the investment risk it was assuming. According to the deal negotiated by the parties, the Fund could receive an upside through the profit sharing mechanism, if the Purchased Securities increased in value. However, the Fund was not sharing in any downside risk. If the Purchased Securities decreased in value, that was Newbury's risk.

[28] Once Newbury discovered that it faced potential significant Canadian tax issues on a future disposition of the BTI and OneChip securities, it protected itself by reducing the amount of the purchase price payable on closing to $18 million and deferring the remaining $2 million. If Newbury was able to exit the BTI/OneChip investments without paying Canadian taxes, the Fund would "earn back" the $2 million, taking it back up to the $20 million purchase price that Newbury had agreed to pay for the Purchased Securities. The only risk the Fund assumed was that Newbury

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[8] I note that s. 2.03 provides for a payment of additional consideration to the Fund if disposition proceeds exceed 150% of Newbury's invested capital, i.e. for a profit or gain. If the parties had intended to restrict payment of the Deferred Proceeds in s. 2.04 to the disposition of the BTI/OneChip securities at a profit or gain, they could have used similar language to that contained in s. 2.03.

would not exit the BTI/OneChip investments free of Canadian taxes, in which case the Fund would not receive the $2 million of Deferred Proceeds for the Purchased Securities.[9]

[29] In my view, Newbury is attempting to shift the risk of loss on its investment onto the Fund. That was not the intention of the parties, as reflected in the clear language of the Share Purchase Agreement and the factual matrix in which they entered into the agreement. The deferral mechanism in s. 2.04 had nothing to do with the price at which Newbury resold the BTI/OneChip securities or whether the resale was at a profit or loss. It only had to do with whether Newbury could exit those investments free of Canadian taxes, in which case the Fund would receive the remaining $2 million of the original $20 million purchase price. Under the mechanism in s. 2.04, Newbury exited the BTI investment free of Canadian taxes. The Fund is now entitled to receive $1 million in Deferred Proceeds.

[30] Newbury advances two other arguments in support of its position.[10] First, it argues that the Fund is precluded from asserting a claim to the Deferred Proceeds on the basis of estoppel by convention. I reject that submission. Estoppel by convention requires that the parties have a shared assumption of fact or law: *Ryan v. Moore*, 2005 SCC 38. The record fails to establish that once Newbury sold the BTI securities, the parties ever had a shared assumption that the Deferred Proceeds were not payable to the Fund.[11]

[31] Finally, Newbury argues that the Fund's claim is statute barred. It submits that the Fund's claim was discoverable on April 5, 2016, when Mr. Lee sent an email to the Fund's counsel advising that the BTI securities had been sold at a material loss. I reject this submission. While the email generally referred to the deferred proceeds mechanism, it did not state that Newbury would not be paying the Deferred Proceeds to the Fund; only that the securities had been sold at a loss. Further, at the time of the email, the proceeds had not been distributed to Newbury – that did not occur until July 2016. The email did not state that any distribution to Newbury would or could be free of Canadian Exit Tax, which was a precondition for the Fund to receive the Deferred Proceeds payment. In my view, the earliest possible date that the Fund could have discovered that it had a claim was on December 12, 2016, when the Fund was advised that the BTI proceeds had been distributed to Newbury. Indeed, Newbury did not advise the Fund that there was an issue with the payment of the Deferred Proceeds until December 15, 2017. Since the Fund brought this

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[9] Each side presented hypothetical situations with respect to the operation and effect of s. 2.04 in order to support its position. None of those hypotheticals is helpful to the analysis of the parties' intention, which is reflected in the provisions of the Share Purchase Agreement, interpreted in light of the factual matrix in which the parties entered into the agreement.

[10] In its factum, Newbury advanced the argument that its interpretation of s. 2.04 was consistent with the parties' subsequent conduct. However, it did not pursue this argument at the hearing since it conceded that the language of s. 2.04, properly interpreted, is not ambiguous and would not meet the test for subsequent conduct evidence set out in *Shewchuk v. Blackmont Capital Inc.*, 2016 ONCA 912.

[11] Newbury relies on the silence of the Fund for a period of time after it received an email in December 2016 with respect to the disposition of the BTI securities. Given the subsequent communications to Newbury by the Fund and its counsel, I am not persuaded that any silence amounts to a shared assumption that the Deferred Proceeds did not have to be paid.

motion on November 2, 2018, less than two years after December 12, 2016, its claim is not statute-barred.

Issue #2 – Did the Removal of the GP Contravene the Stay Order?

[32] Section 15 of the Amended and Restated Initial Order imposes a broad stay of rights and remedies of any Person against or in respect of the Fund or affecting the "Business" or the "Property" of the Fund. The Business is defined generally as the business of the Fund and the Property is defined as "the Fund's current and future assets, undertakings and properties of every nature and kind whatsoever, and wherever situate including all proceeds thereof."

[33] The Fund argues that when Newbury exercised its rights under the Partnership's limited partnership agreement to remove the GP (a wholly owned subsidiary of the Fund) as the general partner of the Partnership, it contravened the stay order.

[34] I disagree. The Amended and Restated Initial Order does not expressly extend to the GP or to the Partnership. While the order does apply to "Portfolio Companies" in which the Fund held an investment interest, neither the GP nor the Partnership is listed as a Portfolio Company. The "Business" of the Fund does not include acting as general partner of the Fund – that is the business of the GP, which is a separate corporate entity. Further, the removal of the GP as the general partner of the Fund did not affect the "Property" of the Fund, as the Fund continues to hold the shares of the GP.

Decision

[35] I therefore grant an order that the Fund is entitled to receive $1 million in Deferred Proceeds pursuant to s. 2.04 of the Share Purchase Agreement in respect of the sale of the BTI securities.

[36] I dismiss the Fund's motion for an order declaring that the purported removal by Newbury of the GP contravened the stay of proceedings in the Amended and Restated Initial Order.

[37] Counsel agreed that the successful party on this motion would be entitled to costs of $50,000, all-inclusive. The primary issue on this motion was the payment of the Deferred Proceeds, on which the Fund was the successful party. The Partnership and Newbury shall therefore pay costs of the motion to the Fund in the amount of $50,000, inclusive of disbursements and taxes.

Conway J.

Date: March 21, 2019