

COURT FILE NUMBER	1601-11552
COURT	COURT OF QUEEN'S BENCH OF ALBERTA
JUDICIAL CENTRE	CALGARY
APPLICANT	NATIONAL BANK OF CANADA IN ITS CAPACITY AS ADMINISTRATIVE AGENT UNDER THAT CERTAIN AMENDED AND RESTATED CREDIT AGREEMENT DATED JANUARY 15, 2016, AS AMENDED
RESPONDENT	TWIN BUTTE ENERGY LTD. IN THE MATTER OF THE RECEIVERSHIP OF TWIN BUTTE ENERGY LTD.
PARTY FILING THIS DOCUMENT	FTI CONSULTING CANADA INC. in its capacity as Court-appointed Receiver of the current and future assets, undertakings and properties of TWIN BUTTE ENERGY LTD.
DOCUMENT	<b>BRIEF of the COURT-APPOINTED RECEIVER</b> <b>(Reply re: <i>Ad Hoc</i> Committee Application re: Subordination)</b>  <b><i>June 30, 2017</i></b>  <b>Honourable Mr. Justice Jeffrey</b>
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## I. OVERVIEW

1. This Brief is submitted by FTI Consulting Canada Inc. in its capacity as Court-appointed receiver and manager (**Receiver**) of Twin Butte Energy Ltd. (**Twin Butte**) and in reply to the Brief of Argument of the *Ad Hoc* Committee<sup>1</sup> filed June 7, 2017 (**Ad Hoc Brief**).
2. This application concerns the subordination provisions in the Convertible Debenture Indenture between Twin Butte and Valiant Trust Company dated December 13, 2013 (the **Indenture**). The Indenture provides for the issuance of 6.25% convertible unsecured subordinated debentures (the **Subordinated Debentures**).
3. The *Ad Hoc* Committee suggests that the subordination provisions governing the Subordinated Debentures do not apply. Alternatively, the *Ad Hoc* Committee says that if the subordination provisions do apply, they are not triggered in this case. The *Ad Hoc* Committee also argues that their “Debenture Damages Claim” is not captured by the subordination provisions in the Indenture such that even if the subordination provisions do apply to their “Debenture Debt Claim”, they do not subordinate the “Debenture Damages Claim”<sup>2</sup>.
4. The *Ad Hoc* Committee seeks a declaration from the Court compelling the Receiver to make distributions to all unsecured creditors, including holders of the Subordinated Debentures (**Subordinated Debentureholders**), on a *pari passu* basis.
5. The Receiver disagrees.
6. The subordination under the Indenture is clear: all “Senior Indebtedness<sup>3</sup>” as defined in the Indenture is repaid first even in a receivership; once “Senior Indebtedness” has been paid in full, then the outstanding unsecured indebtedness of the Subordinated Debentureholders may be satisfied.
7. In other words, the Subordinated Debentureholders are subordinated in right of repayment to all Senior Indebtedness. Accordingly, pursuant to the Indenture, the Receiver intends to effect distributions to holders of Senior Indebtedness first and to the fullest extent possible before making any distribution to the Subordinated Debentureholders.

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<sup>1</sup> As such term is defined in *Ad Hoc* Brief.

<sup>2</sup>The Subordinated Debentureholders advance two claims in the Claims Process: 1) the “Debenture Debt Claim” being the outstanding indebtedness plus interest under the Subordinated Debentures quantified at \$92,220,726.52; and 2) the “Debenture Damages Claim” being a damages claim for alleged breach of contract in the amount of \$92,700,125.07.

<sup>3</sup> The defined term “Senior Indebtedness” is not restricted to secured creditors but includes numerous classifications of unsecured indebtedness include “trade” creditors.

## II. BACKGROUND

### *Receiver's Necessary Involvement in this Application*

8. As detailed in the Receiver's Eighth Report, the Receiver discussed the subordination issue with the *Ad Hoc* Committee's counsel before the application materials and the Receiver's Report were filed. The *Ad Hoc* Committee's view then (as it remains now) was that the matter is between creditors and should not involve the Receiver. The Receiver takes a different view.
9. Following the filing of the application materials and the Receiver's Report, and upon hearing from multiple significant unsecured creditors of Twin Butte, the Receiver determined that it is in the best interests of all of Twin Butte's stakeholders that it provide the Court its view on the Indenture.
10. The Receiver made this determination given the divergent interpretations of the Indenture. The Receiver was also mindful of the Indenture's anticipated impact upon the recovery of Twin Butte's remaining creditors, to whom, like the Subordinated Debentureholders, the Receiver owes a duty to maximize distributions in an impartial, fair manner.
11. Moreover, the Indenture is the basis for the Subordinated Debentureholders' claim in the formal claims process. In that process, the Receiver assesses claims on their merits in light of the relevant contracts, law, Twin Butte records, and supporting documentation provided by the claimant. In the Subordinated Debentureholders' case, this requires the Receiver to analyze the Indenture and apply it in accordance with its terms as elaborated herein.
12. Indeed, Twin Butte is a party to the Indenture, and the Receiver is empowered to enforce Twin Butte's contracts<sup>4</sup>. Where enforcement of a contract materially impacts the recoveries of Twin Butte's creditors, as it does here, the Receiver's power to enforce verges on being obligatory given its fiduciary duty to act honestly and in the best interests of all interested parties.
13. It is against this backdrop that the Receiver states that its involvement in this application is not only proper but required.

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<sup>4</sup> Receivership Order granted September 1, 2016, by the Honourable Madam Justice B. E. C. Romaine, at paragraphs 3(c) and 3(u), excerpted in Appendix "A" to this Brief.

### ***Short Form Prospectus and Indenture Terms***

14. The Receiver's Eighth Report enclosed a copy of the Indenture<sup>5</sup> and a copy of the Short Form Prospectus<sup>6</sup> advertising the Indenture. Specific provisions in those documents are excerpted herein.
15. ***Short Form Prospectus.*** The Short Form Prospectus expressly states as follows regarding the rank and subordination of the Subordinated Debentureholders:

Rank: The Debentures will be direct, unsecured obligations of the Corporation and **will be fully subordinated to all Senior Indebtedness.** [...]

Subordination: The payment of the principal and premium, if any, of, and interest on, **the Debentures will be subordinated and postponed,** and subject in right of payment in the circumstances referred to below and more particularly as set forth in the Indenture, **to the full and final payment of all Senior Indebtedness of the Corporation.**

The Indenture will provide that **in the event of any insolvency or bankruptcy proceedings, or any receivership, [...] then holders of Senior Indebtedness will receive payment in full before the holders of Debentures will be entitled to receive any payment or distribution of any kind or character, whether in cash, property or securities, which may be payable or deliverable in any such event in respect of any of the Debentures or any unpaid interest accrued thereon. The Indenture will also provide that the Corporation will not make any payment, and the holders of the Debentures will not be entitled to demand, institute proceedings for the collection of, or receive any payment or benefit [...] on account of indebtedness represented by the Debentures: (a) in a manner inconsistent with the terms (as they exist on the date of issue) of the Debentures; or (b) at any time when a default or an event of default has occurred under the Senior Indebtedness and is continuing [...] unless the Senior Indebtedness has been repaid in full.** [Emphasis added.]

16. The Short Form Prospectus defines "Senior Indebtedness" broadly as "all obligations, liabilities and indebtedness of the Corporation which would, in accordance with IFRS [the Indenture references GAAP], be classified upon a consolidated balance sheet of the Corporation as liabilities of the Corporation", including "accounts payable to trade creditors".

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<sup>5</sup> Attached at Appendix "A" to the Receiver's Eighth Report.

<sup>6</sup> Attached at Appendix "B" to the Receiver's Eighth Report.

17. Accordingly, any purchaser of the Subordinated Debentures was put on notice of the subordination that would apply to their indebtedness in the event of a receivership.
18. ***The Indenture.*** The terms of the Short Form Prospectus are reflected in the Indenture. Article 5 of the Indenture provides the basis upon which the Subordinated Debentures are subordinated.
19. Clause 5.1 states that the “**Debenture Liabilities shall be subordinated and postponed and subject in right of payment [...] to the prior full and final payment of all Senior Indebtedness of the Corporation [...]** and each holder of any such Debenture by his acceptance thereof, whether directly or on his behalf, agrees to and shall be bound by the provisions of this Article 5.”
20. Clause 5.2 sets the priority of payment in the event of a receivership. Clause 5.2(a) states that “**all Senior Indebtedness shall first be paid indefeasibly in full [...]**”. Clause 5.2(b) makes very clear that “**any payment or distribution of assets of [Twin Butte] [...] to which the holders of the Debentures or the Debenture Trustee on behalf of such holders would be entitled except for the provisions of this Article 5 shall be paid or delivered [...] directly to the Senior Creditors to the extent necessary to pay all Senior Indebtedness in full [...]**”.
21. Clause 5.2(c) provides that the Receiver can sell, mortgage or otherwise dispose of the Corporation’s assets in whole or in part “free and clear of all Debenture Liabilities and without the approval of the Debentureholders or the Debenture Trustee or any requirement to account to the Debenture Trustee or the Debentureholders”.
22. Clause 5.2 continues to state that “**the rights and priority of the Senior Indebtedness and the subordination pursuant hereto shall not be affected by**” a litany of circumstances ending with “**any other matter whatsoever**”.
23. Clause 5.5 confirms that no payment may be made to the Subordinated Debentureholders if the “Senior Indebtedness” is in default. In particular, clause 5.5 states that “[u]pon the maturity of any Senior Indebtedness by lapse of time, acceleration or otherwise, or any enforcement of any Senior Indebtedness, then, [...] **all such Senior Indebtedness shall first be paid in full [...] before any payment is made on account of the Debenture Liabilities**”.

24. Clause 5.5 continues to state that in the event of default with respect to any Senior Indebtedness permitting a demand for payment or acceleration, **“no payment (by purchase of Debentures or otherwise) shall be made by the Corporation with respect to the Debenture Liabilities and neither the Debenture Trustee nor the holders of Debentures shall be entitled to demand, accelerate, institute proceedings for the collection of or receive any payment or benefit on account of the Debentures after the happening of such a default or event of default [...]”**.
25. Clause 5.7 provides for the confirmation of the subordinated position of the Subordinated Debentures. Clause 5.7 contains the “Priority Mechanism” that is the basis of the *Ad Hoc* Committee’s argument that the Subordinated Debentures are not subordinate. In fact, Clause 5.7 simply provides an option that may be exercised by holders of Senior Indebtedness to confirm the subordination.
26. Clause 5.7 begins: “Each holder of Debentures by his acceptance thereof authorizes and directs the Debenture Trustee on his behalf to take such action as may be necessary or appropriate to effect the subordination as provided in this Article 5 and appoints the Debenture Trustee his attorney-in-fact for any and all such purposes”.
27. Clause 5.7 then provides that upon request of Twin Butte by a Senior Creditor (i.e. a holder of Senior Indebtedness), the Debenture Trustee “shall enter into a written agreement [...] with the Corporation and the [Senior Creditor] providing that such [Senior Creditor] are entitled to all the rights and benefits of this Article 5.”
28. Critically, the concluding line of Clause 5.7 declares: **“However, nothing herein shall impair the rights of any Senior Creditor who has not entered into such an agreement.”**
29. Clause 5.10 states: **“No right of any present or future holder of any Senior Indebtedness to enforce the subordination herein will at any time or in any way be prejudiced or impaired by any act or failure to act on the part of the Corporation or by any non-compliance by the Corporation with the terms, provisions and covenants of this Indenture [...]”**
30. The term “Senior Indebtedness”<sup>7</sup> bears the same expansive definition in the Indenture as it does in the Short Form Prospectus.

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<sup>7</sup> The Indenture defines “Senior Indebtedness” as: all obligations, liabilities and indebtedness of the Corporation which would, in accordance with GAAP, be classified upon a consolidated balance sheet of the Corporation as liabilities of the Corporation and,

31. In short, the Indenture repeatedly confirms the subordination of the Subordinated Indentures.
32. Any Subordinated Debentureholder would have had access to these subordination terms before subscribing; regardless, upon subscription the Indenture governed the Subordinated Debentureholders' recovery rights.

### III. LAW AND SUBMISSIONS

#### *Subordinate Means Subordinate*

33. The Receiver agrees with the *Ad Hoc* Committee's articulation of the principles of contract interpretation at paragraphs 23-24 of the *Ad Hoc* Brief.
34. The Receiver emphasizes that, as the Supreme Court of Canada stated, to ascertain the meaning of a contract a decision maker must read the contract 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.<sup>8</sup>
35. Applying the principles of contract interpretation to the Indenture yields one clear result: the Subordinated Debentures are subordinate.
36. As detailed above, the Subordinated Debentures are expressly subordinated to the Senior Indebtedness of Twin Butte.<sup>9</sup> This expressly includes with respect to "any distribution of the assets" of Twin Butte, including in a receivership proceeding,<sup>10</sup> and the subordination is effective whether or not the Senior Indebtedness is secured.<sup>11</sup>

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whether or not so classified, shall include (without duplication): (a) indebtedness of the Corporation for borrowed money; (b) obligations of the Corporation evidenced by bonds, debentures, notes or other similar instruments; (c) obligations of the corporation arising pursuant or in relation to bankers' acceptances, letters of credit, letters of guarantee, performance bonds and surety bonds (including payment and reimbursement obligations in respect thereof) or indemnities issued in connection therewith; (d) obligations of the Corporation under any swap, hedging or other similar contracts or arrangements; (e) obligations of the Corporation under Guarantees, indemnities, assurances, legally binding comfort letters or other contingent obligations relating to the Senior Indebtedness or other obligations of any other Person which would otherwise constitute Senior Indebtedness within the meaning of this definition; (f) all indebtedness of the Corporation representing the deferred purchase price of any property including, without limitation, purchase money mortgages; (g) accounts payable to trade creditors; (h) all renewals, extensions and refinancing of any of the foregoing; (i) all declared but unpaid dividends or distributions; and (j) all costs and expenses incurred by or on behalf of any Senior Creditor in enforcing payment or collection of any such Senior Indebtedness, including enforcing any security interest securing the same. "Senior Indebtedness" shall not include any indebtedness that would otherwise be Senior Indebtedness if it is expressly stated to be subordinate to or rank *pari passu* with the Debentures.

<sup>8</sup> *Sattva Capital Corp. v Creston Moly Corp.*, [2014] 2 SCR 633, 2014 SCC 53, at para 47. [Authorities to *Ad Hoc* Brief, Tab 8.]

<sup>9</sup> Indenture at 5.1.

<sup>10</sup> Indenture at 5.2.

<sup>11</sup> Indenture at 5.2(i).

37. In short, the Indenture contains an unequivocal subordination of the priority of the Subordinated Debentures to virtually all other unsecured debt of Twin Butte (i.e. all indebtedness captured by the defined term “Senior Indebtedness”<sup>12</sup>).
38. The terms of the Indenture could not be more clear.
39. The *Ad Hoc* Committee’s attempts to complicate and seek inconsistency within Article 5 of the Indenture should not be countenanced. The *Ad Hoc* Brief should be read in light of the Subordinated Debentureholders’ (unsurprising) interest in maximizing their own recovery regardless of the impact on other creditors.
40. But the Receiver’s obligation is to maximize recovery for all creditors, and to treat them in a fair and even-handed manner in accordance with the applicable contracts and law governing them. In this regard, given the Indenture, the Receiver’s judgment as to the fair approach for making distributions is to simply comply with the subordination provisions contained in the Indenture.
41. Accordingly, pursuant to its broad authority under the Receivership Order granted by this Honourable Court, the Receiver seeks the Indenture’s interpretation and application on its straightforward terms as drafted and clearly intended. As Twin Butte is a party to the Indenture, the *Ad Hoc* Committee’s arguments about privity of contract have no application to the Receiver’s enforcement of the Indenture terms.
42. To be clear, the *Ad Hoc* Committee does not deny that subordination agreements may be validly upheld. They only state that they are strictly interpreted and that they must be clear and unequivocal to be enforceable, and the Indenture fails to meet these requirements.<sup>13</sup>
43. The Receiver submits that even by the standard of strict interpretation, the Indenture is crystal clear that the Subordinated Debentureholders’ indebtedness is subordinated to the Senior Indebtedness. The Indenture repeatedly states as much. Nowhere in the Indenture are there any exceptions or suggestions to the contrary.
44. Indeed, this is part of the bargain that the Subordinated Debentureholders struck upon subscription: they get an advantageous interest rate and debt-to-equity conversion right not available to other creditors and in exchange they pay the agreed market price for a

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<sup>12</sup> Indenture definitions; see also footnote 7 herein.

<sup>13</sup> *Ad Hoc* Brief, paras 26-30.



Subordinated Debenture and contractually agree to subordinate the priority of their repayment in a receivership.

45. The certainty of subordination is precisely the risk the Subordinated Debentureholders bargained for. Now that the risk has become reality it does not lie in the mouth of the Subordinated Debentureholders to escape it; certainly they have accepted the upside benefits of the Indenture without hesitation had Twin Butte's fortunes been different, so why should they be able to evade the agreed downside?

### ***Subordination Agreements are Routinely Upheld***

46. Commercial courts across Canada have upheld subordination agreements in insolvency proceedings:

- a) In *Bank of Montreal v. Dynex Petroleum*,<sup>14</sup> a decision of the Alberta Court of Queen's Bench, this Honourable Court addressed whether a distribution in bankruptcy should treat Bank of Montreal (**BMO**) as a secured creditor (given its security in Dynex's assets) or give effect to BMO's contractual subordination of its rights to those of the holders of overriding royalties.

After finding that the holders of the royalties had become unsecured creditors, Justice Rooke nevertheless concluded that BMO's subordination of its interest to them was effective, and survived the bankruptcy of the debtor, even though BMO was a secured creditor. The result was that BMO was entitled to realize on its security, but the *proceeds of that realization were deemed to be held in trust for the royalty-holders*. That is, the distribution priorities under the *Bankruptcy and Insolvency Act*<sup>15</sup> were unaffected, but the subordination agreement as between the creditors could be given effect through the imposition of a trust.

- b) Justice Rooke's reasoning was followed by Justice Farley of the Ontario Commercial List in *Air Canada, Re*, a decision involving the treatment of competing unsecured claims under a *Companies' Creditors Arrangement Act*<sup>16</sup> plan. In that case, Justice Farley said that in principle there is no reason why unsecured creditors cannot reach

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<sup>14</sup> *Bank of Montreal v Dynex Petroleum*, 145 DLR (4th) 499, at paras 57, 62, 65, 68, 73 (overturned on appeal on other grounds: 1999 ABCA 363; 2002 SCC 7) [Receiver's Authorities, TAB 1].

<sup>15</sup> RSC, 1985, c B-3 (*BIA*).

<sup>16</sup> RSC, 1985, c C-36.

agreement as between each other with respect to the priority of their claims, including in the context of bankruptcy<sup>17</sup>.

Specifically, Justice Farley noted that a distribution in liquidation can be made in accordance with an agreement to subordinate, provided that this does not adversely affect the rights of other creditors who are entitled to participate *pari passu* in any distributions. His Honour cited with approval the below passage from a scholarly paper:

At the conclusion of the bankruptcy proceedings, a dividend is allocated to all unsecured creditors, including the subordinated creditor, on a *pro rata* basis. The dividend allocated to the subordinated creditor is paid over to the senior creditor, to the extent of its claim, with the subordinated creditor retaining the remainder of the dividend if the senior creditor is paid in full. This process neither affects the amount of claims against the debtor nor the dividend paid to unsecured creditors.<sup>18</sup>

- c) In *Rico Enterprises Ltd., Re*, the British Columbia Bankruptcy Court likewise upheld a subordination agreement, emphasizing that a trustee in bankruptcy can and should give effect to a particular subordination agreement as between unsecured creditors when dealing with the bankrupt's property:

[...] From a purist's point of view, it could be said that the trustee should make the distribution in compliance with s. 139 [of the *BIA*, as it then was] and leave it to the parties to the subordination agreement to deal with the priorities between them. But if the subordinating creditor concedes that it has subordinated its claim to the claim of a lender which falls within s. 139, I see no reason why the trustee could not pay the share of the subordinating creditor directly to the s. 139 lender as if the subordinating creditor had assigned its claim to the lender.<sup>19</sup>

47. As in these cases, this Honourable Court can give effect to the subordination provided for in the Indenture without affecting the rights of other unsecured creditors to their rateable dividend. Rather than creating a "new class" of creditors by subordinating the Subordinated Debentures to all of Twin Butte's unsecured debt, the Indenture can be given effect by the distribution of *pro rata* dividends in the usual course, and an assignment or transfer of the share attributable to the Subordinated Debentures to the Senior Indebtedness until all claims contemplated in the Indenture as having priority over the Subordinated Debentures are paid in full.

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<sup>17</sup> *Air Canada, Re*, [2004] OJ No 1909, 2004 CarswellOnt 1842, at para 10 [Receiver's Authorities, TAB 2].

<sup>18</sup> *Air Canada, Re*, [2004] OJ No 1909, 2004 CarswellOnt 1842, at para 10 [Receiver's Authorities, TAB 2].

<sup>19</sup> *Rico Enterprises Ltd., Re*, [1994] BCI No 3019, 1994 CarswellBC 608, at para 36 [Receiver's Authorities, TAB 3].

48. Such a result would be practical and just, in that it would uphold the contractual bargain struck by the Subordinated Debentureholders and Twin Butte before receivership, and upon which the Senior Creditors of Twin Butte now rely for their priority position.

***Subordinated Debentureholders' "Priority Mechanism" Arguments Fail***

49. The *Ad Hoc* Committee's first argument is that the Indenture is not clear or unequivocal enough to be upheld. The plain words of the Indenture undermine that position.
50. The *Ad Hoc* Committee's secondary argument seems to be that even if the Indenture is clear enough to be enforceable, it is not triggered in this case.
51. In particular, the *Ad Hoc* Committee suggests that because no Senior Creditor requested a confirmatory agreement from Twin Butte of their status as Senior Indebtedness under clause 5.7 of the Indenture, the Subordinated Debentures are not subordinated.<sup>20</sup> This argument also fails.
52. As noted above, the last sentence of clause 5.7 states: "**However, nothing herein shall impair the rights of any Senior Creditor who has not entered into such an agreement.**"<sup>21</sup> This means that clause 5.7 is not mandatory. It simply created an option for those Senior Creditors wanting extra comfort. That no Senior Creditors availed themselves of the option does not mean they lost the benefit of the subordination provisions; they did not even lose the option, for they can still exercise it today should they choose to.
53. Nowhere in the Indenture does it say that the failure to confirm the subordination results in the extinguishment of the subordination.
54. The *Ad Hoc* Committee believes their construal of clause 5.7 "gives effect to the plain and ordinary meaning of the words used in [clause] 5.7" and is "commercially reasonable" on the flawed assumption that because no Senior Creditor requested a confirmatory agreement, no Senior Creditor relied upon the subordination provisions in the Indenture and therefore there will be no injustice in not enforcing the subordination. There is no evidence for this whatsoever.

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<sup>20</sup> The *Ad Hoc* Brief first raises this argument at paragraphs 68-77 in connection with their broader argument that Senior Creditors have no privity of contract and clause 5.7 was their inroad to achieving such privity. The *Ad Hoc* Brief rehashes the argument at paragraphs 90-104 but with a slight different spin: only Senior Creditors who asked for a confirmatory agreement get to rely upon the subordination provisions, and because no Senior Creditor asked for a confirmatory agreement to "clarify its position" no one gets to rely upon the subordination provisions.

<sup>21</sup> The "rights" referred to are in respect of subordinating the indebtedness of the Subordinated Debentures to the Senior Creditors' own indebtedness.

55. It is just as likely, and certainly more reasonable given the last sentence of clause 5.7, that Senior Creditors read the subordination provisions of the Indenture and were satisfied that without requiring any proactive steps those subordination provisions would apply, because that is what the provisions repeatedly say. To reiterate, **“the rights and priority of the Senior Indebtedness and the subordination pursuant hereto shall not be affected by [...] any other matter whatsoever”<sup>22</sup>.**

***Contingent “Debenture Damages Claim” is Subordinated or Disallowed***

56. The *Ad Hoc* Committee has submitted to the Receiver a proof of claim in the formal claims process for two separate amounts and on two separate bases.
57. The first claim is “a debt claim as against Twin Butte based on the principal and accrued interest owed under the [Subordinated] Debentures”<sup>23</sup> in the amount of \$92,220,726.52 (the **Subordinated Debt Claim**).
58. The second claim is for damages “flowing from Article 2.4(j)”<sup>24</sup> of the Indenture in the amount of \$92,700,125.07 (the **Subordinated Damages Claim**). Clause 2.4(j) provides that following the occurrence of a “Change of Control”, such as the sale of Twin Butte’s assets, Twin Butte shall be obligated to offer to purchase all outstanding Subordinated Debentures on certain terms. The *Ad Hoc* Committee alleges that the Court-approved sale of all of Twin Butte’s assets by the Receiver triggered Twin Butte’s (the Receiver’s) obligation under clause 2.4(j) to offer to purchase the outstanding Subordinated Debentures, and the Receiver’s failure to make such offer breached the Indenture giving rise to a claim for damages.
59. It is unclear from the proof of claim whether the Subordinated Debentureholders’ total claim amount is the sum of the Subordinated Debt Claim and the Subordinated Damages Claim or whether they are seeking payment of only one claim or the other and if so, on what basis.
60. As at the date of this Brief, the Receiver has not yet accepted or disallowed either of these claims but can provisionally advise the Court that it anticipates it will allow the Subordinated Debt Claim<sup>25</sup> but disallow the Subordinated Damages Claim on the basis that:

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<sup>22</sup> Indenture at 5.2.

<sup>23</sup> *Ad Hoc* Brief at para 78.

<sup>24</sup> *Ibid.*

<sup>25</sup> While giving effect to the subordination of the Subordinated Debt Claim to the Senior Indebtedness in accordance with Article 5 of the Indenture including, in particular and without limitation, clause 5.5 which confirms that upon maturity of any Senior Indebtedness

- a) following substantial payment of the Subordinated Debt Claim there will be no provable damages under the Subordinated Damages Claim;
  - b) the claim is based on the speculative or contingent foundation of the Receiver not offering to purchase the Subordinated Debentures following the Court-sanctioned sale of Twin Butte's assets in receivership, and the Receiver's view is that clause 5.2(c), which permitted the sale of Twin Butte's assets by the Receiver "free and clear of all Debenture Liabilities", barred any claim under clause 2.4(j);
  - c) to permit payment of the Subordinated Debt Claim *and* the Subordinated Damages Claim would result in "double-dipping" and a \$92 million windfall, which the Receiver will not permit unless ordered by the Court; and
  - d) the Subordinated Debentureholders cannot purport to enhance or "bootstrap" their Subordinated Debt Claim by alleging a breach of contract relating to the subordinated debt so as to enhance their rights of recovery.
61. In any case, the *Ad Hoc* Committee states that even if the Indenture is upheld on its terms and the subordination provisions are enforced, they would only subordinate the Subordinated Debt Claim but not the Subordinated Damages Claim. The *Ad Hoc* Committee says the Subordinated Damages Claim would rank *pari passu* with the other unsecured claims. (This reasoning suggests that the *Ad Hoc* Committee expects payment of the Subordinated Damages Claim on a *pari passu* basis and then another payment of the Subordinated Debt Claim on a subordinated basis.)
62. The basis for their belief lies in the wording of clause 5.2 of the Indenture and the use of "Debenture Liabilities" in clause 5.2(c) but not in clause 5.2(a). They concede that the broadly defined "Debenture Liabilities" captures both the Subordinated Debt Claim and the Subordinated Damages Claim.
63. As noted above, clause 5.2 sets the priority of payment in the event of a receivership. Clause 5.2(a) says that Senior Indebtedness is paid out first, "indefeasibly in full" before "any other liability or obligation in respect of the indebtedness evidenced by the Debentures". The *Ad Hoc* Committee says this means that only the Subordinated Debt Claim is subordinate, because it falls within the meaning of "indebtedness evidenced by the Debentures", and

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by lapse of time, acceleration or otherwise, or any enforcement of any Senior Indebtedness, all such Senior Indebtedness shall first be paid in full before any payment is made on account of the Debenture Liabilities.

because the term “Debenture Liabilities<sup>26</sup>” is not used in the clause, meaning that the drafters only intended to subordinate a subset of Debenture Liabilities, not all Debenture Liabilities.

64. Clause 5.2(c) simply says that the Receiver may sell Twin Butte’s assets “free and clear of all Debenture Liabilities and without the approval of the Debentureholders or the Debenture Trustee or any requirement to account to the Debenture Trustee or the Debentureholders.”
65. To reiterate, because the term “Debenture Liabilities” is used in clause 5.2(c), but not in clause 5.2(a), the *Ad Hoc* Committee thinks that the subordination is only effective over the Subordinated Debt Claim, while the Receiver could sell Twin Butte’s assets free and clear of both the Subordinated Debt Claim and what was then only a hypothetical Subordinated Damages Claim.
66. A reasonable construal of clause 5.2 suggests otherwise. Clause 5.2(a) says that the Senior Indebtedness is paid first in a receivership. This priority aligns with every other aspect of the Indenture: the Subordinated Debentures are subordinate. Regardless, the words “indebtedness evidenced by the Debentures” are broad enough to capture the Subordinated Damages Claim, insofar as that claim only arises in connection with the debentures and becomes a debt of the company if proven.
67. This understanding of clause 5.2 is supported by Article 5 as a whole, including clause 5.5 in particular, which confirms that upon maturity of any Senior Indebtedness by lapse of time, acceleration or otherwise, or any enforcement of any Senior Indebtedness, “**all such Senior Indebtedness shall first be paid in full [...] before any payment is made on account of the Debenture Liabilities**”. Accordingly, both the Subordinated Debt Claim and Subordinated Damages Claim are subordinate.
68. Moreover, clause 5.2(c) suggests that the change of control provision under clause 2.4(j) is inapplicable in a receivership sale, thereby barring any Subordinated Damages Claim. This is reflected in the Receiver’s ability to sell Twin Butte’s assets “**free and clear of all Debenture Liabilities**” and without having to “**account to the Debenture Trustee or the Debentureholders**”. This makes sense given that in a receivership sale the purpose is to liquidate the company to repay creditors, not to create a new \$92 million liability that would dwarf the recovery of existing unsecured creditors.

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<sup>26</sup> Defined in the Indenture as: “the indebtedness, liabilities and obligations of the Corporation under Debentures issued under this Indenture, including on account of principal, interest or otherwise but excluding the issuance of Common Shares upon any conversion pursuant to Article 6, upon any redemption pursuant to Article 4, or at maturity pursuant to Article 4.”

69. Read as a whole, clause 5.2 dictates that in a receivership proceeding the Senior Indebtedness is paid first, and that the Receiver may sell Twin Butte's assets without requiring the Subordinated Debentureholders' approval and without fear of incurring new liability by effecting such sale.

### ***No Elevating the Subordinated Debt Claim***

70. This Court has scrutinized attempts to re-characterize claims made by subordinate equity holders in an insolvency claims process to determine whether they are in substance claims by shareholders for the return of equity that must rank behind the claims of the debtor's unsecured creditors: *Blue Range Resource Corp., Re*<sup>27</sup> and *National Bank of Canada v. Merit Energy Ltd.*<sup>28</sup>.
71. Underlying these decisions is the principle that a party cannot try to elevate the priority of their claim by characterizing it as a contract breach in a way to subvert the applicable priority scheme.
72. The Subordinated Damages Claim seeks to do just that. It is the Subordinated Debt Claim reframed as a breach of contract so as to evade the agreed upon subordination under the Indenture. This is one more reason why attempting to advance a subordinated claim as a breach of contract should be disallowed and not permitted to enhance the Subordinated Debentureholders' priority contrary to the Indenture.

### ***Subordination Mechanism***

73. In the Indenture the subordination agreement is clear and Twin Butte has the right to distribute payment in respect of the Senior Indebtedness in priority in accordance with the negotiated subordination terms.
74. Alternatively, the Receiver agrees with the *Ad Hoc* Committee's suggestion at paragraphs 105-106 of their brief that the subordination can be given effect through the formula used by Justice Farley in the *Air Canada* case:

[A] dividend is allocated to all unsecured creditors, including the subordinated creditor, on a *pro rata* basis. The dividend allocated to the subordinated creditor is paid over to the senior creditor, to the extent of its claim, with the subordinated creditor retaining the remainder of the dividend if the senior creditor is paid in full. This

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<sup>27</sup> 2000 ABQB 4 at paras 14, 17, 25, 27, and 33 [Receiver's Authorities, TAB 4].

<sup>28</sup> 2001 ABQB 583 at paras 48-55 [Receiver's Authorities, TAB 5].

process neither affects the amount of claims against the debtor nor the dividend paid to the unsecured creditors.

**IV. CONCLUSION AND RELIEF SOUGHT**

75. For all the reasons stated herein, the Receiver respectfully requests the Court's confirmation that the holders of the Subordinated Debentures are subordinate to the general class of unsecured creditors of Twin Butte for the purposes of distributions or dividend payments made by the Receiver.

ALL OF WHICH IS RESPECTFULLY SUBMITTED THIS 20<sup>th</sup> DAY OF June, 2017.



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Howard A. Gorman, Q.C.  
Norton Rose Fulbright Canada LLP



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Aditya M. Badami  
Norton Rose Fulbright Canada LLP



## TABLE OF AUTHORITIES

<b>Case / Paragraph References</b>	<b>Tab</b>
<i>Bank of Montreal v Dynex Petroleum</i> , 145 DLR (4th) 499, at paras 57, 62, 65, 68, 73	1
<i>Air Canada, Re</i> , [2004] OJ No 1909, 2004 CarswellOnt 1842, at para 10	2
<i>Rico Enterprises Ltd., Re</i> , [1994] BCJ No 3019, 1994 CarswellBC 608, at para 36	3
<i>Blue Range Resource Corp. Re</i> , 2000 ABQB 4 at paras 14, 17, 25, 27, and 33	4
<i>National Bank of Canada v. Merit Energy Ltd.</i> , 2001 ABQB 583 at paras 48-55	5

## APPENDIX "A"

### Excerpts from Receivership Order Dated September 1, 2016

[...]

#### RECEIVER'S POWERS

3. The Receiver is hereby empowered and authorized, but not obligated, to act at once in respect of the Property and, without in any way limiting the generality of the foregoing, the Receiver is hereby expressly empowered and authorized to do any of the following where the Receiver considers it necessary or desirable:

[...]

(c) to manage, operate and carry on the business of the Debtor, including the powers to enter into any agreements, incur any obligations in the ordinary course of business, cease to carry on all or any part other [sic] business, or cease to perform any contracts of the Debtor;

[...]

(u) to take any steps reasonably incidental to the exercise of these powers or the performance of any statutory obligations; [...]