COURT FILE NUMBER Q.B. ____ of 2015

COURT OF QUEEN'S BENCH FOR SASKATCHEWAN
IN BANKRUPTCY AND INSOLVENCY

JUDICIAL CENTRE SASKATOON

APPLICANT GOLDEN OPPORTUNITIES FUND INC.

RESPONDENT PHENOMENOME DISCOVERIES INC.

IN THE MATTER OF THE COMPANIES' CREDITORS ARRANGEMENTACT, RSC 1985, c C-36

AND IN THE MATTER OF A PROPOSED PLAN OF ARRANGEMENT FOR THE CREDITORS OF PHENOMENOME DISCOVERIES INC.

AND IN THE MATTER OF THE RECEIVERSHIP OF PHENOMENOME DISCOVERIES INC.

BRIEF OF LAW ON BEHALF OF GOLDEN OPPORTUNITIES FUND INC.

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BRIEF OF LAW ON BEHALF OF GOLDEN OPPORTUNITIES FUND INC.

I. INTRODUCTION

1. This Brief of Law is submitted on behalf of Golden Opportunities Fund Inc. ("**GOFI**"):

   a) in response to the application (the "**CCAA Application**") by Phenomenome Discoveries Inc. ("**PDI**" or the "**Debtor**") for relief pursuant to the *Companies' Creditors Arrangement Act,* RSC 1985, c C-36 ("**CCAA**"); and

   b) in support of the application by GOFI (the "**Receivership Application**") for an Order pursuant to section 243(1) of the *Bankruptcy and Insolvency Act*, RSC 1985, c B-3 (the "**BIA**") appointing FTI Consulting, Inc. (the "**Receiver**") as receiver of the property, assets and undertakings of the Debtor, including all proceeds thereof (the "**Property**").

2. In accordance with the practice of using the Saskatchewan Template Receivership Order in Saskatchewan receivership proceedings, GOFI has filed a redlined version of the Saskatchewan Template Receivership Order which identifies the limited manner in which the draft Receivership Order being requested by GOFI varies from the Saskatchewan Template Receivership Order approved by the Insolvency Panel of the Court of Queen's Bench for Saskatchewan.

II. FACTS

3. The facts relied upon by GOFI in this Brief of Law are set out in the Affidavits filed on behalf of GOFI in regard to these applications, including:

   a) the Affidavit of Gavin Preston sworn on November 23, 2015 (the "**Preston Affidavit**");

   b) the Affidavit of David Dube sworn on November 23, 2015 (the "**Dube Affidavit**");

   c) the Affidavit of Craig Bell sworn on November 23, 2015 (the "**Bell Affidavit**");

   d) the Affidavit of Peter Blaney sworn on November 23, 2015 (the "**Blaney Affidavit**"); and

e) the Affidavit of Barry Bridges sworn on November 2015 (the "**Bridges Affidavit**").

4. Unless otherwise defined herein, capitalized terms in this Brief of Law shall have the respective meanings ascribed to them in the Preston Affidavit.

III. ISSUES

5. GOFI respectfully submits that the CCAA Application and the Receivership Application raise the following issues for determination by this Honourable Court, namely:

a) Is PDI insolvent, such that GOFI was contractually entitled to demand payment of its loan from PDI?

b) In the absence of a resolution of the board of directors of PDI authorizing commencement of the CCAA Application, has the CCAA Application which Dayan Goodenowe has caused to be filed with the Court been validly commenced on behalf of PDI, such that the Court has jurisdiction to entertain the CCAA Application?

c) To what extent Is it necessary or appropriate for the Court to grant relief to PDI pursuant to the CCAA?

d) To what extent Is it just or convenient for the Court to grant an Order appointing a receiver of PDI upon the terms contained in the draft Receivership Order?

IV. ARGUMENT

Is PDI Insolvent?

6. As a preliminary matter, in the materials filed in support of the CCAA Application, PDI has taken issue with the right of GOFI to have demanded payment of the Loan from PDI. PDI relies upon a "standstill letter" dated June 8, 2015 addressed by GOFI to PDI comprising Exhibit "D" to the Affidavit of Dayan Goodenowe sworn on November 20, 2015 (the "**Goodenowe Affidavit**").

7. As described in paragraph 25 of the Preston Affidavit, the second sentence of the second paragraph of the June 8, 2015 letter contains a proviso or qualification reading as follows:

> Notwithstanding the foregoing it is understood by PDI that GOF reserves the right to make demand on the Debenture if GOF determines that PDI has become bankrupt or insolvent or has committed an act of bankruptcy or insolvency that jeopardizes GOF's position under the debenture.

8. The CCAA Application is predicated upon the foundation that PDI is a "debtor company" within the meaning of the CCAA. Section 2 of the CCAA defines "debtor company" to mean a company that:

a) is bankrupt or insolvent,

b) has committed an act of bankruptcy within the meaning of the BIA or been deemed insolvent within the meaning of the *Winding-up and Restructuring Act*, whether or not proceedings in respect of the company have been taken under either of those Acts,

c) has made an authorized assignment in bankruptcy, or has had a bankruptcy order against it, under the BIA, or

d) is in the course of being wound up under the *Winding-up and Restructuring Act* because it is insolvent.[1]

9. The filing of the CCAA Application by PDI therefore constitutes an irrefutable admission by PDI that it meets one of the above criteria and is, therefore, definitively insolvent.

10. In any event, PDI is insolvent as a result of having ceased to meet its liabilities as they become due, and is therefore an "insolvent person" as defined in section 2 of the BIA. In particular:

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[1] CCAA, s 2(1).

a) PDI has failed to pay arrears of rent to its landlord, Saskatchewan Opportunities Corporation, in amounts exceeding One Million, Five Hundred Thousand ($1,500,000.00) Dollars;

b) PDI has failed to pay the $1,096,552.16 owed by it to GOFI;

c) PDI lacks the resources required to meet monthly payroll obligations to its employees; and

d) PDI has ceased to pay its accounts payable to certain trade creditors in accordance with ordinary course terms of payment to such trade (including, without limitation, its patent lawyers, Gowlings LLP, to whom PDI owes approximately $500,000).[2]

Without a PDI Board Resolution Authorizing It, The CCAA Application Has Not Been Validly Commenced And Should Not Be Entertained By The Court

11. Those persons responsible for the filing of the CCAA Application (which persons appear to comprise Mr. Dayan Goodenowe solely) have expressed an intention in the CCAA Application itself for PDI to restructure its business and financial affairs.

12. In that regard, paragraphs 6(c) and 6(e) of the Application Without Notice filed on behalf of PDI on November 20, 2015 read as follows:

> (c) By reason of the facts and matters described above and in the Affidavit of Dayan Goodnough, PDI requires relief under the CCAA and a stay of proceedings against it by its creditors, in order to permit PDI to continue to carry on business operations, to manage the cash flow crisis created by it, and to pursue meaningful opportunities to restructure its business and financial affairs through a plan of compromise or arrangement with its creditors;
>
> ....
>
> (e) PDI intends to restructure its business and financial affairs and to propose one or more plans of compromise or arrangement to one or more classes of its creditors, in order to permit PDI to continue to carry on its business

[2] Preston Affidavit at para 29.

operations, to continue to pay its employees and to continue to contribute to the local economy; [Emphasis added]

13. The Amended and Restated Unanimous Shareholders' Agreement of PDI made as of July 9, 2012 (the "**PDI Shareholder Agreement**") is attached as Exhibit "A" to the Blaney Affidavit.

14. As described in paragraph 6 of the Blaney Affidavit, an application by PDI for relief under the CCAA is required, by virtue of Articles 4.8(a)(xviii) and 4.8(a)(xix) of the PDI Shareholder Agreement[3], to be supported by the approval of at least three-quarters of the votes cast by the directors of PDI at a duly convened meeting of the PDI board of directors.

15. In this case, the filing of the CCAA application appears to have been undertaken solely by Dayan Goodenowe on his own initiative, as such action was not approved by PDI's board of directors.[4]

16. Mr. Goodenowe's action in instructing his solicitors to bring the CCAA Application is therefore a nullity, as would be any relief granted by this Honourable Court in respect thereof.

17. Although the doctrine of ostensible authority prevents parties to contracts with a corporation from asserting a lack of corporate authority to enter into a contract, there is no analogous doctrine applicable to the bringing of a court application.

18. Rather, this Honourable Court must exercise its inherent jurisdiction to prevent frivolous lawsuits and abuses of process by individuals who invoke court processes without having the proper authority to do so.

19. GOFI therefore respectfully submits that the CCAA Application has not been validly commenced on behalf of PDI. As a result, the CCAA Application is an unauthorized initiative by Dayan Goodenowe which is not validly or properly before the Court and which should not be heard or entertained by the Court.

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[3] Article 4.8(a)(xiv) of the PDI Shareholder Agreement likely also applies to the CCAA Application so as to require approval of three-quarters of the PDI board of directors.
[4] Preston Affidavit, para's 53 to -55; Blaney Affidavit, para's 5 to 8.

CCAA Relief In Favour of PDI Is Neither Necessary Nor Appropriate In This Case

CCAA relief is not appropriate if existing management has lost confidence of creditors and stakeholders

20. An initial stay pursuant to the CCAA will not be granted where existing management has lost the confidence of significant creditors and stakeholders.[5] Rather, the granting of an initial order requires that the debtor act in good faith and with due diligence to outline a realistic and commercially reasonable plan for recovery.[6]

21. In this case, each of the Preston Affidavit, the Dube Affidavit, the Bell Affidavit, the Bridges Affidavit and the Blaney Affidavit provide compelling evidence that existing management of PDI (its President and CEO, Mr. Dayan Goodenowe) has lost the confidence of creditors (GOFI, the largest secured creditor), shareholders (including those shareholders represented by Peter Blaney, GOFI, Concord Centres Inc., PIC Investment Group Inc. and Barry and Bonnie Bridges – a shareholder group comprising the holders of more than one-third of the common shares of PDI) and directors (including Peter Blaney, at a minimum).

22. In these circumstances, CCAA case law instructs (and common sense suggests) that an elaborate initiative to grant protection to PDI under the CCAA is not appropriate. In the absence of trust and confidence in management of PDI among key PDI stakeholders, the goodwill and working relationships necessary to achieve the compromise required to drive a successful CCAA restructuring are absent.

CCAA relief is not appropriate if the debtor company has no source of interim financing with which to fund operations

23. There is no purpose to an initial order granting creditor protection pursuant to the CCAA if the debtor presents no viable plan, including a viable source of financing. Rather, "there should be a germ of a reasonable and realistic plan, particularly if there is opposition from the major stakeholders most at risk in the proposed restructuring."[7]

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[5] E.g. *Bargain Harold's Discount Ltd. v Paribas Bank of Canada* (1992), 10 CBR (3d) 23, 7 OR (3d) 362; Serra, *Rescue!*, *ibid* at 35.
[6] *Alberta Treasury Branches v Tallgrass Energy Corp*, 2013 ABQB 432 at paras 12-17, 8 CBR (6th) 161 [*Tallgrass*].
[7] *Tallgrass*, *ibid* at para 13.

24. The Goodenowe Affidavit does not establish that PDI has any source of verifiable or documented interim financing with which to fund operations (including meeting its payroll obligations and paying its trade creditors). The only specific source of funding that is mentioned is a company which is controlled by Mr. Goodenowe. In light of the fact that Mr. Goodenowe is the source of many of the current problems plaguing PDI, GOFI submits that further financing arrangements involving Mr. Goodenowe are best viewed with a healthy degree of caution and skepticism.

25. Further, the requirements of good faith and due diligence are negated in this case by the ill-considered and frankly bizarre actions of Mr. Goodenowe in commencing the CCAA Application contrary to the PDI Shareholder Agreement and without notifying the PDI board of directors.[8]

26. PDI has lost the confidence of its key stakeholders and has no commercially reasonable plan for recovery. To the extent that PDI presents any plan whatsoever, it only represents "more of the same" and cannot be said to be an improvement. PDI continues to be controlled by Mr. Goodenowe, who has demonstrated that he cannot be relied upon to guide the Debtor back to financial stability. Where, as here, preservation of the *status quo* is unfeasible and unacceptable to the relevant stakeholders, GOFI submits that there is no tenable basis upon which an initial CCAA order can be granted.

It Is Just And Convenient To Appoint a Receiver of PDI

Legal framework for BIA receivership

27. GOFI brings the Receivership Application primarily pursuant to section 243(1) of the BIA, which section grants the Court the jurisdiction and authority, on application by a secured creditor, to appoint a receiver of the property of an insolvent person if it is "just or convenient to do so". The section reads as follows:

> 243(1) Subject to subsection (1.1), on application by a secured creditor, a court may appoint a receiver to do any or all of the following if it considers it to be just or convenient to do so:

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[8] Preston Affidavit at e.g. paras [**48-62**].

(a) take possession of all or substantially all of the inventory, accounts receivable or other property of an insolvent person or bankrupt that was acquired for or used in relation to a business carried on by the insolvent person or bankrupt;

(b) exercise any control that the court considers advisable over that property and over the insolvent person's or bankrupt's business; and

(c) take any other action that the court considers advisable.

(1.1) In the case of an insolvent person in respect of whose property a notice is to be sent under subsection 244(1), the court may not appoint a receiver under subsection (1) before the expiry of 10 days after the day on which the secured creditors sends the notice unless

(a) the insolvent person consents to an earlier enforcement under section 244(2); or

(b) the court considers it appropriate to appoint a receiver before then.

28. There are numerous factors which a court may consider in determining whether or not it is "just or convenient" to appoint a receiver. The following cases are instructive.

29. In *Bank of Montreal v Carnival National Leasing Ltd.*,[9] Bank of Montreal ("**BMO**") applied to appoint a receiver pursuant to section 243(1) of the BIA. Carnival was indebted to BMO for approximately $17 million and BMO held a general security agreement over the assets of Carnival, pursuant to which it had the right to appoint a private or court-appointed receiver. The Ontario Superior Court of Justice (Commercial List), citing the earlier decision of *Bank of Nova Scotia v Freure Village on Clair Creek*,[10] listed the following factors as being relevant to the court's determination:

a) the court must have regard to the nature of the property and the rights and interests of all parties in relation thereto;

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[9] *Bank of Montreal v Carnival National Leasing Ltd.*, 2011 ONSC 1007, 74 CBR (5th) 300 (OntSCJ) [*Carnival*]. [TAB A]

[10] *Bank of Nova Scotia v Freure Village on Clair Creek*, 40 CBR (3d) 274 (OntCJ GenDiv) [*Freure Village*]. [TAB B]

b) the fact that the moving party has a right under its security to appoint a receiver is an important factor to consider but so, in such circumstances, is the question of whether or not an appointment by the court is necessary to enable the receiver to carry out its work and duties more efficiently; and

c) it is not essential that the moving party, a secured creditor, establish that it will suffer irreparable harm if a receiver is not appointed.[11]

30. In *Kasten Energy Inc. v Shamrock Oil & Gas Ltd.*,[12] the Alberta Court of Queen's Bench listed the following additional non-exhaustive list of factors that may be considered in making a determination of whether it is just or convenient to appoint a receiver:

a) whether irreparable harm might be caused if no order were made, although it is not essential for a creditor to establish irreparable harm if a receiver is not appointed, particularly where the appointment of a receiver is authorized by the security documentation;

b) the risk to the security holder taking into consideration the size of the debtor's equity in the assets and the need for protection or safeguarding of the assets while litigation takes place;

c) the apprehended or actual waste of the debtor's assets;

d) the preservation and protection of the property pending judicial resolution;

e) the balance of convenience to the parties;

f) the fact that the creditor has the right to appoint a receiver under the documentation providing for the loan;

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[11] *Carnival* at para 24.

[12] *Kasten Energy Inc. v Shamrock Oil & Gas Ltd.*, 2013 ABQB 63, 20 PPSAC (3d) 128 [*Kasten*]. [TAB C]

g) the enforcement of rights under a security instrument where the security-holder encounters or expects to encounter difficulty with the debtor and others;

h) the principle that the appointment of a receiver is extraordinary relief which should be granted cautiously and sparingly;

i) the effect of the order upon the parties;

j) the conduct of the parties;

k) the length of time that a receiver may be in place;

l) the cost to the parties;

m) the likelihood of maximizing return to the parties; and

n) the goal of facilitating the duties of the receiver.[13]

31. The foregoing list of factors has also been cited and relied upon by the Supreme Court of British Columbia.[14]

A BIA Receivership Order Is Just and Convenient

32. Applying the relevant factors to the facts of this case, GOFI submits that it is both just and convenient to appoint a receiver of PDI in light of the facts and matters set forth below.

33. GOFI is a secured creditor of PDI that has advanced financing to PDI pursuant to a Debenture dated March 29, 2010 (the "**Debenture**"). As of November 10, 2015, PDIr

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[13] *Kasten* at para 13, citing Frank Bennett, *Bennett on Receiverships*, 2nd ed. (Toronto: Thompson Canada Ltd, 1995) at 130.

[14] See e.g. *Maple Trade Finance Inc. v CY Oriental Holdings Ltd.*, 2009 BCSC 1527, 60 CBR (5th) 142 at para 25 [*Maple Trade*]. [TAB D]

was indebted to GOFI in the total aggregate amount of $1,096,552.16, plus interest accruing thereafter, in addition to legal fees to date (the "**Indebtedness**").[15]

34. In order to secure repayment by PDI to GOFI of amounts advanced pursuant to the Debenture, GOFI was granted a security interest in all of the undertaking, property and assets of PDI described in Section 3.1 of the Debenture (the "**Security**").

35. As discussed above, it is definitively the case that PDI is insolvent.

36. As a result of the insolvency of the Debtor described above and in the Preston Affidavit, it became necessary and appropriate for GOFI to demand repayment of the entire amount of the Indebtedness from PDI the Debtor and to serve upon PDI on November 10, 2015, a Notice of Intention to Enforce Security under section 244 of the BIA.[16]

37. An order appointing a receiver is not an extraordinary remedy where a secured creditor is exercising the right to enforce its security.[17] Courts have consistently held that, where a security document confers upon a secured creditor the right to apply to a court to appoint a receiver, that fact weighs heavily in support of granting the order.[18] In other words, it is both just and convenient for the court to enforce the express terms of the contract between the parties.

38. The Debenture confers upon GOFI the right to seek a court order appointing a receiver upon default by the Debtors thereunder. The Debenture had matured and was payable in full by PDI to GOFI. Further, the insolvency of PDI was an additional

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[15] Preston Affidavit at paras 13 and 31, and Exhibit E.

[16] *Ibid*.

[17] *Carnival*, *supra* note 9 at paras 25-26.

[18] See e.g. *Maple Trade*, *supra* note 14 at para 26.

event of default under the Debenture.[19] GOFI is therefore *prima facie* entitled to its chosen remedy.

39. The jurisprudence is clear that a secured creditor need not establish that irreparable harm may be caused if no order were made.[20] However, where such harm would likely ensue, it is an important factor for the Court's consideration. In this case, GOFI is likely to suffer irreparable harm if a receiver is not appointed.

40. As described above, the Security and the interests of all stakeholders of PDI (including GOFI) are in jeopardy under the control of Mr. Goodenowe, such that an Order appointing a Receiver is essential for the protection of the Security and the interests of all stakeholders (including GOFI).

41. Additionally, the overall balance of convenience favours the appointment of a receiver. PDI is in a highly precarious financial position and its leadership does not have the business judgment necessary to guide the Debtor's affairs during these difficult times.[21]

42. Furthermore, the dire situation at PDI is apparent from the following facts:

a) PDI is operating without a CFO, COO or in-house legal counsel and much of its former senior management team;[22]

b) the CEO of PDI does not utilize budgets or cash flow forecasts with which to administer the business and financial affairs of PDI;[23]

c) PDI is in danger of losing its remaining credibility in the market and the business and investment community;[24]

d) PRI owes arrears of rent of over $1,500,000 to its landlord;[25]

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[19] Preston Affidavit, Exhibit B, section 7.1(f) and 7.1(g).
[20] See e.g. *Carnival, supra* note 9.
[21] Blaney Affidavit, at para. 4, Dube Affidavit, Bell Affidavit, Bridges Affidavit and Preston Affidavit.
[22] Preston Affidavit, at para. 52(b).
[23] Blaney Affidavit, at para. 4.
[24] Preston Affidavit, at para. 52(a).
[25] Preston Affidavit, at para. 18(b).

e) PDI lacks the cash resources required to fund its payroll obligations for the month of December of 2015;

f) PDI lacks the cash resources required to meet its obligations to its patent lawyers, the law firm of Gowlings LLP, with the result that the maintenance of the intellectual property rights of PDI which are among its most valuable assets, are in jeopardy;[26] and

g) the President of PDI has purported to commence the CCAA Application contrary to the PDI Shareholder Agreement and without the corporate authority of PDI to do so.[27]

43. On the other hand, GOFI has identified a highly qualified insolvency professional, Deryck Helkaa of FTI Consulting, Inc., who is able and willing to take over the oversight of the Debtor's operations (if appointed by the Court as receiver).[28]

44. Further, in light of GOFI's strong interest in maintaining the business of the Debtor as a going concern, GOFI is committed to make all reasonable efforts (including, potentially, additional lending secured by a Receiver's Borrowing Charge) in order to permit PDI's operations to continue.[29] In light of the general lack of faith and confidence in Mr. Goodenowe's management of PDI, such financing will very likely not be available if Mr. Goodenowe remains in control of PDI.

45. Having regard to all of the relevant factors, GOFI submits that it is both just and convenient to appoint a receiver of the property of PDI. Such an outcome holds the best possible prospects for preservation of the enterprise value of PDI as a going concern and the preservation of the value of its Assets (including the development and commercialization of its technology). As presently constituted and governed under the authority of Mr. Goodenowe, PDI is not capable of managing these challenges.

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[26] Preston Affidavit, at para. 52(e).
[27] Blaney Affidavit, at para's 5 to 8.
[28] Preston Affidavit at para 67 and Exhibit "L".
[29] Preston Affidavit at para 62.

V. RELIEF REQUESTED

46. For all of the foregoing reasons, GOFI respectfully requests that this Honourable Court grant an Order appointing FTI Consulting, Inc. as receiver of PDI in accordance with the terms of the draft Receivership Order.

ALL OF WHICH IS RESPECTFULLY SUBMITTED this 23rd day of November, 2015.

MacPHERSON LESLIE & TYERMAN LLP

Per: _____
Jeffrey M. Lee, Q.C. and Paul Olfert,
counsel for Golden Opportunities Fund Inc.

VI. TABLE OF AUTHORITIES

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