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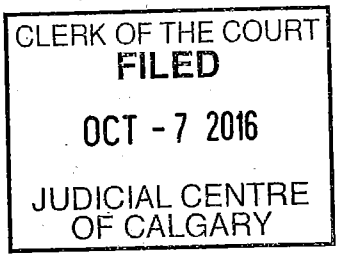

COURT FILE NUMBER	1601 - 12571
COURT	COURT OF QUEEN'S BENCH OF ALBERTA
JUDICIAL CENTRE	CALGARY
	IN THE MATTER OF THE *COMPANIES' CREDITORS ARRANGEMENT ACT*, RSC 1985, c C-36, as amended AND IN THE MATTER OF A PLAN OF COMPROMISE OR ARRANGEMENT OF LIGHTSTREAM RESOURCES LTD, 1863359 ALBERTA LTD, LTS RESOURCES PARTNERSHIP, 1863360 ALBERTA LTD AND BAKKEN RESOURCES PARTNERSHIP
APPLICANTS	LIGHTSTREAM RESOURCES LTD, 1863359 ALBERTA LTD AND 1863360 ALBERTA LTD
PARTIES IN INTEREST	LTS RESOURCES PARTNERSHIP AND BAKKEN RESOURCES PARTNERSHIP
DOCUMENT	**REPLY BRIEF OF THE APPLICANTS (COMEBACK HEARING)**
ADDRESS FOR SERVICE AND CONTACT INFORMATION OF PARTY FILING THIS DOCUMENT	**BLAKE, CASSELS & GRAYDON LLP** Barristers and Solicitors 3500 Bankers Hall East 855 – 2nd Street SW Calgary, Alberta T2P 4J8 Attention: Kelly Bourassa / Richard Bell Telephone No.: 403-260-9697/9656 Email: kelly.bourassa@blakes.com **/richard.bell@blakes.com** Fax No.: 403-260-9700 File: 89691/8 Attention: Milly Chow / Michael Barrack Telephone No.: 416-863-2594/ 5280 Email: **milly.chow@blakes.com** / **michael.barrack@blakes.com** Fax No.: 416-863-2653

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I. INTRODUCTION

1. This brief is submitted on behalf of the Lightstream Group in response to the brief of argument dated October 6, 2016 (the "**Plaintiffs' Second Brief**") from two groups of holders of Unsecured Notes, Mudrick Capital Management ("**Mudrick**"), FrontFour Capital Corp. and FrontFour Capital Group LLC (together, "**FrontFour**", and collectively with Mudrick, the "**Plaintiffs**"). The Plaintiffs, among other things, opposed certain relief sought in the initial order (the "**Initial Order**") granted pursuant to the *Companies' Creditor Arrangement Act*, RSC 1985, c C-36, as amended (the "**CCAA**") on September 26, 2016, by the Honourable Justice A.D. Macleod.

2. The Lightstream Group previously provided this Honourable Court with a bench brief in support of the Initial Order (the "**Initial Order Brief**"), which outlines the legislation and jurisprudence that is relevant to the relief granted in the Initial Order and a bench brief in anticipation of the comeback hearing on October 11, 2016 (the "**Comeback Brief**"), which responds to the Plaintiffs' September 26, 2016 bench brief. The purpose of this brief is to respond to certain statements made in the Plaintiffs' Second Brief. This brief should be read in conjunction with the Initial Order Brief and the Comeback Brief. Capitalized terms used and not otherwise defined herein will have the meaning given to them in the Initial Order Brief or the Comeback Brief.

II. FACTS

3. A summary of the facts relevant to the application for the Initial Order is set out in the Initial Order Brief and the Comeback Brief.

III. LAW AND ARGUMENT

4. The Lightstream Group's response to the Plaintiffs' Second Brief can be encapsulated in two themes: (1) courts have upheld the supremacy of the business judgment rule in CCAA proceedings and the Lightstream Group submits that this Court should grant deference to the business judgment of the Lightstream Group's highly qualified management and board of directors, whose good faith decisions and actions were taken, and continue to be taken, with advice from its professional advisors and the Court-appointed Monitor, and are supported by the First Lien Lenders and its advisors and the *Ad Hoc* Committee of Secured Noteholders and

its advisors; and (2) the Plaintiffs are two unsecured creditors, who in the current environment are expected to be out-of-the-money, with the result that their significant motivation is to disrupt these proceedings, at the expense of the Lightstream Group and its other stakeholders, who are forced to bear all of the risk of the disruption the Plaintiffs are causing, including continued funding of these proceedings and the continued erosion of secured creditors collateral.

A. Directors and Executive Officers

5. As set out in the Initial Order Brief, LTS is the parent of the Lightstream Group.[1] The officers of LTS are listed in the Affidavit of Peter D. Scott sworn September 21, 2016 (the "**Scott Affidavit**") at paragraph 13. The executive team of LTS consists of extremely qualified individuals with significant professional and academic achievements and an exceptional amount of experience in the oil and gas business, as well as other industries.[2] Specifically, a few of the most senior members of LTS' management team include:

(a) John D. Wright, President and Chief Executive Officer, who has been CEO of LTS since its inception in 2009, began his full time career in the oil industry after he graduated from the University of Alberta in 1981 with a Bachelor of Science degree in Petroleum Engineering, was the President and CEO of Petrobank Energy and Resources Ltd., the President and Chief Executive Officer of Pacalta Resources Ltd., Executive Vice President and Chief Operating Officer of Morgan Hydrocarbons Inc., and Vice President Production of Morgan Hydrocarbons Inc. and is also a Chartered Financial Analyst charterholder;

(b) Peter D. Scott, Senior Vice President and Chief Financial Officer, who has been CFO at LTS since May 2010, started his career in the oil and gas industry in 1983 with Amoco Canada Petroleum Company Ltd., was a founding member of the executive team as Vice President Finance and CFO at Rock Energy Inc., VP Finance and CFO at Iteration Energy, CFO and Director of Absolute Software Corporation, Vice President and CFO at Beau

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[1] Scott Affidavit at para 8.

[2] Affidavit of Emily van de Pol, sworn October 7, 2016, at Exhibit A (the "**Van de Pol Affidavit**").

Canada Exploration Ltd., and Treasurer, Finance Manager and Financial Analyst at Crestar Energy Inc. including 17 years as CFO of oil and gas exploration and production companies;[3] and

(c) Doreen Scheidt, Vice President and Controller, who has over 30 years of industry experience in a variety of management roles including financial accounting, operations accounting, oil & gas receiverships and oil & gas accounting systems implementation, and has been the Corporate Controller of Lightstream since the company's inception in 2009.

6. LTS' board of directors is also comprised of highly qualified and accomplished individuals with extensive experience in capital markets, finance and business with both private and publicly traded companies.[4] Members of the board of directors of LTS include, among others:

(a) Kenneth McKinnon, Chairman, who has practiced as a corporate commercial and securities lawyer for over 28 years, has held the position of Vice President Legal and General Counsel of Critical Mass Inc. since March 2000, holds volunteer Board positions with the University of Calgary and Alberta Innovate Technology Futures, has a Bachelor of Commerce degree from the University of Calgary majoring in accounting in 1980, an LLB from Queen's University and was admitted to the Alberta Law Society and the Law Society of England and Wales and was appointed a Queen's Counsel in 2012 and holds an ICD.D designation, as a certified corporate director;

(b) Martin Hislop, who is a Chartered Accountant and retired businessman with over 30 years' experience in all aspects of financing and managing private and listed oil and gas companies, partnerships and trusts, including acting as founder and former CEO of APF Energy Trust before it was bought out for approximately one billion dollars in June 2005 and President and CEO of Lakewood Energy Inc., a TSX listed oil and gas company, which was created

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[3] Scott Transcript at 7, line 24, 8, line 5. [**Comeback Brief, TAB 2**]

[4] Van der Pol Affidavit at Exhibit B.

as a result of the merger of 10 limited partnership drilling funds he created beginning in 1986; and

(c) W. Brett Wilson, who has more than 25 years of experience in investment banking with extensive knowledge of Canada's resource sectors as well as a substantial amount of business experience including co-founding FirstEnergy Capital Corp. in 1993, a leading Canadian brokerage firm that provides investment-banking services to Canada's energy-based industries, and is currently Chairman of Prairie Merchant Corporation, a private merchant bank focused on business opportunities in the energy, agriculture, real estate, sports, and entertainment industries.

B. The Business Judgment Rule Applies

7. Without providing any substantiation beyond the Plaintiffs' self-serving assertions, the Plaintiffs' Second Brief is a compilation of statements that question the business judgment of the officers and directors of the Lightstream Group and the manner in which they propose to conduct these CCAA proceedings. In particular, the Plaintiffs' Second Brief, without any expert evidence: (i) self-proclaims that the Sale Process is "truncated" in the face of the expert opinions of the Sale Advisor and the Monitor stating that the timelines in the Sale Process are reasonable and sufficient; and (ii) makes accusations that the officers and directors of the Lightstream Group have abdicated their duties to act in the best interests of the Lightstream Group.

(i) The Business Judgment Rule

8. Canadian courts have developed a rule of deference upon the review of the business decisions of directors and officers of a corporation pursuant to the "business judgment rule." If a director or officer has exercised the care, diligence, and skill that a reasonably prudent person would have exercised in comparable circumstances, and did so in a manner that was procedurally reasonable and appropriate, a court will give deference to the director's or officer's exercise of business judgment.[5]

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[5] *People's Department Stores Ltd (1992) Inc, Re*, 2004 SCC 68 at paras 64-65 [*People's*]. **[Plaintiffs' Second Brief, TAB 5]**

9. The business judgment rule does not hold directors or officers to the unattainable standard of perfection. The Court will look to see if the directors made a reasonable decision, not a perfect decision. If the decision falls within a range of reasonable alternatives, the Court ought not to substitute its own opinion for that of the board or management.[6]

10. The business judgment rule reflects the reality that directors, who are mandated to manage the corporation's business and affairs, are often better suited to determine what is in the best interests of the corporation. This applies to decisions on stakeholders' interests, as much as any other decision before the board of directors.[7]

11. The business judgment rule has been given even more weight in CCAA proceedings where the activities of a debtor company are reviewed and approved by highly qualified professionals with great experience in restructuring and are done in a consultative process.[8]

(ii) The Lightstream Group continues to act in the Best Interests of the Lightstream Group

12. The Plaintiffs suggest that the Lightstream Group has not fulfilled its obligation to consider all restructuring options. This allegation is not supported by any of the evidence before this Court.

13. The Plaintiffs' Second Brief alleges that management's failure to act in the best interests of the Lightstream Group is supported by the fact that management is not attempting to negotiate a restructuring or recapitalization plan. However, this allegation ignores the evidence that the Lightstream Group has pursued all possible restructuring avenues since December 2014, including spending over two months attempting to negotiate a consensual plan of arrangement that would have seen a debt-for-equity exchange and allowed the Lightstream Group to continue as a going concern.[9] Given the already exhaustive attempts by the Lightstream Group to pursue other restructuring options outside of these CCAA proceedings, and the frustration of those efforts by the Plaintiffs, the Lightstream Group

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[6] *People's* at paras 64-65 [**Plaintiffs' Second Brief, TAB 5**]; *Pente Investment Management Ltd v Schneider* Corp, [1998] OJ No 4142 at para 36. [**TAB 1**]

[7] *BCE Inc, Re*, 2008 SCC 69 at para 40. [**Plaintiffs' Second Brief, TAB 6**]

[8] *Essar Steel Algoma Inc, Re,* 2016 ONSC 3205 at para 29 [**Comeback Brief, TAB 5**]; *US Steel Canada Inc, Re,* 2016 ONSC 5215 at para 22. [**Comeback Brief, TAB 6**]

[9] Scott Affidavit at paras 80-84.

determined the only logical remaining option was to seek protection under the CCAA and seek the approval of the Sale Procedures.[10]

14. The evidence is that the Lightstream Group is pursuing the Sale Procedures after exploring every other avenue of restructuring. This business decision followed an exhaustive negotiation process with creditors, including the Plaintiffs, and after consulting advisors, the board of directors (who consulted its own independent legal and financial advisors) and the Monitor. These efforts include the Lightstream Group's extensive negotiations to obtain the Replacement Credit Facility under the Commitment Letter for a restructuring within the Arrangement Proceedings or these CCAA proceedings. The efforts to secure the Replacement Credit Facility were tireless as is apparent from the Lightstream Group's continued inability through July and into August to secure the Replacement Credit Facility.[11] The evidence clearly indicates that the directors and management have been continuously engaged in ensuring the best possible outcome for the Lightstream Group and its stakeholders as a whole in the circumstances. The Plaintiffs' suggestion that the Lightstream Group is "forced" to pursue the Sale Procedures is unsupported and simply incorrect.[12]

15. The Sale Procedures and the timelines set out therein were prepared in consultation with the Sale Advisor, who has significant experience in marketing Canadian oil and gas assets such as those of the Lightstream Group.[13] The Lightstream Group, the Sale Advisor and the Monitor took into consideration a range of factors with regard to the timeline for the Sale Procedures, including the fact that the assets had already been marketed for three months (and some assets for much longer).[14] The Monitor is of the view the Sale Procedures "provide parties that, to-date, have not been actively engaged in the process sufficient time to participate in the process."[15] The Plaintiffs' assertions of the Sale Procedures being anything other than reasonable in the circumstances are completely unsupported by any evidence from the Plaintiffs and are contrary to the professional opinions of the Sale Advisor and the Monitor.

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[10] Scott Transcript at 75, lines 14-17. **[Comeback Brief, TAB 2]**

[11] See Bench Brief of the Administration Agent at paras 18-21 and Tabs 2 and 3 thereto.

[12] Plaintiffs' Second Brief at para 2.

[13] Monitor's First Report at Appendix A.

[14] Proposed Monitor's Report at para79; Monitor's First Report at Appendix A.

[15] Proposed Monitor's Report at para79.

16. While the Secured Noteholder Credit Bid has, in fact, been confirmed, [16] management continues to act in the best interests of the Lightstream Group by diligently carrying on negotiations to finalize a definitive asset purchase agreement having regard to the best interests of its stakeholders, as a whole. The Plaintiffs criticize the Lightstream Group for allegedly not considering all restructuring alternatives and, at the same time, criticize the Lightstream Group that it has not yet fully negotiated a definitive asset purchase agreement with the *Ad Hoc* Committee of Secured Noteholders. Prior to September 16, 2016 and the failure to enter into a settlement of the Actions with the Plaintiffs, the officers and directors of Lightstream were focused on completing a restructuring through the Arrangement Proceedings. It was only after it became evident that the Arrangement Proceedings would fail that the Lightstream Group was required to advance the CCAA proceedings as a backstop together with the Secured Noteholder Credit Bid that it had negotiated as part of the Support Agreement.

17. Management's and the board's good faith is also demonstrated by the Lightstream Group's willingness to consider other plans, offers or solutions if they ultimately come forward.[17] To date, no other party, including the Plaintiffs, have submitted any plan, offer or solution to restructure or refinance the Lightstream Group. To suggest at this stage that senior creditors should continue to wait for an even longer period of time[18] in the hope that market conditions improve, including commodity prices and access to debt and equity capital markets, is not practical, not based in law and most definitely not in the best interests of the Lightstream Group or its stakeholders as a whole.

18. The Plaintiffs, representing two of many unsecured creditors, are asking this Court to reject a going concern sale process that has effectively been underway for over three months, is supported by the Lightstream Group's management, board of directors, the Monitor and secured creditors, who have all been working diligently to restructure the Lightstream Group for quite some time. In cases such as this, "the court should be reluctant to substitute its own opinion for that of the directors where the business decision was made in a reasonable and

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[16] Supplemental Affidavit of Peter D. Scott, sworn September 23, 2016, at Exhibit "A".

[17] Scott Transcript at 68, lines 1-22. **[Comeback Brief, TAB 2]**

[18] Scott Affidavit at para 55.

informed reliance on the advice of financial and legal advisors appropriately retained and consulted in the circumstances".[19]

C. The Plaintiffs offer no Solutions or Economic Commitment

19. The Plaintiffs' Second Brief speculates that, with the benefit of more time and increased spending, alternative restructuring transactions *could* be found, which *may* unlock more value than would be obtained through the Sale Procedures. There is no evidence supporting the Plaintiffs' assertion that more time and increased spending will benefit the Lightstream Group. The Plaintiffs offer no economic commitment of their own, which leaves the secured creditors and other stakeholders to bear all of the risk, including continued funding of these proceedings (through the use of secured creditors' cash collateral), continued erosion of their collateral, and uncertainty to employees and contractual counterparties surrounding the future of the Lightstream Group.

20. The Plaintiffs' Second Brief suggests that the Lightstream Group should activate plans to make certain capital expenditures to increase asset value. The Plaintiffs completely ignore the equally probable alternative outcome, being that drilling programs may also decrease value depending on the result of the well compared to the estimated value of the well.[20] In addition, pursuing a drilling program while undergoing insolvency proceedings is likely to result in higher costs from service providers making it unreasonable and irresponsible to commence a capital expenditure program at this time.

21. To fund the recommended drilling program, the Plaintiffs suggest the Lightstream Group seek super-priority debtor-in-possession financing.[21] The Plaintiffs fail to recognize that any debtor-in-possession financing is likely to come at a high cost interest (including high fees) and would likely be objected to by the Lightstream Group's secured creditors, whose security would likely be primed by any such interim financing. Further, the Plaintiffs fail to recognize that buyers will consider the value of undrilled inventory, and as such it is unnecessary to drill wells to obtain the value suggested by the Plaintiffs in a sales process.[22] In short, the Plaintiffs make

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[19] *CW Shareholdings Inc v WIC Western International Communications Ltd* (1998), 160 DLR (4th) 131 (Ont Ct Gen Div) at para 60. [**TAB 2**]

[20] Scott Transcript at 16, lines 23-27 and 17, lines 1-9. [**Comeback Brief, TAB 2**]

[21] Plaintiffs' Second Brief at para 28.

[22] Scott Transcript at 17, lines 20-24. [**Comeback Brief, TAB 2**]

suggestions based on best-case-scenario speculative outcomes without putting up any money of their own, making any economic commitments, or bearing any of the risk.

22. The Plaintiffs assert the Lightstream Group should be focussed on a restructuring proposal. In fact, the Plaintiffs have not taken even the most cursory of steps that might demonstrate a serious intention to provide a solution to this CCAA proceeding. The Plaintiffs criticize the Sale Procedures, the associated Secured Noteholder Credit Bid, the Support Agreement and TD Securities' appointment as Sale Advisor without offering any realistic alternative solution. The Support Agreement, entered into by the Lightstream Group with a view to presenting a successful restructuring to its security holders through the Arrangement Proceedings, provides a CCAA backstop together with the Secured Noteholder Credit Bid. This preserves value in the Lightstream Group and provides certainty to many stakeholder groups with respect to the future of the Lightstream Group, which certainty would not be present in "free fall" CCAA proceedings.

23. The Plaintiffs rejected a restructuring proposal that provided them with a return on their investment and which the independent financial advisor to the board of directors of LTS opined would leave the Unsecured Noteholders in a better position than the alternative.[23]

D. Market Conditions are not a Relevant Factor in the Timing of the CCAA Sale Process

24. The Plaintiffs are now concerned that a sale process may prove they no longer have economic interest in the Lightstream Group and they are trying to delay the progress of these proceedings to leverage their own position against the best interests of the Lightstream Group given they have nothing to lose. The remaining stakeholders, however, are not obligated to wait "in the hopes of some future result".[24] Further delay directly prejudices the stakeholders of the Lightstream Group, as its cash on hand and petroleum and natural gas assets, which are the collateral of the Lightstream Group's secured creditors, diminish.

25. Market circumstances do not preclude the Court from ordering a marketing process. It would be unfair to allow the debtor to be inactive at the expense of the creditors who are

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[23] CBCA Opinion of RBC Capital Markets, Scott Affidavit at Exhibit 2, the Affidavit of Peter D. Scott, sworn July 28, 2016, at Exhibit B10. **[TAB 3]**

[24] *Nelson Education Limited, (Re)*, 2015 ONSC 5557 at para 38 ("*Nelson Education*"). **[TAB 4]**

trying to recover value, particularly where that value is eroding. Such an approach of "doing nothing" in the hopes that market circumstances change has no legislative or jurisprudential basis; despite the cyclical nature of many industries, courts have not ordered lenders against their wishes to "wait and see" for an indeterminate period whether market conditions may improve.[25]

26. In particular, downturns in the market, especially in the boom and bust economy of Alberta, have been considered to be foreseeable and an ordinary business risk, such that it should not necessitate special considerations in CCAA proceedings.[26]

E. The Threshold Issue

27. Prior to the granting of the Initial Order the Plaintiffs brought an application seeking an order:

> (a) excluding their claims against Lightstream from the stay of proceedings in the Initial Order; and
>
> (b) directing a trial of the issues raised in their actions prior to hearing any further orders or proceedings with respect to Lightstream's application under the *CCAA*.[27]

28. In response, Lightstream submitted that if the Court were to determine that, based upon the pleadings, the Plaintiffs would only ever have an unsecured claim for the value of their Unsecured Notes plus pre-filing interest, there would be no need to have the underlying lawsuits, which have merged into the *CCAA*, be made the subject of a contested, multi-day, trial-like proceeding to be determined prior to December 31, 2016.

29. This Court agreed with Lightstream's submissions, and directed that the threshold issue identified by Lightstream be determined on a basis to be agreed to by the Parties, or at the return date of October 11, 2016 if the parties were unable to come to an agreement.

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[25] *Kerr Interior Systems Ltd, Re,* 2011 ABQB 214 at para 62, ("*Kerr*") **[TAB 5]**; *Nelson Education* at para 38(e) **[TAB 4]**; *Stelco Inc, (Re),* [2006] OJ No 276 at paras 17-18. **[TAB 6]**

[26] *Kerr* at para 62. **[TAB 5]**

[27] Affidavit of David Kirsch, sworn September 23, 2016 at paras 28-29, (the "**Kirsch Affidavit**").

30. The parties have been unable to come to an agreement regarding the basis on which the threshold issue should be determined. Accordingly Lightstream submits that the Plaintiffs' claim raises the three following threshold questions, each of which would, if decided in the negative, render a trial of the Actions unnecessary:

(a) Have the claims of the Plaintiffs asserted in the Actions become potential claims within the *CCAA* proceeding?

(b) Is there jurisdiction in the Court to recognize the Plaintiffs' claims as secured claims after the granting of the Initial Order or to make an order varying the Transaction and requiring Lightstream to issue additional Secured Notes to remedy alleged oppressive conduct?

(c) If there is jurisdiction to make an Order recognizing the Plaintiffs' claims as secured claims or varying the Transaction, would the Court exercise its discretion to do so based upon the facts as pleaded and evidence agreed upon?

(collectively, the "**Threshold Issues**").

31. The Plaintiffs have objected to the first and third of the Threshold Issues, and have proposed that the threshold issue should be confined to a single question regarding one of the remedies originally sought by the Plaintiffs:

> "Does the Court have jurisdiction in the context of the present proceeding under the CCAA to require Lightstream Resources Ltd. to issue additional secured notes to the oppression claimants as Plaintiffs in Action Nos. 1501-08782 and 1501- 07813 (the "Action")."

32. Lightstream disagrees with this framing of the Threshold Issues. Its submissions on the proper form of the questions are set out below.

(i) Have the Claims of the Plaintiffs asserted in the Actions become Potential Claims within the CCAA Proceeding?

33. This question is of fundamental importance in determining whether the Plaintiffs could ever be entitled to the relief that they seek in these proceedings.

34. Whatever claims the Plaintiffs had against Lightstream upon the commencement of the *CCAA* proceedings have become claims within the *CCAA* upon issuance of the Initial Order. This is consistent with the purpose of the *CCAA* and the single proceeding model established for the protection of all creditors. Those claims should and will be dealt with in the *CCAA* proceedings.[28]

35. In the Actions, the Plaintiffs seek, *inter alia*, a declaration that they were entitled to participate in the Transaction and an order requiring Lightstream to issue Secured Notes under section 242(3)(e) of the ABCA to remedy alleged oppressive conduct.[29]

36. This claim, like any other claim of the Plaintiffs against the Lightstream Group, has been subsumed within the single proceeding model of the *CCAA*. However, a threshold issue arises on the facts as pleaded by the Plaintiffs as to whether this remedy is even available in the *CCAA*.

37. If the Court determines, as Lightstream will submit, that based upon the pleadings the Plaintiffs would only ever have an unsecured claim for the value of their Unsecured Notes plus pre-filing interest, then there will be no basis to have the underlying lawsuit, which has merged into the *CCAA*, be the subject of a contested trial-like proceeding.

(ii) Is there Jurisdiction in the Court to Recognize the Plaintiffs' Claims as Secured Claims after the granting of the Initial Order or to make an order varying the Transaction and requiring Lightstream to issue additional Secured Notes to remedy Alleged Oppressive Conduct?

38. The Plaintiffs' desire to re-frame the second Threshold Issue is an oversimplification of the issue and focuses solely on one of the remedies sought by the Plaintiffs' rather than the question of the jurisdiction of this Honourable Court to adjudicate their claims. The relief sought by the Plaintiffs is not simply an order requiring the issuance of additional secured notes, but a declaration that the Transaction of July 2, 2015 be unwound, that the Plaintiffs be entitled to participate in the Transaction on the same basis as the Secured Noteholders, and an order that Lightstream issue further Secured Notes in order to remedy the allegedly oppressive conduct.

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[28] CCAA, s 2(1), "claim". **[Initial Order Brief, TAB 2]** See also *AbitibiBowater Inc, Re*, 2012 SCC 67 at paras 21-26. **[Initial Order Brief, TAB 24]**

[29] ABCA, s 242(3)(e). **[Initial Order Brief, TAB 25]**

39. In order to grant the remedy sought by the Plaintiffs, the *CCAA* Court must find: first, that the Plaintiffs' claims survived Lightstream's entry into *CCAA* protection as secured claims; and second, that a *CCAA* court has the same broad jurisdiction to fashion a remedy for oppression as a court sitting outside the ambit of the *CCAA*. Lightstream will submit that neither of these positions is correct. Accordingly, the second Threshold Issue must reflect the actual relief being sought.

(iii) If there is Jurisdiction to make an Order recognizing the Plaintiffs' Claims as Secured Claims or varying the Transaction, would the Court exercise its Discretion to do so based upon the Facts as Pleaded and Evidence agreed upon?

40. The Plaintiffs submit that this threshold question as framed would require the Court to determine the ultimate issue based on an incomplete factual record. With respect, this is based on a misunderstanding of Lightstream's position.

41. Lightstream proposes that the hearing of the Threshold Issues should proceed on a summary basis, with all facts as pleaded and as subsequently admitted by the Plaintiffs or as may be agreed between the parties. The Court would not be required to make any factual determination concerning the reasonable expectations of the Plaintiffs, or whether oppressive conduct had taken place. Rather, Lightstream will submit that even in the event that the Court were to find the facts on which the Plaintiffs' base their oppression claim, and determine that it had the jurisdiction to grant the relief sought, the court would not exercise that jurisdiction on those facts.

42. The Plaintiffs purchased unsecured notes in a secondary market with contractual rights associated with them. They plead that these contractual rights have been breached. They also allege that based on a misrepresentation, they held on to their notes instead of selling them into the market.[30] The appropriate remedy for both of these allegations is an award of damages in the amount of the diminution in value of the unsecured notes caused by either the breach of contract or tort of misrepresentation.

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[30] Kirsch Affidavit at paras 16-18.

43. The conduct upon which the oppression claim is based is identical. Accordingly, there would be no basis to award any other measure of damages by relying on the oppression remedy.

44. In addition, Lightstream will submit that, on the facts of this case, a CCAA Court would not award a remedy which would have the effect of diluting the security position of existing secured creditors who provided real value to the company in return for their secured claims, particularly when this could endanger the Secured Noteholder Credit Bid.

45. To do so would be contrary to the very purpose of the CCAA to facilitate a restructuring which allows the business of the debtor company to continue to operate. These are the very types of orders that the Ontario Court of Appeal held were not appropriate in the CCAA context in *US Steel Canada Inc, Re*.[31]

46. On the facts of this case, the Plaintiffs have an undisputed, unsecured claim for the full principal amount of their Unsecured Notes, plus any unpaid pre-filing interest. The unsecured Notes at issue suffered only a partial reduction in value, and the damages which might be awarded in respect of the Plaintiffs' causes of action would be less than the face value of the notes plus unpaid pre-filing interest.

47. Accordingly, there is no issue of quantification of their unsecured claim. There is no need for a claims process to determine this.

48. To the extent that the Plaintiffs seek to have their unsecured claim "equitably securitized", if such relief were to be available, it would be necessary to determine the quantum of both the unsecured portion and secured portion of the claim.

49. If such relief is not available as a threshold matter, it would be a waste of the court's resources to hold a hearing to determine the underlying facts.

(iv) Timing and Procedure

50. The issues raised by the Plaintiffs have the potential to affect the restructuring transaction that Lightstream has secured, being the Secured Noteholder Credit Bid, coupled

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[31] *US Steel Canada Inc, Re*, 2016 ONCA 662 at paras 52, 59, 76, 82. **[TAB 7]**

with the fully committed refinancing of the first lien lenders (which requires, as a condition, another $50 million cash injection, fully committed from the Secured Noteholders). The restructuring transaction and Replacement Credit Facility, by their terms, are required to be fully implemented prior to December 31, 2016.[32]

51. Lightstream submits that the hearing to determine the Threshold Issues (the "**Threshold Issues Hearing**") should proceed on the basis of the facts pleaded by the Plaintiffs and any additional facts which are not in dispute. Lightstream is prepared to work with the Plaintiffs to prepare an agreed statement of facts for the Court. The agreed statement of facts may be supported by an agreed book of documents.

52. Lightstream submits that, based on this Honourable Court's advice that time is available during the week of November 14, 2016, the Threshold Issues Hearing should proceed on the following timetable:

(a) Any agreed statement of facts and supporting documents will be settled four weeks prior to the Threshold Issues Hearing.

(b) Lightstream's written submissions (and those of any party supporting Lightstream) shall be delivered on the third Friday prior to the threshold issues hearing, on October 28, 2016.

(c) The Plaintiffs' written submissions shall be delivered on November 4, 2016.

(d) Any reply submissions shall be filed on November 10, 2016.

53. In the event that Lightstream is not successful at the Threshold Issues Hearing, Lightstream agrees that a trial of issues should be conducted on an expedited basis. Lightstream submits that this should take no longer than one week (the "**Trial**"). Accordingly, Lightstream also seeks an order putting the following timetable in place:

(a) The agreed statement of facts, supporting documents to be settled four weeks prior to the Trial;

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[32] Scott Affidavit at para 57.

(b) Any primary expert reports opinions tendered by the parties to be served four weeks prior to the Trial and any rebuttal expert reports to be served two weeks prior to the Trial; and

(c) Written evidence in chief to be delivered on one week prior to the Trial.

54. On August 3, 2016, the Plaintiffs also filed applications to amend their statements of claim to add the following individuals who, at all material times, were the directors of Lightstream: John D. Wright, Ian Brown, Martin Hislop, Kenneth R. McKinnon, Corey C. Ruttan, Craig Lothian and W. Brett Wilson (the "**Individual Defendants**").[33]

55. This motion was adjourned *sine die* by Justice Campbell on August 8, 2016 in light of the *CBCA* filing. Lightstream further submits that, in the event that it is unsuccessful at the Threshold Issues Hearing, the Plaintiffs' motion to amend the Statement of Claim should also be heard in advance of the trial (the "**Motion to Amend**"). Accordingly, Lightstream also seeks an order putting a timetable in place with respect to the Motion to Amend.

IV. NATURE OF THE ORDER SOUGHT

56. The Lightstream Group seeks the continuation of the Initial Order in the form granted on September 26, 2016, by the Honourable Justice A.D. MacLeod and an extension of the stay of proceedings to December 16, 2016.

ALL OF WHICH IS RESPECTFULLY SUBMITTED THIS 7th DAY OF OCTOBER, 2016

BLAKE, CASSELS & GRAYDON LLP

Kelly Bourassa /Michael Barrack
Counsel to the Lightstream Group

[33] FrontFour Motion to Amend the Statement of Claim [**Tab 8**]; Mudrick Motion to Amend the Statement of Claim. [**Tab 9**]

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Pente Investment Management Ltd. v. Schneider Corp.

1998 CarswellOnt 4035, [1998] O.J. No. 4142, 113 O.A.C. 253, 42 O.R. (3d) 177, 44 B.L.R. (2d) 115, 83 A.C.W.S. (3d) 51

Maple Leaf Foods Inc. and Sch Acquisition Inc., Plaintiffs (Appellants) and Schneider Corporation, Douglas W. Dodds, Anne C. Fontana, Gerald A. Hooper, Frederick D. Morash, Larry J. Pearson, Brian J. Ruby, Eric N. Schneider, Ronald J. Simmons, Hugh W. Sloan, J.M. Schneider Family Holdings Limited, Frederick P. Schneider, Betty L. Schneider, Herbert J. Schneider, Jean M. Hawkings, Bruce Hawkings, CIBC Mellon Trust Company, Smithfield Foods Inc., Harbour Glen Securities Limited, Kinspan Investments Limited, Laurel Ridge Investments Limited and Jadebridge Holdings Limited, Defendants (Respondents)

Pente Investment Management Ltd. and Cascade Holdings Ltd., Plaintiffs (Appellants) and Schneider Corporation, Douglas W. Dodds, Anne C. Fontana, Gerald A. Hooper, Frederick D. Morash, Larry J. Pearson, Brian J. Ruby, Eric N. Schneider, Ronald J. Simmons, Hugh W. Sloan, Frederick P. Schneider, Betty L. Schneider, Herbert J. Schneider, Jean M. Hawkings, CIBC Mellon Trust Company, Smithfield Foods Inc., Maple Leaf Foods Inc., J.M. Schneider Family Holdings Limited, Sch Acquisition Inc., Harbour Glen Securities Limited, Kinspan Investments Limited, Laurel Ridge Investments Limited and Jadebridge Holdings Limited, Defendants (Respondents)

Osborne, Weiler, Feldman JJ.A.

Heard: August 4-6, 1998
Judgment: October 20, 1998 *
Docket: CA C29923, C29945

Proceedings: affirming (May 10, 1998), Doc. 98CL-1011, 98-BK001935, 95-BK-001935A (Ont. Gen. Div. [Commercial List])); additional reasons at (July 31, 1998), Doc. 98-GD-422580, 98-BK001935 (Ont. Gen. Div. [Commercial List])

Counsel: *Lyndon A.J. Barnes*, and *David A. Stamp* for the appellant, Maple Leaf Foods.
Harvey T. Strosberg, Q.C., *G. Wesley Voorheis*, and *Michael Woolcombe*, for the appellant Pente Investment and Cascade Holdings.
J.D.G. Douglas and *Freya Kristjonson*, for the respondents J.M. Schneider Family Holdings (the Schneider Family).
Thomas G. Heintzman, *R. Paul Steep* and *Susan Rothfels*, for the respondent, Smithfield Foods, Inc.
Alan H. Mark, *Jessica A. Kimmel* and *Nando DeLuca* for the respondents, Schneider Corporation, Douglas W. Dodds, Gerald A. Hooper, Frederick D. Morash, Larry J. Pearson, Brian J. Ruby, Ronald J. Simmons and Hugh W. Sloan.

Subject: Corporate and Commercial; Civil Practice and Procedure

APPEAL by competitor from judgment reported at (1998), 40 B.L.R. (2d) 244, 62 O.T.C. 1 (Ont. Gen. Div. [Commercial List]) dismissing action by minority shareholders against company for oppression remedy.

The judgment of the court was delivered by *Weiler J.A.*:

Overview

1 The appellants are Maple Leaf Foods Inc. ("Maple Leaf"), a bidder for the shares of Schneider Corporation ("Schneider"), and two small shareholders of Schneider who are supporting Maple Leaf. They raise two principal issues. The first concerns the duties of a Special Committee of the Board of Directors of Schneider Corporation and of the Board itself when dealing with a bid for change of control of the company. The second involves the interpretation of a provision in the articles of a company commonly known as the "coattail provision".

2 Schneider Corporation is an 108 year old Ontario corporation that is controlled by members of the Schneider Family ("the Family") [1] through a holding company. The issued share capital of Schneider consists of common voting shares and Class A non-voting shares. Both classes of shares trade on the Toronto Stock Exchange, with the Class A shares representing most of the equity in the company. Although the Family only owns 17% of the non-voting shares, the Family controls the company because it owns approximately 75% of the common voting shares.

3 On November 5, 1997, Maple Leaf, a competitor of Schneider, announced its intention to make an unsolicited take-over bid for Schneider at $19 a share, through its holding company SCH. In response, the Board established a Special Committee consisting of the independent non-family directors to review the Maple Leaf offer and to consider other alternatives. Subsequently Maple Leaf itself made an offer of $22 a share, but this offer was rejected by the Family. Ultimately, the Family told the Special Committee that the only after it would accept was an offer made by Smithfield Foods, an American company that, at the time, was equal to $25 a share. In order for the Family to accept the Smithfield offer, which would have had the effect of enabling Smithfield to "lock-up" control of Schneider, the Board had to take certain steps which, on the advice of the Special Committee, it took. Despite this, and after the Family had agreed to the Smithfield offer, on December 22, 1997, Maple Leaf made a further offer of $29 a share to Schneider's common and Class A shareholders.

4 The law as it relates to the general duties of the directors of a company is well known. The directors of a company have an obligation to act honestly and in good faith in the best interests of the corporation: s. 134(1)(a) *Business Corporations Act*, R.S.O. 1990, c. B.16 (the "*OBCA*"). Further, in discharging their obligations, the directors must exercise the care, diligence and skill that a reasonably prudent person would exercise in comparable circumstances: s. 134(1)(b). If the actions of the directors unfairly disregard the interests of a shareholder, unfairly prejudiced those interests, or are oppressive to them, s. 248 of the *OBCA* comes into play and allows the court to grant any remedy it thinks fit. [2]

5 The appellants attack the actions of the Special Committee on the basis, first, that it was not in fact independent, and second, that the advice given by the Special Committee to the Board was not in the best interests of Schneider and its shareholders. The appellants allege that the Special Committee did not act independently because it allowed Dodds, the Chief Executive Officer of Schneider, to negotiate on the Committee's behalf with potential bidders. Furthermore, the appellants submit that Dodds and the members of the Special Committee were unduly deferential to the wishes of the Family. The appellants' position is that public statements made by the Family created an expectation that an auction for the controlling block of shares of Schneider (the Family Shares) would be held and that those shares would be sold to the highest bidder. The appellants say that, because Maple Leaf was not given a chance to bid after the Smithfield offer of $25 a share was received, the Special Committee, in acceding to the Family's request to accept the Smithfield offer, truncated the auction process. Maple Leaf and the other appellants seek to have this court invalidate the agreement between the Family and Smithfield on the basis that the process undertaken by the Special Committee and the Board, which led to the Family's agreement with Smithfield, unfairly disregarded the interests of the non-Family shareholders and unfairly prejudiced them.

6 The second issue involves the coattail provision in Schneider's articles. A typical coattail provision provides that if an offer is made for the voting shares of a corporation and the non-voting shareholders are excluded from that offer because an identical bid is not made for their shares, the non-voting shareholders have the right to convert their non-voting shares to common voting shares. They can then tender to the offer for the common shares.

7 Maple Leaf offered the same premium to the Class A non-voting shareholders as it did to the holders of common voting shares. But Maple Leaf claims that its bid nonetheless triggered the coattail provision in Schneider's articles because the condition attached to its bid for the non-voting shares was not identical to the condition attached to its bid for the common shares. As a result, Maple Leaf says that the effect of its bid was to convert the non-voting Class A shares into common voting shares. If all Class A non-voting shares were converted into common voting shares the Family's percentage of common voting shares would be diluted to a level where the Family's support might not be necessary for Maple Leaf's bid to be successful. Maple Leaf might then be able to gain control of Schneider despite the Family's lock-up agreement with Smithfield.

8 Farley J. dismissed the appellants' actions. In relation to the first issue, he concluded that the Special Committee and the directors "exercised their powers and discharged their duties honestly, and in good faith, with a view to the best interests of Schneider and that they exercised the care, diligence and skill that a reasonable and prudent person would exercise in comparable circumstances in relation to dealing with the take over bid situation." He also found that because Schneider was known to be controlled by the Family which could decide whether or not to sell its shares, the company was never truly in play and no public expectation was created that an auction would be held.

9 In relation to the second issue, Farley J. found that to the extent that Maple Leaf's bid did not exclude the Class A shareholders from the premium being offered for the Family's shares, the coattail provisions were not triggered. Even if Maple Leaf's offers were exclusionary, he held that the conversion rights did not arise because, pursuant to Schneider's articles, the Family had filed certificates undertaking not to accept an exclusionary offer without giving written notice to its transfer agent. For the reasons which follow. I am of the opinion that Farley J. was correct.

The Oppressions Claims, Reasonable Expectations and the Duties of Officers and Directors

Facts

10 I do not propose to repeat all of the facts outlined in the reasons of Farley J. and the facta of the parties, but some further information is essential to understand the issues which must be determined on this appeal.

11 The Board of Schneider consists of nine persons: two members of the Schneider Family (Eric Schneider and Anne Fontana), two members of the senior management (Douglas Dodds, the Chairman of the Board and Chief Executive Officer, and Gerald Hooper, the Chief Financial Officer), and five outside directors who are all successful business persons with no connection to the Schneider Family. The Board established a Special Committee consisting of the five independent non-Family directors to review and consider the Maple Leaf offers and to make appropriate recommendations to the Board.

12 The Special Committee retained Nesbitt Burns Inc. as its financial advisor and Goodman, Phillips & Vineberg as its legal advisor.

13 The first SCH/Maple Leaf offers for Schneider were formally made on November 14, 1997 to both the common voting and Class A non-voting shareholders.

14 After the first SCH/Maple Leaf offers, the Special Committee through its financial and legal advisors, and the senior management of Schneider, commenced a process of contacting other parties that might be interested in acquiring Schneider. Schneider also established a data room containing confidential information to be provided to potential bidders. As a condition to being provided with access to the data room, potential bidders were required to sign a confidentiality agreement which contained a standstill provision that prevented them from acquiring or making any proposal to acquire shares of Schneider for two years without the written consent of the board of directors of Schneider. The form of confidentiality agreement used by Schneider provided that the only representatives of Schneider that potential bidders could contact were Dodds, the Chairman and Chief Executive Officer, Hooper, the Chief Financial Officer and Eric Schneider the General Counsel, Secretary and a Vice-President.

15 On November 23, 1997, the Board issued its directors' circular responding to the Maple Leaf offer and recommended that Schneider shareholders not tender to the Maple Leaf offer on the basis that among other things, the Maple Leaf offer was not reflective of the fair value of the shares of Schneider and that the Family had no intention of accepting the Maple Leaf Offer. Under the heading "Alternatives to the Offers" the directors' circular stated:

> The Board of Directors is committed to maximizing Shareholder value. In this connection, the Corporation and Nesbitt Burns have held discussions with several interested parties concerning possible transactions which would result in Shareholders receiving greater value for their Shares than under the Maple Leaf Offers. The Board of Directors and Nesbitt Burns are actively exploring alternatives to maximize Shareholder value. The Schneider family, which collectively beneficially owns or controls approximately 75% of the Common Shares and approximately 17% of the Class A shares on a fully-diluted basis, has advised the Board of Directors that it might consider accepting a financially more attractive offer for its Shares.

Also on November 23, 1997, the Family confirmed in writing to the Board that:

> The undersigned also confirm that they might consider alternative control transactions involving the Corporation and acknowledge that, on the basis of such confirmation, Nesbitt Burns Inc., financial advisor to the special committee of the Board of Directors constituted to consider the Offers, is pursuing alternatives to the Offers.

16 On December 2, 1997, Schneider adopted a temporary shareholder rights plan. A rights plan is a common interim measure intended to give a Board time to see if there are other bids for a company and to stall an unsolicited or hostile take-over bid. Here, the rights plan provided that if a purchaser acquired 10% or more of the shares of Schneider, both classes of shareholders had the right to purchase Class A shares at 50% of the market price as at November 4, 1997 ($13.25) following a special meeting of shareholders. The press release announcing the Rights Plan stated:

> In the midst of ongoing discussions with several parties who have expressed interest in the company, the Board of Directors of Schneider Corporation today announced that, on the recommendation of its Special Committee, the Corporation has adopted a temporary Shareholder Rights Plan. This measure has been enacted to ensure that the Board and its advisers have the opportunity to fully explore all options for maximizing shareholder value... "The Board adopted the Rights Plan to create a stable environment in which it will have the time and flexibility it needs to explore and evaluate the options for maximizing value for all Schneider's shareholders" said Douglas W. Dodds. Chairman and CEO...

17 On December 11, 1997, Dodds wrote to Maple Leaf and requested that it deliver enhanced offers by December 12, 1997, stating that:

> The process of shareholder value maximization in which our Board of Directors has been engaged since receipt of your offers is fast approaching its climax. Schneider Corporation will be receiving alternative offers to the Maple Leaf Foods offers from interested parties by this Friday December 12, 1997... Accordingly, we invite you to deliver to us your enhanced offers by this Friday. We encourage you to put forward your enhanced offers on a basis that most appropriately and fairly reflects the inherent and strategic values to Maple Leaf Foods of Schneider Corporation. Please also advise how we may be in contact with you and your advisers over this weekend.

18 On December 12, 1997, Maple Leaf increased its offer for Schneider shares to $22 per share and allowed Schneider's shareholders to elect to receive part of this consideration in the form of shares of Maple Leaf Foods Inc. On the same day, Schneider received written proposals from each of Booth Creek Inc. and Smithfield to acquire all of the shares of Schneider. The proposal from Booth Creek contemplated a take-over bid for all of the outstanding shares of Schneider at a price per share of $24.50 cash, conditional upon 66 $^{2}/_{3}$% of the common voting shares and non-voting shares being deposited under the offer. The proposal from Smithfield contemplated a take-over bid for all of the outstanding shares of Schneider, with Schneider shareholders receiving shares exchangeable into shares of Smithfield. Based on the closing

price of Smithfield shares on December 12, 1997, and the relevant exchange rate on that date, the Smithfield proposal was worth approximately $23 per share.

19 Prior to the announcement of the unsolicited bid by Maple Leaf's subsidiary on November 5, 1997, the Family had no intention of selling its shares. By December 13, 1997, the Family had indicated a tentative preference to sell its shares to Smithfield and doubted that either Booth Creek or Maple Leaf would enhance their offers sufficiently that the Family would tender to them. However, the Family had made no decision to sell, and if they were to sell, to whom, or at what price. The criteria used by the Family to evaluate offers were first arrived at on December 13.

20 On December 14, 1997, at a meeting of the Board of Directors, management advised that it believed that Schneider was "too big to be small and too small to be big", and that a strategic merger was in the best long-term interests of Schneider. The Family stated that it shared this belief. The Family also advised the board of directors that it had reviewed the amended Maple Leaf offer as well as the proposals from Booth Creek and Smithfield in terms of three factors: financial value, continuity of Schneider in a manner consistent with the Family's desires, and the effect of any transaction on customers and suppliers. The Family told the Board that, while the Smithfield proposal did not meet its financial adequacy criteria, it did meet the Family's other two criteria and that, assuming the Smithfield could satisfy the Family's financial adequacy criteria, a strategic merger would be in the best interests of Schneider.

21 Following this, a meeting was held by a working group that included Dodds and advisers from Nesbitt Burns and Goodman's. This group made the decision that Dodds should go to see Luter, the Chairman of the Board and Chief Executive Officer of Smithfield, and enter into negotiations with Booth Creek.

22 On December 15, Dodds conducted further negotiations with Booth Creek and on the morning of December 16, he met with representatives of Smithfield, including Luter. Dodds explained why Schneider was historically undervalued.

23 Around lunchtime, Smithfield increased the value of its offer to $25 per share on the basis of the price of Smithfield's shares and the relevant exchange rate on that date. In addition, Dodds obtained Smithfield's agreement that it would not sell Schneider for at least two years, and would allow the Schneider family to appoint a representative to Smithfield's board of directors. Luter told Dodds that this was his best, last offer and that if he had any suspicion Schneider was using Smithfield's offer to try to obtain higher offers from others, he would withdraw his offer and make a public announcement disclaiming any interest in the company. The Smithfield offer was open until 8 a.m. on December 18. That same day, Dodds reported this offer to the Family and Mida, the director of mergers and acquisitions at Nesbitt Burns and an adviser to the Special Committee.

24 After Dodd's meeting with Luter the Board issued an amended directors' circular recommending that Schneider shareholders not tender to the revised Maple Leaf offers. The Board of Directors did not disclose that the Family would evaluate the offers using criteria additional to financial considerations. Under the heading "Alternative Transactions" the circular stated:

> The Board of Directors has been actively engaged in a process of identifying other transactions that might result in greater value to Shareholders than was offered under the Original Offers. On December 12, 1997, the Board of Directors received proposals for, and is in the process of negotiating, alternative transactions which might result in greater value to Shareholders than is being offered under the Amended Maple Leaf Offers.

25 At 5 p.m. on December 17, 1997, Booth Creek made a revised written proposal to Schneider increasing the value of its offer to $25.50 cash and stated that its offer was open until 8 p.m. that same evening. At $25.50 the Booth Creek proposal was less attractive financially to the Family than the Smithfield share exchange proposal, which would yield them a tax saving of $4 per share. Non-family shareholders, depending on their individual tax position, might or might not be in the same position. Booth Creek, a private company, could not offer a share exchange transaction.

26 At the meeting of the Board on December 17, 1997, the Family announced that it wanted to accept the revised offer from Smithfield. Among other things, the Family stated to the Board that:

> We also think that it is important to reiterate that we as a family did not seek to sell this company but that through the process of the last 6 weeks we have come to the conclusion that now is the time to sell the control of the company.

27 At a subsequent meeting of the Special Committee that night, Nesbitt Burns advised that while the Smithfield proposal was within the $25-29 fair price range, the risk associated with adverse share price movement and exchange rate movement during the short period until the offer could be formally accepted should be reflected by applying a 6% discount to the offer so that its present value was $23.50. Nesbitt Burns also told the Special Committee that, in its view, if the Smithfield offer were permitted to expire and no other change of control transaction involving Schneider were consummated, the shares of Schneider would settle in a trading range between $18 and $20 a share.

28 The Special Committee then recessed and Dodds made enquiries of Smithfield as to whether it would raise its offer. Smithfield refused to pay more but Dodds was successful in negotiating a slight improvement in the exchange rate aspect of the offer.

29 The original proposal, as submitted by Smithfield contemplated that the transaction would proceed by way of a plan of arrangement or merger. That is the Board would approve of the Family entering into a lock-up agreement for its shares with Smithfield then the merger proposal would be voted upon by all shareholders and approved by the court. Before asking the shareholders and the court to approve the merger the Board would have had to provide and opinion that the transaction was fair. In light of Nesbitt Burns' discounted valuation of the Smithfield proposal, the Board was unwilling to do so.

30 To avoid the Board having to issue an opinion that the proposed transaction was fair, Smithfield made offers by way of take-over bids to acquire any and all common voting shares and all Class A shares of Schneider on the condition that the Family agree to tender its shares. The shares of Schneider were to be exchanged for 5415 of a share in a newly incorporated, wholly-owned Canadian subsidiary of Smithfield. Each whole exchangeable share would then be exchangeable for one common share in Smithfield. The structure of this second transaction meant that Smithfield might not be able to acquire two-thirds of the Class A shares and, therefore, might not be able to take Schneider private.

31 In order for the Family to accept the offer from Smithfield, it was still necessary for the Board to waive the standstill provision in the confidentiality agreement Smithfield signed and to remove the rights plan. The Family asked the board to do this. Upon the recommendation of the Special Committee, the Board did so. On December 18, 1997, the Family entered into the lock-up agreement.

32 On December 22, 1997, Maple Leaf announced that, despite the Family's lock-up agreement with Smithfield, it was increasing its offer to $29 per share, cash, conditional on obtaining two-thirds of each class of share. Prior to this, Maple Leaf entered into deposit agreements with two funds to buy Maple Leaf's shares at $29, no matter what the outcome of its latest bid was. On December 30, 1997, five Class A shareholders, holding in aggregate 675,000 shares, representing more than 10% of the total Class A shares outstanding, wrote a letter to Schneider's Board of Directors complaining that "the actions or inaction of the Special Committee, together with those of the Schneider family have in effect contaminated the value maximization process outlined by the board in its directors' circular and in its public statements."

Determining Whether the Directors have acted in the best interests of the Corporation

33 The mandate of the directors is to manage the company according to their best judgment: that judgment must be an informed judgment; it must have a reasonable basis. If there are no reasonable grounds to support an assertion by the directors that they have acted in the best interests of the company, a court will be justified in finding that the directors acted for an improper purpose: *Teck Corp. v. Millar* (1972), 33 D.L.R. (3d) 288 (B.C. S.C.) at 315-316, adopted as the law in Ontario by Montgomery J. in *Olympia & York Enterprises Ltd. v. Hiram Walker Resources Ltd.* (1986), 59 O.R. (2d) 254 at 255 (Ont. H.C.), affirmed (1986), 59 O.R. (2d) 254 (Ont. Div. Ct.).

34 One way of determining whether the directors acted in the best interests of the company, according to Farley J., is to ask what was uppermost in the directors' minds after "a reasonable analysis of the situation.": *820099 Ontario Inc. v. Harold E. Ballard Ltd.* (1991), 3 B.L.R. (2d) 113 at 123 (Ont. Gen. Div.), affirmed (1991), 3 B.L.R. (2d) 113 (Ont. Div. Ct.); *CW Shareholdings Inc. v. WIC Western International Communications* (May 17, 1998), Doc. Toronto 98-CL-2821 (Ont. Gen. Div.). It must be recognized that the directors are not the agents of the shareholders. The directors have absolute power to manage the affairs of the company even if their decisions contravene the express wishes of the majority shareholder: *Teck Corp. v. Millar* (1972), 33 D.L.R. (3d) 288 (B.C. S.C.) at 307. However, acting in the best interests of the company does not necessarily mean that the directors must act in the best interests of one of the groups protected under s. 234. There may be a conflict between the interests of individual groups of shareholders and the best interests of the company: *Brant Investments Ltd. v. KeepRite Inc.* (1987), 60 O.R. (2d) 737 (Ont. H.C.), aff'd (1991), 3 O.R. (3d) 289 (Ont. C.A.) at 301. Provided that the directors have acted honestly and reasonably, the court ought not to substitute its own business judgment for that of the Board of Directors: *Brant Investments v. KeepRite Inc., supra*, which deals with the analogous section of the *Canadian Business Corporations Act*, R.S.C. 1985, c. C-44. If the directors have unfairly disregarded the rights of a group of shareholders, the directors will not have acted reasonably in the best interests of the corporation and the court will intervene: *820099 Ontario Inc. v. Harold E. Ballard Ltd., supra.*

35 The appellants have urged this court to consider the actions of the directors pursuant to a standard which is derived from statute law in the State of Delaware known as "enhanced scrutiny". The key features of the enhanced scrutiny test are a judicial determination of the adequacy of the decision-making process employed by the directors, and a judicial examination of the reasonableness of the directors' actions in light of the circumstances then existing: *Paramount Communcations Inc. v. QVC Network Inc.*, 637 A.2d 34 (U.S. Del. Super. 1994) at 45 . The directors have the onus of satisfying the court that they were adequately informed and acted reasonably. Some Canadian authorities such as *Exco Corp. v. N.S. Savings & Loan Co.* (1987), 35 B.L.R. 149 (N.S. T.D.) and *347883 Alberta Ltd. v. Producers Pipelines Inc.* (1991), 80 D.L.R. (4th) 359 (Sask. C.A.) have adopted a proper purpose test, which is similar to enhanced scrutiny in that it shifts the burden of proof to the directors to show that their acts are consistent only with the best interests of the company and inconsistent with any other interests. These cases recognize that there may be a conflict between the directors who manage the company and the interests of certain groups of shareholders, particularly those s. 248 is designed to protect, and have espoused shifting the burden of proof as a method of overcoming the potential conflict.

36 The law as it has evolved in Ontario and Delaware has the common requirements that the court must be satisfied that the directors have acted reasonably and fairly. The court looks to see that the directors made a *reasonable* decision *not a perfect* decision. Provided the decision taken is within a range of reasonableness, the court ought not to substitute its opinion for that of the board even though subsequent events may have cast doubt on the board's determination. As long as the directors have selected one of several reasonable alternatives, deference is accorded to the board's decision: *Paramount, supra*, at 45: *Brant Investments, supra*, at 320. *Themadel Foundation v. Third Canadian Investment Trust Ltd.* (1998), 38 O.R. (3d) 749 (Ont. C.A.) at 754 . This formulation of deference to the decision of the Board is known as the "business judgment rule". The fact that alternative transactions were rejected by the directors is irrelevant unless it can be shown that a particular alternative was definitely available and clearly more beneficial to the company than the chosen transaction: *Brant Investments, supra*, at 314-315.

37 A common method used to alleviate concerns that a conflict of interest exists between directors, who may be major shareholders, and the interests of a minority or non-voting group of shareholders, is the creation of a special committee from among the independent members of a board who do not have a conflict. The purpose of a special committee is to advise the Directors and to make a recommendation as to what the Board should do. It appears that under the law of Delaware, where a Board acts on the recommendation of a special committee, the decision will be accorded respect under the business judgment rule, provided that the special committee has discharged its role independently, in good faith, and with the understanding that in a situation where a change of control transaction is contemplated, the special committee can only agree to a transaction that is fair in the sense of being the best available in the circumstances: *First Boston. Inc. Shareholders Litigation, Re*, Fed. Sec. L. Rep. P 95,322 (U.S. Del. Ch. 1990).

38 The duty of directors when dealing with a bid that will change control of a company is a rapidly developing area of law and as I have indicated. Canadian authorities dealing with the question of the onus, or burden of proof, have not been uniform. In *Brant Investments, supra*, the issue whether the burden of proof is on the directors to justify their actions as being in the best interests of the company or on the shareholders challenging the actions of the company was also raised. McKinlay J.A., at 311-312, found it unnecessary to decide the question because the trial judge had dealt with the issues on a substantive basis, and his decision did not turn on which party had the onus or burden of proof[3] The same is true in the present case.[4] I would add, however, that it may be that the burden of proof may not always rest on the same party when a change of control transaction is challenged. The real question is whether the directors of the target company successfully took steps to avoid a conflict of interest. If so, the rationale for shifting the burden of proof to the directors may not exist. If a board of directors has acted on the advice of a committee composed of persons having no conflict of interest, and that committee has acted independently, in good faith, and made an informed recommendation as to the best available transaction for the shareholders in the circumstances, the business judgment rule applies. The burden of proof is not an issue in such circumstances.

39 The members of the committee acted in good faith in the sense that they acted honestly. The Committee's decision was also informed, in the sense that the Committee was aware that any offer for Schneider's shares might be bettered by Maple Leaf, and that the Family would not sell to Maple Leaf. While the appellants have challenged Farley J.'s finding that the Family would not sell to Maple Leaf, there is ample evidence to support this finding. Even at $29 a share, when tax considerations were factored in the Maple Leaf offer was only as advantageous as the Smithfield offer to the Family, not more advantageous. Apart from financial criteria, Maple Leaf did not meet the Family's expressed concern about the effect of a change of control on the continuity of employment for Schneider's employees, the welfare of suppliers, and the relationship with its customers, whereas Smithfield did. Once again, the real questions are whether the Committee was independent and whether the process undertaken by the Special Committee was in the best interests of Schneider and its shareholders in the circumstances. While *Paramount, supra*, indicates that non-financial considerations have a role to play in determining the best transaction available in the circumstances, here it was conceded that the court should only have regard to financial considerations.

The Special Committee

(i) Should expert evidence have been admitted on the question whether the Special Committee was independent, and on the process by which the agreement with Smithfield was reached.

40 Farley J. declined to admit the proposed evidence of the expert witnesses, Messrs. Cameron and Beck. The appellants seek to overturn the finding of Farley J. that the directors and the Family did not act improperly. In part, they do so on the basis that he erred by refusing to admit the proposed evidence of the two expert witnesses.

41 The proposed evidence of Messrs. Cameron and Beck was contained in two reports. The report of Mr. Beck was essentially a statement of his views on the legal rights and obligations which arose under Ontario law from a set of facts communicated to him. The report of Mr. Cameron consisted largely of his conclusions based on a set of assumed facts given to him and his inferences from those facts on the appropriateness of senior management's participation in negotiations with potential bidders, the process conducted by the Special Committee, and the expectations created by public statements made by the Family.

42 Farley J. ruled that the qualifications of the experts related to corporations, their securities, takeover bids and directors' obligations. He declined to receive the experts' reports on three bases: 1) that the opinions expressed related to domestic law, a matter upon which a court ought not to receive opinion evidence; 2) that there was no specialized and standardized body of conduct to study in this area; and 3) that he did not need the assistance of the experts in understanding the evidence or the concepts and principles involved.

43 For the reasons given by Farley J. I would not give effect to this ground of appeal.

(ii) Should members of Schneider's senior management, particularly Dodds, have been permitted to have a significant role in the sale negotiations with potential bidders?

44 The appellants submit that Dodds had a conflict of interest because he had an interest in continued employment with Schneider and a further conflict arising out of his loyalty to the Family.

45 A potential conflict of interest arises because as a director of a target company, the senior executive has a duty to act in the best interests of the shareholders, but as a member of senior management the executive retains an interest in continued employment. In actively negotiating with a potential bidder the executive is negotiating with his potential boss or executioner. The appellants rely on the decision of Blair J. in *CW Shareholdings Inc.*, for the proposition that no senior executive of a company being sold should be permitted to have a significant role in the sale process.

46 The raison d'etre of a Special Committee independent of management and the controlling shareholder is to protect the interests of minority shareholders and to bring a measure of objectivity to the assessment of bids. If, as was the case in *CW Shareholdings*, senior management in the target company is a member of the Special Committee, the purpose in setting up the Special Committee might be compromised and less reliance placed on its assessment of a particular bid than if the committee were truly independent. Blair J. recognized this and he was critical of the role played by senior management in *CW Shareholdings*. In the end however, he concluded that the involvement of management in the Special Committee did not so taint its approval of the Shaw Communications bid as to undermine the transaction. He also found that the committee had conducted itself in a fashion that enabled the directors to carry out their objective of maximizing shareholder value. In that case, Blair J. upheld the Board's decision, based upon the Special Committee's recommendation to enter into an agreement with Shaw that provided for a break fee and asset agreement in the event that its bid was not accepted.

47 A major distinction between the *CW Shareholdings* decision and this case is that senior management, including Dodds, was not part of the Special Committee that was set up and consequently had no vote as to whether to recommend a bid. A potential conflict of interest still existed, however, because of the active role Dodds played in negotiating with the bidders.

48 Farley J. recognized that in allowing Dodds and to a lesser extent Hooper, the Chief Financial Officer of Schneider, to deal with bidders directly, a potential conflict of interest existed but that this had to be balanced against the benefits to be obtained. He stated:

> It would be appropriate, however, to comment as well [th]at the use of the two management directors. Dodds and Hooper, in dealing with the bidders and advisors directly, would not seem inappropriate. Potentially there could be conflict, but that must be balanced against the reasonable benefits to be obtained. They knew the operations of the business -- what the bidders would be interested in and they were guided by the advisors. They reported to the Special Committee which could make the 'final' decisions and give directions. Potential conflict was minimized by the bail-out packages granted them. From the material before me it would not appear that these management persons acted or behaved inappropriately overall. It would be undesirable to subject each step they took to isolated microscopic inspection. I note in passing that Dodds would have received approximately $1,000.000 in stock and options value extra if the Maple Leaf $29 offer had been accepted as opposed to the Smithfield one; of course no one but Maple Leaf knew how much it would have offered if it had been solicited on December 17th.

49 Dodds' employment agreement entitled him to resign within two years following a change of control transaction with 30 months severance. In *CW Shareholdings*, Blair J. commented that a golden parachute did not eliminate the potential for conflict of interest that exists when a member of senior management negotiates directly with bidders. Here, however. Dodds was not given any assurances by Smithfield of continued employment although he knew that Smithfield intended to leave Schneider's management in place and allow it to operate as an autonomous unit. On the other hand. Dodds was given some assurance of continued employment by Maple Leaf if Schneider was taken over by it. He was

told that he would manage the integration of Schneider for two years, and be a candidate to head the meat operations of the two companies. He was also told that he would retain his salary and be issued additional options in Maple Leaf. In addition, at the time, Dodds held 250,000 options in Schneider with a strike price of $13 and it was believed that Maple Leaf would top any bid that was openly made for Schneider. It seems that if there was any financial bias arising out of Dodds' self interest in continued employment it would have been a bias in favour of Maple Leaf.

50 The appellants also submit that Dodds had a conflict of interest in conducting the negotiations because his loyalties were to the Schneider Family. But the Family did not ask Dodds to negotiate with potential bidders. After Nesbitt Burns suggested that Smithfield might be a potential bidder, Dodds' meetings with Smithfield were at the behest of the Special Committee, or its advisers, Nesbitt Burns and Goodman. Phillips & Vineberg. Farley J. found that the deadline for considering bids had been set by Mida, the Vice-President of Nesbitt Burns and its director of mergers and acquisitions, as an appropriate deadline in order to prevent the process from stalling. He also found that it was appropriate for Dodds to keep the Family informed of the progress of the negotiations since they could veto any sale. Counsel for the appellants strenuously submitted that inasmuch as Dodds advised the Family of the result of his negotiations with Smithfield on December 16th, and did not advise any member of the Special Committee of the negotiations, an inference should be drawn that Dodds' loyalties were to the Family and that this was illustrative of yet another conflict that Dodds had. The evidence indicates that although Dodds did not advise any members of the Special Committee directly on the 16th, he called Mida of Nesbitt Burns, the adviser to the Special Committee. It does not appear that Mida told anyone on the Special Committee of the Smithfield proposal, as the evidence indicates that the Committee was unaware of it until it met on the evening of the 17th. In the circumstances there would appear to be no reason to impute bias to Dodds because of this omission.

51 The appellants also allege that it was Dodds' suggestion to Luter that Smithfield proceed by way of a takeover for any and all shares of Schneider -- as opposed to a plan of arrangement -- and that this suggestion also indicates Dodds' bias against Maple Leaf. The proposal to proceed by way of takeover as opposed to merger was not a suggestion that came from Dodds, but one that had been identified previously as the alternative Luter was prepared to pursue if the Board could not recommend the Smithfield proposal.

52 Farley J. found that Dodds pressed the negotiations with the bidders diligently and did nothing inappropriate. His conclusions are supported by the evidence. There is no merit in this ground of appeal.

Process Arguments

(i) Should the Special Committee have been created?

53 The appellants submit that by creating a special committee, hiring advisers, and setting up a data room, the Family used Schneider's money to better the offer from Maple Leaf, which it was not entitled to do. In addition to being rejected by Farley J., a similar argument was rejected by Montgomery J. in *Olympia and York, supra*, at p. 272. The reason is obvious; the appointment of a special committee is intended to ensure that the interests of those the oppression remedy is intended to protect are not unfairly disregarded or prejudiced. It is clearly in the interests of a company, and of all shareholders, for alternatives to an unsolicited takeover offer to be explored. It might give the shareholders a higher price for their shares. The creation of a Special Committee was part of the process undertaken by the Board to obtain the best transaction available in the circumstances.

(ii) Should the Special Committee have created a data room?

54 The appellants' submission that proprietary confidential information obtained from the data room was a valuable corporate asset that was either given away to the acquiring company or dissipated must also fail. As Farley J. pointed out, access to the data room was essential in order to conduct a market canvass for alternative offers. Other bidders, particularly those who had not operated in the Canadian market, needed to gain an appreciation of market conditions, and of Schneider's business. That could only be obtained with access to Schneider's confidential information.

No alternative bid would have been elicited without access to Schneider's confidential information. Maple Leaf, as a competitor of Schneider for many years, had an appreciation of market conditions and of Schneider's business and did not require further information in order to make its bid.

55 The decision to establish a data room at the company's expense was that of the Special Committee, made with full knowledge of the Family's position that it was not committed to selling. The Board did not seek the approval or the consent of the Family to establish the data room, for the use of information, or for the nature of the confidentiality agreements that were signed with prospective bidders.

56 In creating a data room the Special Committee acted independently and reasonably. The creation of a data room made confidential information available to all bidders as part of a process to get the best transaction available to the shareholders in the circumstances. I see no merit in this ground of appeal.

(iii) Flawed Committee Process

57 The appellants submit that the trial judge ignored or failed to appreciate the evidence given by Ruby, the Chairman of the Special Committee, to the effect that the Special Committee had no involvement in any negotiations with prospective bidders, that Dodds conducted the negotiations, and that the Special Committee did not consider whether Dodds had any conflict of interest. After considering the circumstances under which Dodds acted, I have already concluded that Dodds did not have a conflict of interest.

58 The Special Committee had no prior experience in dealing with a take-over bid and did not have the in-depth knowledge of Schneider that Dodds did. It was therefore appropriate for the Special Committee not to conduct the negotiations with potential bidders directly, Farley J. found that although the Special Committee did try to determine the views of the Family "recognizing its gatekeeper and veto role", there was no evidence that the approval of the Family was sought with respect to any decision taken by the Special Committee. The evidence supports the conclusion that the members of the Special Committee acted independently in the sense that they were free to deal with the impugned transaction on its merits This ground of appeal also fails.

(iv) Should the Special Committee have insisted that Maple Leaf and any other interested party be given an opportunity to make their best and final offer prior to the board of directors of Schneider taking the steps that it did on December 17, 1997 to commit its shares to Smithfield?

59 The appellants submit that the Board was obliged to keep the bidding process alive by going back to Maple Leaf after it received the Smithfield bid on December 17th. This submission has two alternative premises: 1) the Directors could only discharge their duty to act in the best interests of the corporation by conducting an auction of the shares of Schneider: 2) a public expectation had been created by the comments made by the Schneider family that an auction would be held and therefore both the Family and the Board were under a duty to ensure that an auction was conducted.

60 The appellant's first premise is wrong in law. The second is contrary to Farley J.'s findings of fact and those findings are supported by the evidence.

Was there a duty to conduct an auction of the shares of Schneider?

61 The decision in *Revlon Inc. v. MacAndrews & Forbes Holdings Inc.*, 506 A.2d 173 (U.S. Del. Super. 1985), stands for the proposition that if a company is up for sale, the directors have an obligation to conduct an auction of the company's shares. *Revlon Inc.* is not the law in Ontario. In Ontario, an auction need not be held every time there is a change in control of a company.

62 An auction is merely one way to prevent the conflicts of interest that may arise when there is a change of control by requiring that directors act in a neutral manner toward a number of bidders: *Barkan v. Amsted Industries Inc.*, 567 A.2d 1279 (U.S. Del. Super. 1989) at 1286 . The more recent *Paramount* decision in the United States, *supra*, at 43-45

has recast the obligation of directors when there is a bid for change of control as an obligation to seek the best value reasonably available to shareholders in the circumstances. This is a more flexible standard, which recognizes that the particular circumstances are important in determining the best transaction available, and that a board is not limited to considering only the amount of cash or consideration involved as would be the case with an auction: *Paramount, supra* at 44. There is no single blueprint that directors must follow. Although the decision in *Paramount* and the other decisions of the courts in Delaware to which I have referred are not the law of Ontario, they can, however, offer some guidance.

63 When it becomes clear that a company is for sale and there are several bidders, an auction is an appropriate mechanism to ensure that the board of a target company acts in a neutral manner to achieve the best value reasonably available to shareholders in the circumstances. When the board has received a single offer and has no reliable grounds upon which to judge its adequacy, a canvass of the market to determine if higher bids may be elicited is appropriate, and may be necessary: *Barkan, supra*, at 1287, citing *Fort Howard Corp. Shareholders Litigation, Re*, Doc. Civ. A. 9991 (U.S. Del. Ch. August 8, 1998).

64 The Family did not seek to sell its controlling interest in Schneider. The Board received an offer from Maple Leaf that it felt was inadequate, but, in the final analysis, the best way to judge its adequacy was to determine if higher bids could be elicited through a market canvass. The fact that a market canvass was conducted did not mean that the Family would agree to sell its stake. Indeed, Farley J. found as a fact that the Family's decision to sell was highly conditional on a satisfactory offer being received.

65 The appellant submits that there was considerable evidence indicating that the Schneider Family had by December 17th, if not before, concluded that a sale of its shares was inevitable. Having undertaken a market canvass, however, there was no obligation on the Special Committee to turn this canvass into an auction, particularly because to do so was to assume the risk that the competing offers that the market canvass had generated might be withdrawn. There was no obligation on the Special Committee or the Board to go back to Maple Leaf on December 17th and ask it to make another offer. A market canvass and not an auction was being conducted; the Special Committee and the Board only had a short time within which to consider Maple Leafs offer; Maple Leaf had already been asked to make an appropriate offer and there was no certainty it would make a higher bid. There was an obligation on the Special Committee and the directors to consider the bids which their market canvass had realized in addition to Maple Leafs bid. Farley J. found Maple Leaf knew, or should have known, that the bidding process was almost over when it made its $22 per share bid. Maple Leafs board had authorized the issuance of enough Maple Leaf shares to finance a $29 a share bid for Schneider before the bidding process entered its final stage. Maple Leaf was nonetheless content to let its $22 bid stand despite knowing that there were competing bids that might be accepted in preference to its own, and despite the fact that Maple Leaf's board had authorized a higher $29 bid. This was a risk Maple Leaf chose to assume.

Was there a public expectation created by the Family that an auction would be held?

66 Conduct which disregards the *interests* of any shareholder and not simply a shareholder's legal rights will infringe s. 248 of the OBCA. This is because the oppression remedy is basically an equitable remedy and the court has jurisdiction to find an action is oppressive, unfairly prejudicial, or unfairly taken in disregard of the interests of a security holder if it is wrongful, even if it is not actually unlawful: *Westfair Foods Ltd. v. Watt*, [1990] 4 W.W.R. 685 (Alta. Q.B.), aff'd [1991] 4 W.W.R. 695 (Alta. C.A.), leave to appeal refused [1992] 1 W.W.R. lxv (S.C.C.).

67 A statement made to shareholders in a press release can create a public expectation that is deserving of protection through the oppression provisions of the *OBCA*. As Carthy J.A. stated in *Themadel Foundation, supra*, at 753:

> The public pronouncements of corporations, particularly those that are publicly traded, become its commitments to shareholders within the range of reasonable expectations that are objectively aroused.

68 While s. 248 protects the legitimate expectations of shareholders, those expectations must be reasonable in the circumstances and reasonableness is to be ascertained on an objective basis.[5] The interests of the shareholders of a

company are intertwined with the expectations that have been created by the company's principals: *Naneff v. Con-Crete Holdings Ltd.* (1995), 23 O.R. (3d) 481 (Ont. C.A.). Therefore, the question is whether the statements made by the Family, and widely reported in press releases issued in response to Maple Leaf's bids, created a reasonable expectation that an auction would be held. Whether or not a reasonable expectation has been created is a question of fact: *Arthur v. Signum Communications Ltd.* (July 29, 1993), Doc. 123/91 (Ont. Div. Ct.). Campbell J., for the court, at paras. 6-7. After examining the press releases and the evidence. Farley J. found that any expectations of the claimants, who were non-Family shareholders, were not reasonable or founded in fact.

69 A summary of his findings on this point is as follows:

- the Family's position on selling its controlling shareholding in Schneider was always conditional to a high degree. The Family only said that they "might consider" selling. The conditional nature of the Family's position was always clearly expressed by the Board in its public statements.

- it was inappropriate for Maple Leaf to ignore the plain meaning of the public statements made by the Family and the Board. Maple Leaf "wished" that there was an unrestricted auction for Schneider but in fact there never was.

- the claimants had not proved that their reasonable expectations were thwarted. "When the gatekeeper shareholder merely indicates that it 'might consider' accepting a more financially attractive offer, then the shareholders are speculating that a deal on that basis may come to pass in which they could participate.

70 There was more than adequate evidence to support these findings and they cannot be disturbed.

71 Inasmuch as there was no reasonable expectation on the part of the non-Family shareholders that an auction would be held after receiving the last Smithfield bid, the Special Committee was not obliged to give Maple Leaf an opportunity to make a third bid for Schneider's shares.

Was the course of action and the advice given by the Special Committee in the best interests of Schneider and its shareholders? Should the Special Committee and the Board of Directors have refused to waive the standstill provisions in the confidentiality agreement with Smithfield?

72 The appellants allege that the advice given by the Special Committee to the Board of Schneider was not in Schneider's best interests or those of its shareholders. They submit that the Special Committee should have refused to waive the standstill provisions in the confidentiality agreement with Schneider, thereby preventing the agreement between the Family and Smithfield. The appellants also submit that if the Board of Schneider could not enter into a share exchange with Smithfield because of fairness concerns it could not agree to a takeover bid. These submissions are really alternative ways of saying that the transaction with Smithfield was unfair to the non-Family shareholders, that it was not in the best interests of the company.

73 If the Smithfield offer can reasonably be considered to be the best available offer in the circumstances, then the Smithfield offer was not unfair or contrary to the best interests of the company. This is also essentially a fact driven question on which Farley J. made the following findings:

- the Smithfield offer was solicited by Schneider. Smithfield, a reluctant suitor, had to be "coaxed" to make a bid. Smithfield imposed a "no-shop" condition on its offer to the Schneider Family and did not want to haggle.

- there was no breach of confidence in the communications between Smithfield, and the Schneider Board and the Family. The spirit of the standstill provision between Smithfield and Schneider was honoured. Confidential information was used appropriately in the best interests of the shareholders. At all times the Schneider Board remained in control of the process dealing with the Smithfield offer.

• it was reasonable for the Board to accommodate a transaction between Smithfield and the Family by waiving the standstill provision contained in the Smithfield confidentiality agreement in view of advice received that the share price of Schneider would fall back to a range of $18 to $20 per share in the absence of a change of control transaction.

• Maple Leaf could not have made an offer that would have been satisfactory to the Schneider Family at that time.

• the Board exercised their powers and discharged their duties honestly and in good faith.

• the Board pursued all available opportunities to maximize shareholder value and achieved reasonable results for all of the shareholders of Schneider.

• it was unfair to say that the Special Committee had the Family's interests uppermost in its mind not those of the shareholders generally, or the non-Family shareholders specifically. It was beyond the power of the Special Committee to insist that the Family give up its veto power and the Special Committee realized this.

74 As Farley J. emphasized, one of the particular circumstances having a bearing on a board of directors' attempts to obtain the best deal available in the circumstances was whether the company has a controlling shareholder. For example, in *Paramount, supra*, control of the corporation was not vested in a single person, entity, or group, but was widely held by a number of unaffiliated shareholders. In that case, the proposed sale of shares represented a premium for the change and consolidation of control of the company in a group that would have the power to materially alter the interests of the widely dispersed shareholders. Here, the control premium for the shares of Schneider belongs to the Family. The unaffiliated shareholders do not own, and are not giving up, the power to control the company's future.

75 Another distinction between this case and *Paramount* is that the offer from Maple Leaf, which was before the Special Committee at the time it was asked to make its decision, was considerably less than the Smithfield offer. In coming to its conclusion that it was not in the interests of the non-Family shareholders to prevent the Family from entering into a lockup agreement with Smithfield the Special Committee considered, among other things:

a) that the shares would likely trade in the $18 to $20 range if no sale was effected;

b) the position of the Family that it would not accept the Maple Leaf offer at $22 or the Booth Creek offer -- or indeed any other offers from them; [6]

c) that Smithfield would publicly withdraw its offer if the offer was shopped and, if this happened, the amount that Maple Leaf would be prepared to offer was problematic.

76 While Smithfield's offer was not within the range that Nesbitt Burns had placed on the shares as fair value, "'a decent respect for reality forces one to admit that ... advice [of an investment banker] is frequently a pale substitute for the dependable information that a canvass of the relevant market can provide'": *Barkan, supra*, at 1287. It was widely known that a change of control was being considered, and few rival bids were forthcoming over an extended period of time: these facts support the decision to proceed with the impugned transaction.

77 The Board acted on the advice of the Special Committee in agreeing to facilitate the Smithfield bid by passing a resolution waiving the standstill provision, thereby allowing Smithfield to bid and to enter into the lock-up agreement with the Schneider Family. Unless another bid was received that was not conditional on the tender of any of the Schneider Family shares, which was highly unlikely, this decision by the Board had the effect of making the Smithfield bid the only one which would effectively be available to the shareholders. Implicit in the steps taken by the Board was a decision by the Board that the Smithfield bid was in the best interests of all the shareholders and therefore a bid which the Board could recommend to the shareholders.

78 The Special Committee was entitled to make, and did make, business and negotiating judgment calls which, having regard to the interests of the non-Family shareholders, were reasonable in the intense and time-limit-driven context. The

deal with Smithfield was the only deal that the controlling shareholder was willing to consider. With respect to the alleged pre-empting of the process by not going back to Maple Leaf, Farley, J. stated:

> ...[I]t appears that this merely prevented a further round of enquiry of Booth [Creek] and Maple Leaf which may or may not have elicited a higher bid than Smithfield whose last bid was tested.

If Maple Leaf was given an opportunity to top the Smithfield bid and that bid was then publicly withdrawn, then there was no guarantee that Maple Leaf would make a higher offer. There was no alternative bid which was definitely available and clearly more beneficial to Schneider and all its shareholders than the Smithfield bid. The Board acted on the advice of the Special Committee. The advice given and accepted was reasonable at the time and fair to the non-Family shareholders.

79 I would dismiss the first main ground of appeal.

The Coattail Provisions

80 There are three sub-issues here:

a) whether Farley J. erred in his interpretation of the coattail provisions;

b) whether, as held by Farley J., the filing of anti-conversion certificates by Schneider prevented the coattail provisions from being triggered; and

c) whether Maple Leaf's failure to disclose the exclusionary nature of its offers in the take-over bid circulars and notices of variation is an omission of a material fact, and if so, what the remedy should be.

Did Farley J. interpret the coattail provisions correctly

(i) Facts re interpretation of coattail provisions

81 Coattail provisions are designed to ensure that if the common voting shareholders wish to accept an offer that will lead to a change in control and if the price or terms offered to the common voting shareholders are more favourable than those offered to the holders of non-voting shares, the non-voting shareholders get an equal opportunity to participate in any change of control premium.

82 The provisions work in the following way. If the holders of restricted shares, such as non-voting shares, are excluded from participating in the common voting share takeover bid, they will then be given a right of conversion of their restricted or non-voting shares into common voting shares. Coattail provisions are intended to encourage non-exclusionary bids. When triggered, the non-voting shareholders then have the opportunity to participate in the take-over bid.

83 The Schneider Family proposed that a coattail provision be added to its articles of incorporation in a tradition of "fair dealing" in 1988, even though a company listed on the Toronto Stock Exchange ("TSE") was not required to have a coattail provision at that time. The Schneider coattails are consistent with the present TSE policy requirements. Mr. MacKay, Schneider's lawyer at the time, obtained the particular wording for the coattail from a precedent provided by the TSE. It was intended that the Class A shareholders would be entitled to share in the control premium only if the requisite number of common voting shareholders accepted the offer and the premium was in fact paid to the holders of common shares. Instead, in the coattail provision provided by the TSE as a precedent, and adopted by Schneider, even if it was apparent that a change of control would not take place because a sufficient number of common shares had not been acquired or purchased pursuant to the offer to the common shareholders, the company making the offer would have to take up and pay for all the shares held by the Class A shareholders who tendered to the offer.

84 Read literally, the coattail provision provided that if even a single common share was tendered to the offer for the common shares, the company making the offer would have to pay for all the Class A shares tendered whether or not any Class A shares were actually taken up and purchased or acquired. This is because the definition of exclusionary offer in paragraph 12(e) of the articles of Schneider uses the word "tendered" as opposed to the word "purchased" or "acquired".

85 Paragraph 12(e) defines an exclusionary offer as follows:

> (e) "Exclusionary Offer" means an offer to purchase common shares of the Corporation that:
>
> (i) must by reason of applicable securities legislation ... be made to all or substantially all holders of common shares...; and
>
> (ii) is not made concurrently with an offer to purchase Class A Non-Voting shares that is identical to the offer to purchase common shares in terms of price per share and percentage of outstanding shares to be taken up exclusive of shares owned immediately prior to the offer by the Offeror and in all other material respects *and that has no condition attached other than the right not to take up and pay for shares tendered if no shares are* ***tendered*** *pursuant to the offer for common shares* [Emphasis added]

86 If the word *acquired* or *purchased* had been used in the definition of "exclusionary offer" instead of *tendered* there would not have been a problem with the coattail provision. But Maple Leaf's lawyers recognized the problem. Maple Leaf's offer to purchase the common shares of Schneider was made concurrently with its offer to purchase the Class A shares. The offer to the Class A shareholders contained a condition entitling Maple Leaf not to take up and pay for any Class A shares deposited if Maple Leaf did not *acquire* any common shares pursuant to the offer to purchase common voting shares. This was not the condition permitted under the coattail provisions. The coattail provisions gave the right not to take up and pay for Class A shares if no common shares were *tendered.* Because the condition attaching to its Class A shares was different, Maple Leaf submits that its offer to the common shareholders was an exclusionary one.

(ii) Findings of The Trial Judge

87 With respect to the coattail provision in the articles of Schneider, Farley J. made the following findings:

- the so called "flaw" in the coattail was recognized by Maple Leaf well before it made its offer;
- a literal or technical interpretation of the wording of the Schneider coattail would be impractical and lead to a commercial absurdity;
- when Maple Leaf made its offer, the intention and the effect of the conditions it imposed in its offer was to make its offers identical for both the voting and non-voting shares of Schneider;
- Maple Leaf did not disclose to the shareholders that its offer was exclusionary in its original take-over bid circular or in any subsequent amendment to that circular prior to the announcement of the Smithfield lock-up agreement with Schneider on December 19, 1997. It was not until January 8, 1998, that Maple Leaf issued a Notice of Variation which disclosed to all shareholders for the first time its belief that its Offer was exclusionary;
- Schneider's directors, on the other hand, described the Maple Leaf offer as a non-exclusionary offer in the directors' circular which was submitted to shareholders on November 23, 1997;
- he did not accept any of Maple Leaf's reasons for failing to disclose its belief that its offer was exclusionary.

88 With respect to Maple Leaf's failure to disclose its belief that it had made a non-exclusionary offer, the trial judge made the following findings:

• Maple Leaf put too narrow a focus on its obligation to disclose that its bid was designed to be exclusionary. It was inappropriate and misleading for Maple Leaf not to set out in an obvious fashion the information which a reasonable shareholder requires to make an informed decision;

• Maple Leaf "lay in the weeds" about its interpretation of the coattail, notwithstanding its knowledge of the Schneider directors' statement that Maple Leaf's offer was non-exclusionary. Maple Leaf did so because it did not want other competitive offerors to "twig" to its scheme;

• the technical interpretation now urged by Maple Leaf was not consistent with the intention of instituting the coattail at any time leading up to and including the time of the takeover.

89 In view of his findings, Farley J. held that the word "tender" should be construed as "tendered and taken up" thereby embodying the concept of "acquired" or "purchased".

Discussion

90 The following principles are of assistance in determining whether Farley J. correctly interpreted the coattail provisions.

• The interpretation of a word or words is not a technical exercise undertaken in isolation from the objective or purpose sought to be accomplished: See *Dreidger on the Construction of Statutes* 3rd ed. (Toronto: Butterworths, 1994) at 131; thus, where giving a word its ordinary grammatical construction would lead to a contradiction of its apparent purpose or to a commercial absurdity, a construction may be put upon it which modifies the meaning of the word: P. St. J. Langan, *Maxwell on the Interpretation of Statutes* 12th ed. (London: Sweet & Maxwell, 1969), at p. 228.

• A purposive approach is to be used whether one is interpreting a provision of a statute, a contract or other form of private legal document. In many respects the problems are the same in all three. A document is also a form of "sub-legislation" respecting those governed by its provisions: see Morden, "The Partnership of Bench and Bar" (1982), 16 *Law Soc. Gaz.* 46, and cases cited therein at 89-95; *Dreidger on the Construction of Statutes*, 3rd ed. (Toronto: Butterworths, 1994) at 131; *Maxwell on the Interpretation of Statutes*, 12th ed. (London: Sweet & Maxwell, 1969), at 228.

• The words of a statute to be interpreted are to be read in their entire context and in their grammatical and ordinary sense harmoniously with the scheme of the Act, the object of the Act and the intention of Parliament: *Rizzo & Rizzo Shoes Ltd., Re*, [1998] 1 S.C.R. 27 (S.C.C.). (This decision holds that although the literal reading of the words in the *Employment Standards Act* entitling an employee to severance, termination or vacation pay upon termination by the employer would not include the employer's bankruptcy, when the words are examined in their entire context they must be interpreted to include a termination *resulting from the bankruptcy of the employer*.) So, too, here, the wording of the coattail provision must be given an interpretation which accords with its object and the intention of the framers of the provision.

• The interpretation of a coattail provision must be viewed objectively and as a reasonably prudent business person would view it: *CW Acquisition Inc. v. Cathton Holdings Ltd.* (1997), 88 B.C.A.C. 264 (B.C. C.A.) at 272.

• When the public interest is involved, evidence with respect to the understanding and intention of the provision is admissible to assist in determining whether a proposed interpretation is consistent with the public interest: *Canadian Tire Corp. v. C.T.C. Dealer Holdings Ltd.* (1987), 35 B.L.R. 117 (Ont. Div. Ct.) at 143-144.

91 The purpose of adopting a coattail provision is to discourage exclusionary offers, whereas a literal reading of Schneider's coattail provision gives the opposite effect. Certainty of meaning is of paramount importance in commercial

transactions that affect the public. Those considering whether or not to tender to an offer to purchase their shares must know what investment decision they are making: See *CW Acquisition Inc., supra*, at 272-73. In this instance, it appeared to the shareholders that the offers were the same because the amount to be paid to both classes of shareholders was the same. Maple Leaf understood how its offers would be perceived. If, instead, Maple Leaf was of the opinion that its offer was exclusionary, it could have said in its offering circular that it intended to apply to the appropriate authorities to have the issue of whether or not the offer was exclusionary determined in court as was done in *CW Shareholdings, supra*, Maple Leaf did not.

92 The interpretation of Maple Leaf's offers adopted by Farley J. is consistent with the way a reasonably prudent business person would construe the offer. The outcome he reaches is consistent with public expectations and is commercially sound. It employs a purposive approach. Farley J. did not err in holding that the Maple Leaf offer for common shares was not an "exclusionary offer" and that the coattail provisions in Schneider's articles had not been triggered.

The Anti-Conversion Certificates

Did Farley J. err in his conclusion that an effective anti-conversion certificate had been filed?

93 The articles of Schneider provide that conversion of the Class A non-voting shares into common voting shares does not arise, even if an offer is an exclusionary offer, if the holders of 50% or more of the common shares file a certificate with the transfer agent and the secretary of the corporation, under section 16, indicating that they will not accept an exclusionary offer without giving the transfer agent written notice of their intention. Such a certificate can be a standing certificate filed before an offer is made (a 16(a) certificate), or a certificate filed within seven days of the making of an exclusionary offer (a 16(b) certificate). It is only if no certificate under section 16 is filed that conversion rights arise.

94 The purpose of the filing of a s. 16(a) certificate with the transfer agent is to have an outside entity receive confirmation of the controlling shareholder's intention concerning exclusionary bids. Unless and until a bid for change of control of the company is made, the transfer agent does not have to take any further steps. As soon as possible after the seventh day after an offer is received, articles 17 and 18 of Schneider's articles require the transfer agent to send holders of Class A non-voting shares a notice advising them whether they are entitled to convert their Class A non-voting shares into common shares (presumably on the basis whether a s. 16(a) or s. 16(b) certificate is filed) and the reasons they are, or are not, entitled to convert their shares. The manifest purpose of the provision is to make the Class A non-voting shareholders aware of their rights.

95 Farley J. found as a fact that when the coattails were adopted, Schneider's secretary filed a 16(a) certificate under cover of May 2, 1988, with the transfer agent of Schneider which, at the time, was the Canada Trust Company.

96 Royal Trust Corporation succeeded Canada Trust as transfer agent for Schneider and later sold its transfer agency business to a company, which became CIBC Mellon Trust Company. Schneider's current transfer agent. Schneider did not file a new 16(a) certificate with Royal Trust when it became its transfer agent. CIBC Mellon has no record of having received the 1988 certificate from any source prior to receiving it from Goodman Phillips & Vineberg on December 29, 1997 -- after the Maple Leaf offers had been made. A representative of CIBC Mellon testified that he would not expect Canada Trust to have forwarded the April 29, 1988 certificate to Royal Trust or its successors because CIBC Mellon's practice, and the practice in the industry generally, was not to do so. He testified that this is the type of document a company would redeliver. Mr. MacKay, however, testified that he had arranged for Canada Trust to deliver this certificate to Royal Trust. Farley J. accepted MacKay's evidence on this point. Assuming the certificate was received by Royal Trust, there was no evidence what Royal Trust did with the certificate once Royal Trust sold its business to CIBC Mellon.

97 Article 16 of Schneider simply states that the certificate is to be delivered to "the transfer agent". Farley J. stated:

> ...the coattails provisions as provided for in the TSE precedent and adopted by Schneider provides for the certificate to be given to the transfer agent and to the secretary of Schneider. It does not say that it is to be given to the Secretary "for the time being". The context of the delivery of the certificate is that it be given to both at the same [general] time.

98 The articles of Schneider do not require the controlling shareholder to redeliver a s. 16(a) certificate when the company changes transfer agents. Farley J. held that in the circumstances the s. 16(a) certificate did not have to be redelivered by Schneider. I agree with this interpretation. The role of a transfer agent is to maintain the records of a corporation. When there is a change in transfer agent, as with a change in trustee, it does not deprive the shareholders of the effect of the document. The notice to the original transfer agent is valid. See *Slattery v. Slattery*, [1945] O.R. 811 (Ont. C.A.) at 819.

99 Even if the Maple Leaf bid was an exclusionary bid the 16(a) certificate delivered in 1988 was effective and blocked the conversion of the Class A shares into common voting shares.

100 There is a further alternative argument raised in relation to the anti-conversion certificates. It is whether the filing of a s. 16(b) certificate after Maple Leaf's bid was made was effective.

101 Following notice that Maple Leaf's holding company SCH proposed to make a bid for Schneider. Eric Schneider delivered to himself as Corporate Secretary on November 11, 1997 as. 16(b) certificate, but it was not provided to CIBC Mellon until December 22, 1997 and was therefore ineffective because it was not delivered within seven days of the "offer date" by SCH. On December 12, 1997, Maple Leaf, and not its holding company SCH, made a bid for the shares of Schneider and increased its offer to $22 a share. In addition, for the first time shares of Maple Leaf were offered as partial consideration for the shares of Schneider. Schneider again filed a s. 16(b) anti-conversion certificate dated December 19.

102 Farley J. found that the Family had a consistent intention to implement an effective anti-conversion certificate against any exclusionary offer. He acknowledged that under the ordinary principles of contract law a change in the essential terms of the offer such as occurred here between the November 11 offer and the December 12 offer, would be a new offer. He held, however, that the December 12 bid by Maple Leaf was not a new offer having regard to the definition of "Exclusionary Offer" contained in article 12(e)(ii) of the coattails provision which says in part:

> ...[I]f an offer to purchase common shares is not an Exclusionary Offer ... the varying of any term of such offer shall be deemed to constitute the making of a new offer unless an identical variation concurrently is made to the corresponding offer to purchase Class A Non-Voting shares;

103 I am of the opinion that Farley J. erred in holding that the December 12th offer by Maple Leaf was not a new offer on the basis of Article 12(e)(ii). The words construed by Farley J. are a saving provision. The saving provision presupposes that an offer was originally non-exclusionary and the offer is varied with the result that unequal terms are offered to the common and Class A shareholders. In those circumstances the offer will be considered to be a new offer which is exclusionary. The deeming provision of article 12(e)(ii) does not deprive the controlling shareholder of the substantive right in article 16(b) to file an anti-conversion certificate if the original offer made is exclusionary and the subsequent offer is also exclusionary but completely different as to its terms. This interpretation is supported by regard to Article 16(b). Under Article 16(b), the anti-conversion certificate must be delivered within seven days after "the Offer Date". The "Offer Date" is defined in article 12(g):

> Offer Date means the date on which an Exclusionary Offer is made.

Thus, whenever an offer which is exclusionary is made, Schneider has seven days to deliver an anti-conversion certificate.

104 Based on both the wording of the articles and on general contract principles, the offer of December 12th was a new offer and the 16(b) anti-conversion certificate filed was effective.

The Omission of Maple Leaf to state that its offers were exclusionary in its offering circular and the effect, if any, of such omission

105 Farley J. did not find it necessary to decide this issue and I am of the opinion that it is unnecessary to do so in view of my conclusions concerning the other issues raised.

Disposition

106 For the reasons given, the appeals from the judgment of Farley J. are dismissed. Because I have held that Farley J. did not err in holding that the offer to purchase common shares made by Maple Leaf to shareholders of Schneider was not an exclusionary offer within the meaning of the articles of Schneider, it was not necessary to deal with the cross-appeals by the Family. I have, however, dealt with one aspect of the cross-appeals, namely, the effectiveness of the anti-conversion certificates. If it were necessary to do so. I would allow the cross-appeal to the extent necessary to grant relief in accordance with paragraph (a) of the Family's notice of cross-appeal. The balance of the cross-appeal has not been considered and is dismissed. If necessary, I would also allow the cross-appeal of Smithfield which relates to the same point, namely, the effectiveness of the anti-conversion certificates.

107 Counsel have asked to make further submissions concerning costs. I would invite the respondents to file their submissions in writing within 15 days from the release of these reasons and the appellants 10 days thereafter. Reply submissions respecting costs, if any, should be filed within a further 5 days.

Appeal dismissed.

APPENDIX

Business Corporations Act, R.S.C. 1995, c. B.16

134. (1) Standard of care, etc., of directors, etc.--Every director and officer of a corporation in exercising his or her powers and discharging his or her duties shall,

(a) act honestly and in good faith with a view to the best interests of the corporation; and

(b) exercise the care, diligence and skill that a reasonably prudent person would exercise in comparable circumstances.

(2) Duty to comply with Act. etc. -- Every director and officer of a corporation shall comply with this Act, the regulations, articles, by-laws and any unanimous shareholders agreement.

248. (1) Oppression remedy -- A complainant and, in the case of an offering corporation, the Commission may apply to the court for an order under this section.

(2) Idem -- Where, upon an application under subsection (1), the court is satisfied that in respect of a corporation or any of its affiliates.

(a) any act or omission of the corporation or any of its affiliates effects or threatens to effect a result;

(b) the business or affairs of the corporation or any of its affiliates are, have been or are threatened to be carried on or conducted in a manner; or

(c) the powers of the directors of the corporation or any of its affiliates are, have been or are threatened to be exercised in a manner,

that is oppressive or unfairly prejudicial to or that unfairly disregards the interests of any security holder, creditor, director or officer of the corporation, the court may make an order to rectify the matters complained of.

(3) Court order -- In connection with an application under this section, the court may make any interim or final order it thinks fit including, without limiting the generality of the foregoing.

(a) an order restraining the conduct complained of;

(b) an order appointing a receiver or receiver-manager;

(c) an order to regulate a corporation's affairs by amending the articles or by-laws or creating or amending a unanimous shareholder agreement;

(d) an order directing an issue or exchange of securities;

(e) an order appointing directors in place of or in addition to all or any of the directors then in office;

(f) an order directing a corporation, subject to subsection (6), or any other person, to purchase securities of a security holder;

(g) an order directing a corporation, subject to subsection (6), of any other person, to pay to a security holder any part of the money paid by the security holder for securities;

(h) an order varying or setting aside a transaction or contract to which a corporation is a party and compensating the corporation or any other party to the transaction or contract;

(i) an order requiring a corporation, within a time specified by the court, to produce to the court or an interested person financial statements in the form required by section 154 or an accounting in such other form as the court may determine;

(j) an order compensating an aggrieved person;

(k) an order directing rectification of the registers or other records of a corporation under section 250;

(l) an order winding up the corporation under section 207;

(m) an order directing an investigation under Part XIII be made; and

(n) an order requiring the trial of any issue.

(4) Idem -- Where an order made under this section directs amendment of the articles or by-laws of a corporation.

(a) the directors shall forthwith comply with subsection 186 (4); and

(b) no other amendment to the articles or by-laws shall be made without the consent of the court, until the court otherwise orders.

(5) Shareholder may not dissent -- A shareholder is not entitled to dissent under section 185 if an amendment to the articles is effected under this section.

(6) Where corporation prohibited from paying shareholder -- A corporation shall not make a payment to a shareholder under clause (3) (f) or (g) if there are reasonable grounds for believing that.

(a) the corporation is or, after the payment, would be unable to pay its liabilities as they become due; or

(b) the realizable value of the corporation's assets would thereby be less than the aggregate of its liabilities.

Footnotes

* A corrigendum was delivered by the court on October 27, 1998 stating changes that have been incorporated herein.

1 There are four branches of the Schneider Family. In this appeal, "Family" refers to the collective family holding company J.M. Schneider Family Holdings Limited (Family Holdings): the four individual family holding companies (Harbour Glen Securities Limited. Kinspan Investments Limited, Laurel Ridge Investments Limited, and Jadebridge Holdings Limited); and seven of the eight Family members who serve as directors of Family Holdings. Herbert J. Schneider, Frederick P. Schneider, Jean M. Hawkings, Betty L. Schneider, Anne Fontana, Eric Schneider, and Bruce Hawkings.

2 For the sake of convenience I will refer to s.248 as the "oppression-remedy". For ease of reference the text of ss. 134 and 248 is attached to these reasons as an appendix.

3 Reversing the burden of proof was rejected by Farley J. in this case. He declined to adopt the test in this case and to place the burden of proof on the directors. He indicated that the rights of shareholders in Ontario were protected by s.248 of the OBCA and he would apply it. The enhanced scrutiny standard was also rejected by Blair J. in *CW Shareholdings Inc., supra,* at 27, in dealing with an application under the *Canad[a] Business Corporations Act* to set aside defensive measures taken by a company respecting a takeover. He commented that to the extent "enhanced scrutiny" imposed the initial evidentiary burden on the directors of a target company to justify their actions and their business decisions it went too far and did not represent the law in Ontario. While s.248 of the OBCA does not clearly state on whom the onus lies, the use of the term "complainant" in s.248 and the broad definition of a "complainant", which includes any other person whom the court considers a proper person, suggest that the onus is on the person alleging that the directors have unfairly prejudiced, disregarded, or acted oppressively towards the person. In many cases the facts necessary to found such a complaint will be in the knowledge of the person alleging them and the burden of adducing evidence on those facts should rest on that person. The cases arising under these sections are, however, fact specific. In cases where trust property is the subject of the litigation and it is alleged that a personal benefit has been given to members of the Board as a result of its actions, the Board may bear the burden of adducing evidence as to the nature of the transaction.

4 There are fewer and fewer situations today where the resolution of the question turns on the onus of proof. See the comments of Sopinka J. in *Amchem Products Inc. v. British Columbia (Workers' Compensation Board)*, [1993] 1 S.C.R. 897 (S.C.C.).

5 It is worthwhile nothing however that on a subjective basis no shareholder testified that any public pronouncement made by the family created an expectation that an auction would be conducted.

6 Recall that the Maple Leaf and the Booth Creek offers were worth considerably less to the Family and to the non-Family shareholders, provided they were in a similar tax position to the family. Smithfield's share exchange offer was worth approximately $4 a share more to them.

End of Document

Tab 2

1998 CarswellOnt 1891
Ontario Court of Justice, General Division [Commercial List]

CW Shareholdings Inc. v. WIC Western International Communications Ltd.

1998 CarswellOnt 1891, [1998] O.J. No. 1886, 160 D.L.R. (4th) 131, 38 B.L.R. (2d) 196, 39 O.R. (3d) 755, 61 O.T.C. 81, 79 A.C.W.S. (3d) 518

CW Shareholdings Inc., Applicant, and WIC Western International Communications Ltd., Shaw Communications Inc., Charles R. Allard, Robert G. Brodie, Peter Classon, Rhys T. Eyton, Michael G. Francis, Edmondo R. Giacomelli, John S. Lacey, Wendy Leaney, Robert A. Manning, Roderick A. McLennan, Garth Olmstead, Harold A. Roozen, J. Edward Smith, Respondents

Blair J.

Judgment: May 11, 1998
Docket: 98-CL-2821

Counsel: *Sheila R. Block*, *James Tory* and *Linda Plumpton*, for the applicant CW Shareholdings Inc.
Robert W. Staley, *Robyn M. Bell* and *D. Michael Brown*, for the respondents WIC Western International Communications Ltd. and its directors.
Neil Finkelstein, *Jeremy Freedman*, *J.P. Bisnaire* and *Vincent Mercier* for the respondents Shaw Communications Inc.

Subject: Corporate and Commercial

APPLICATION by shareholder for oppression remedy.

***Blair J.*:**

Part I - Overview and Background

Overview

1 In the maelstrom of a takeover bid process there are often a number of rights-related ships tossing about simultaneously on the turbulent waters. This proceeding is one of them.

2 Can West Global Communications Corp. and Shaw Communications Inc. (both large Canadian public corporations with interests in the broadcasting and communications fields, albeit with slightly different emphases) are locked in a takeover bid battle for the prize of WIC Western International Communications Ltd. WIC is another large Canadian public corporation with interests in broadcasting and communication enterprises (television and radio, primarily). Both CanWest - through a subsidiary, CW Shareholdings Inc. - and Shaw Communications are at present significant shareholders of WIC. CanWest is the largest holder of WIC equity, through its 35.7% ownership of non-voting Class B shares. Shaw Communications has recently acquired 49.96% of WIC's Class voting shares, and increased its holdings of Class B shares to approximately 14%.

3 Faced with this recent development in mid-March of this year, CanWest decided to launch a takeover bid, and on March 24, 1998 it announced an Offer to acquire all of WIC's Class A and Class B shares at a price of $39.00 per share. WIC's reaction was negative. Its board of directors responded initially on April 3rd with a Directors' Circular advising shareholders not to accept the CanWest offer and stating that the directors intended to take steps to maximize shareholder value and to treat all potential suitors equally. At about the same time, the WIC directors implemented what

they referred to as a "shareholders' rights plan", and what CanWest characterizes as a "poison pill", which had the effect of impeding CanWest's ability to take up shares tendered to its bid, and which was designed as well to buy the directors more time to respond to the situation. However it was characterized, this initiative was struck down after a joint hearing of the Ontario, Alberta and British Columbia Securities Commissions, on April 9, 1998. Although there were various expressions of interest none led to a competing bid, and over the Easter Weekend of April 10-12, the latent (but always existing) interest of Shaw Communications came to life. After a 2 day period of active and intense negotiations beginning early in the morning of April 15, 1998, Shaw Communications announced on April 17 that it had agreed to make an Offer for all of the WIC Class B shares.

4 It is this Offer which is the subject of attack in these proceedings.

5 The Shaw Communications Offer is at $43.50 per share (by way of 35% cash and 65% Shaw Class B Shares) and it carries with it - in exchange for the making of the bid - a Pre-Acquisition Agreement which entitles Shaw Communications to a "break fee" of $30 million in the event that its bid is unsuccessful and which, in addition, grants to Shaw Communications an option to purchase WIC's radio assets (which, everyone appears to concede - in one fashion or another - are of considerable interest and value to those in the radio broadcasting business in Canada). These two "inducements", and the process through which they were arrive at, form the gravamen of CanWest's complaint.

6 CanWest applies for relief under the "oppression remedy" provisions of s. 241 of the *Canada Business Corporations Act*, R.S.C. 1985, c. C-44 as amended ("*CBCA*"), seeking to have the Pre-Acquisition Agreement set aside. It submits that the WIC directors have exercised their powers in a manner that is contrary to their statutory and fiduciary duties in takeover bid situations, and that this failure has resulted in prejudice to CanWest as a WIC shareholder (in common with all other WIC Class B shareholders), justifying relief under the oppression remedy. WIC and Shaw Communications argue, on the other hand, that what the WIC directors have done is perfectly proper and has resulted in a competing Offer which is $4.50 per share (about $115 million overall) better than the CanWest Offer, and that CanWest is simply a "bitter bidder" [1], coming to court because it is unhappy the WIC board has successfully initiated an active, live and successful auction for WIC's shares.

7 That is what these proceedings are about. Is CanWest simply a takeover bid wolf dressed in the comforting lambs cloak of an oppressed shareholder? Or is the WIC/Shaw Communications agreement the product of a flawed directors' process in which an existing shareholder with "insider" characteristics has been granted a combination of inducements that are unreasonable in their generosity and that are "auction killing" in nature, thus leading to substantial loss of value to shareholders per share?

8 After the commencement of these proceedings, on April 30, 1998, CanWest made a second Offer, increasing the price per share it is prepared to pay to match Shaw Communication's $43.50, but contingent upon this Court setting aside the Pre-Acquisition Agreement.

Background and History

The Contesting Parties

CanWest

9 The Applicant CW Shareholdings Inc. is a wholly-owned subsidiary of CanWest Global Communications Corp., and is the corporate vehicle through which CanWest holds its shareholding interest in WIC. CanWest is publicly owned. It is a diversified media company operating internationally, holding broadcasting interests in Canada, Australia and New Zealand. As the owner of the Global Television Network, it is one of Canada's largest private independent broadcasters. As well, it syndicates its programming and provides advertising sales services to its own, and other, television stations across Canada. The province of Alberta is the only major English-speaking market in Canada that CanWest does not directly serve.

10 Although it is the owner of a commercial radio network in New Zealand, CanWest has at present no radio presence in Canada or North America. According to Thomas Strike, the Executive Vice-President of CanWest and Chief Financial Officer of CW Shareholdings, CanWest has an interest now in expanding into radio in Canada. Indeed, he said, on of the attractions of WIC to CanWest is that it has very significant radio properties, of the sort that are hard to come by.

WIC Western International Communications Ltd.

11 WIC is a Canadian public corporation with business interests in television and radio broadcasting, pay television, satellite network and wireless communication services. It is one of the largest private television and radio broadcasters in Canada, with television broadcasting facilities in British Columbia, Alberta, Ontario and Quebec and radio broadcasting facilities across western Canada and in Ontario.

12 WIC has two classes of shares: Class A voting shares which are not publicly traded) and Class B non-voting shares (which are listed on the Toronto Stock Exchange).

13 Through CW Shareholdings Inc., CanWest is the holder of 35.7% of the Class B shares of WIC and of 0.04% of WIC's Class A shares. The CanWest investment in WIC was first made in 1994 and its position has been gradually increased to the point where it is now the largest equity holder in the Company - with an investment valued at approximately $350 million (at March-end trading prices).

14 WIC's Class B shares are non-voting, however. Accordingly, with only 0.04% of the Class A shares, CanWest - although the largest equity holder in the Company - has very little voting power. It has sought a seat on the board of directors over the years, but has been rebuffed in this regard. In 1995 CanWest made an unsolicited and unsuccessful takeover bid in an attempt to acquire control of WIC. In late 1997 it came close to negotiating an agreement to acquire control from the Griffiths family but, in the end, was again unsuccessful. Thus, CanWest's interest in furthering its stake in and acquiring control of WIC has been evident for some time.

15 In mid-March of this year, however, the WIC shareholding landscape shifted under CanWest's feet. The Griffiths family sold its majority interest in the WIC's Class A shares -- through which the Company is controlled - to the Respondent, Shaw Communications, and to the then second largest Class A shareholder, Cathton Holdings Ltd. As a result of this transaction, Shaw presently holds 49.96% of the WIC Class A shares and Cathton holds 49.96% of those shares (with an option to bring its holdings to 50%). Shaw and Cathton also hold approximately 14% and 11%, respectively, of the WIC Class B shares.

Shaw Communications Inc.

16 Shaw is a Canadian public corporation with diversified business interests in the entertainment, information and communications fields. Its businesses are advanced-technology oriented and offer a variety of integrated media, video and data services. Amongst these are cable television, television programming, high-speed Internet access, digital audio services and paging services. It owns 11 radio stations. Through a related company, it is a provider of direct-to-home satellite television services.

17 It is apparent from the foregoing descriptions that WIC, CanWest and Shaw are all competitors of each other, in certain areas of the broadcasting industry, as well as takeover-bid target and rival bidding shareholders.

The CanWest TakeOver Bid

18 On March 24, 1998, CanWest made an unsolicited bid to acquire all of the outstanding Class A and Class B shares of WIC. [2] The offering price was $39.00 cash per share, the same price which had been received by the Griffiths for their Class B shares when they sold their Class A control block to Shaw and Cathton.

19 The public rationale provided by CanWest for its bid is stated in the Offer and Take Over Bid Circular, in part, as follows:

> CanWest believes that its business and that of WIC are complementary and that mutual benefits would be obtained through co-ordination of their activities. These benefits would be available on the most effective and efficient basis if all of the equity securities of WIC were acquired by the Offeror. If the Offeror acquires control of WIC, subject to CRTC approval, CanWest intends to conduct a thorough review of the business and affairs of WIC to enable the combined group to optimize future business opportunities.
>
> Through its Canadian broadcasting companies, CanWest owns and operates the Global Television Network consisting of eight television stations in Canada which reach an estimated 17.8 million persons, or approximately 77% of the English language market in Canada. CanWest believes that significant growth in Canadian advertising revenue can be achieved primarily by increasing its potential audience under signal. CanWest's strategy focuses on increasing advertising sales and decreasing operating costs. ...the province of Alberta is the only major English-speaking market in Canada that CanWest does not directly serve. The acquisition of all of the Shares by the Offeror would enable CanWest to extend its coverage to WIC's western Canadian broadcasting facilities and thus to substantially all of the Canadian English-speaking market.

20 In his evidence, Mr. Strike elaborated on this rationale and explained some of the strategy linked to it. CanWest, he said, was faced with a dilemma after the change in control of WIC as a result of the March 13th transactions in which the Griffiths sold to Shaw and Cathton. It had a large position in WIC, but it was an non-liquid interest which was not easily tradeable because of its size (8.8 million out of 26 million shares) and which represented a $350 million investment. With the old controlling shareholders of WIC - the Griffiths - gone, CanWest felt that it could best protect its investment by making the bid and acquiring as large a position as possible so that it could not be ignored by the new holders of the Class A voting shares, who might have a different agenda for the Company.

The WIC Reaction

21 WIC reacted negatively to the CanWest bid. The directors felt it was inadequate.

22 There was an additional underlying reason for the WIC management and directors to oppose the CanWest offer, however. The Class B shares carry with them a "coattail" provision, which permits holders of those shares to exchange them for Class A voting shares in the event of a change in "control" of the Company. CanWest indicated in its Offering Circular that it intended to apply to the appropriate authorities to have the issue of whether the March 13th transactions triggered the coattail rights, determined.

23 In any event, the WIC board of directors met to consider how to respond to the CanWest bid. They appointed a Special Committee of the directors to deal with the questions arising in relation to it, and they retained CIBC Wood Gundy and Bennett Jones Verchere to provide the Board and the Special Committee with financial and legal advice, respectively. Mr. Rhys Eyton was nominated as Chair of the Special Committee, which also had as one of its members Mr. John Lacey - the President and Chief Executive Officer and another director of WIC. Mr. Lacey is the person who in practical and logistical terms has had carriage of the WIC response to the CanWest initiative. I shall return to the matter of the composition and conduct of the Special Committee later in these Reasons.

24 Amongst the first responses on the part of the directors - on March 30th - was to approve and initiate what is either described as a "shareholders' rights plan" or a "poison pill", depending upon one's perspective. It is not necessary to discuss this initiative in detail. Suffice it to say that notwithstanding its professed purpose of providing the directors with more time to respond to the bid, it appeared to be more directed towards placing an impediment in the way of CanWest in taking up shares that may be tendered to its bid. Following a joint proceeding before the Ontario, Alberta and British Columbia securities commissions, an order was made cease trading the Plan.

25 Meanwhile, in a Directors' Circular of April 3rd the Board indicated that it unanimously recommended the shareholders not accept the CanWest offer. In doing so it announced that its stated intention in the circumstances was to maximize near term value for the shareholders, and that they considered themselves to be under a legal duty to do so.

26 In public statements and in evidence before the securities commissions in the previously mentioned proceedings, Mr. Lacey variously described the $39 CanWest Offer as "unfriendly", "coercive" and "opportunistic", and characterized CanWest as having been "stalking" WIC for the last two years. Can West has taken umbrage at these appellations, but I am not sure that much turns on them. The bid *was* unsolicited and made without notice, and it is apparent to all that it is "unfriendly". No one has ever described a takeover battle as a tea party. The OSC has rejected the notion that the bid was "coercive".

27 The Special Committee also took steps, through and with its advisors — as it was required to do — to attempt to generate competitive bids. Wood Gundy prepared and circulated an information package about WIC to potentially interested participants; there were talks with different parties who expressed interest; "data rooms" were set up in Vancouver, Toronto and New York. Some who expressed interest in pursuing the quest further were granted access to confidential information, subject to "standstill" agreements which precluded them from acquiring WIC securities without prior approval of the Board.

28 CanWest was not permitted access to confidential information, in spite of repeated requests for such access, because - for obvious reasons - it was not prepared to enter into such a standstill agreement. Wood Gundy advised that CanWest ought not to be afforded access to confidential information until another bidder had made a bid or, at least, until it was clear that there would be no other such bidder. Paul Spafford, the lead Wood Gundy advisor, testified that in Wood Gundy's view CanWest was very unlikely to increase its bid without another bidder in hand and that there might possibly be adverse affects to permitting CanWest to have such access in that CanWest might decide to reduce or withdraw the Offer that did exist. The WIC Special Committee and Board considered and acted upon this advice. It was a judgment call in the business context at hand, and I am satisfied that WIC was entitled to rely and act upon this advice, and was acting reasonably in doing so.

29 The decision of the Commissions to cease trade the rights under the shareholders' rights plan/poison pill was released on April 9, 1998. Thereafter, WIC decided to be somewhat more flexible in negotiating confidentiality agreements with interested parties on a case by case basis - apart from CanWest, of course. Mr. Spafford testified that several U.S. media companies executed such agreements, amongst them the National Broadcasting Corporation (NBC). Presentations were made to NBC by WIC management and Wood Gundy in New York on April 13. Although apparently interested in exploring a possible transaction, NBC advised on April 14 that it was not possible for it to negotiate and agree upon a proposal by the expiry date of the CanWest bid - which had by then been extended to April 20th.

30 Almost simultaneously with this development Shaw Communications rose to the bidding lure. Shaw had sided with CanWest in opposing the shareholders' rights plan/poison pill. It had also requested, and been provided with, a list of WIC shareholders. It had had negotiations with the Special Committee about access to the data rooms, but had refused to sign a confidentiality agreement containing a standstill provisions, and no such agreement had been entered into. Over the long Easter Weekend, however, Shaw and its financial advisors - RBC Dominion Securities Inc. ("RBC DS") - considered the pros and cons of mounting a competing bid for the WIC Class B shares.

31 In the late afternoon of April 14, RBC DS contacted Wood Gundy to indicate that Jim Shaw (the principal force at Shaw) would be calling Mr. Lacey of WIC to set up an early morning meeting the following day to put forward a bid proposal. The meeting took place at 7:00 A.M. in Vancouver, and at it Shaw Communications presented a draft term sheet for consideration. At the time CanWest's bid was due to expire on April 20th - only 5 days later. By noon Vancouver time the following day, April 16, the Special Committee and the WIC board of directors had approved and

authorized an agreement with Shaw Communications, and by the afternoon of April 17 the full agreement had been negotiated, finalized and signed.

32 Counsel for Can West place great emphasis on the haste with which the WIC/Shaw transaction was put together. However, in the intense and time-limit-driven context of a take-over bid I do not think this metamorphosis from the cacoon of nascent interest to the full spread of a takeover bid butterfly, is strikingly unusual. The issue to be determined, of course, is whether the Shaw butterfly will, in fact, "fly".

The Shaw Bid and the Pre-Acquisition Agreement

33 The Shaw bid is for all Class B shares of WIC at a price of $43.50 per share (comprised of 35% cash and 65% by way of an exchange for Shaw Class B shares). In consideration of Shaw making the bid WIC and Shaw agreed that Shaw would receive a "break fee" of $30 million and an irrevocable option to acquire WIC's radio assets for $160 million. The break fee is payable if the Shaw bid is unsuccessful because a bid superior to the $39 Can West bid is made. The radio asset option, however, is exercisable even if a "superior" offer is not induced - i.e., if the shareholders had decided, for whatever reasons (perhaps a reduction in the value of Shaw Class B shares) to accept the $39 Can West Offer - and, arguably, is exercisable even if the Shaw bid *is* successful.

34 Two subsequent developments may have affected the latter aspects of the radio asset option. The first is that Can West has since increased its bid, offering on April 30, 1998 to pay $43.50 per share, subject to the Court setting aside the Pre-Acquisition Agreement. The second is that at the Hearing of this matter on May 8, and after argument about the effect of article 3 of the Pre-Acquisition Agreement, Mr. Finkelstein advised the Court that his instructions were to indicate that Shaw Communications does not take the position that it is entitled to exercise the radio asset option in the event that its bid is successful. For purposes of determining the enforceability of the Pre-Acquisition Agreement however, I think the Agreement must be considered on the basis of the factual substratum existing at the time it was negotiated and entered into.

35 It is the break fee and radio asset provisions of the Pre-Acquisition Agreement, and the process through which these inducements to Shaw were negotiated and granted, which form the nub of the attack by Can West at this Hearing. I turn now to an analysis of the circumstances surrounding these issues. I will then turn to an analysis of the law pertaining to them, and finally, to my conclusions.

Part II - Analysis and Law

A. The Positions of the Parties

CanWest's Position

36 On behalf of CanWest, Ms. Block and Mr. Tory submit that the process and substance of the manner in which the WIC directors responded to the Can West bid and committed to the Shaw bid constitutes conduct which is in breach of their fiduciary duties in the take-over bid context and which amounts to "oppression" under the provisions of the *Canada Business Corporations Act*. This conduct -- they argue - resulted in prejudice to CanWest, not in its capacity as a bidder in the take-over bid contest, but in its capacity as a shareholder of WIC (in common with all other WIC Class B shareholders). Can West is therefore entitled to the benefit of an "oppression remedy", and in the circumstances of this case the appropriate remedy is an order setting aside the Pre-Acquisition Agreement, their argument concludes.

The WIC Position

37 On behalf of WIC, Mr. Staley and Ms. Bell submit vigorously that Can West is nothing more than a "bitter bidder" purporting to be a prejudiced shareholder. They argue that Can West is simply unhappy that the WIC board has succeeded in initiating an active and live auction for its shares, and is now coming to Court to try to invalidate the

contract which induced the competing bidding so that the auction will, in effect, be over. In substance, their submissions are summarized as follows:

> a) Can West is not entitled to resort to the oppression remedy provisions of the *CBCA* because its complaint is essentially a complaint *qua* bidder rather than *qua* shareholder; but, in any event,
>
> b) The actions of the WIC directors did, indeed, maximize shareholder value;
>
> c) The Break Fee and Radio Asset Option were reasonable and justifiable inducements to attract a necessary bidder to the process;
>
> d) The conduct of the WIC board was appropriate in the circumstances; and,
>
> e) An auction is an auction.

The Position of Shaw Communications

38 Mr. Finkelstein and Mr. Freedman support the WIC position, on behalf of Shaw Communications. They argue that there is no basis in fact or in law for the application of an oppression remedy in the circumstances of this case. The WIC directors complied with their fiduciary and statutory obligations to conduct an auction and to maximize shareholder value. Inducements to potential bidders, in order to accomplish this purpose, are permissible, and indeed common-place, in take-over bid situations - including break fees, asset sales, and a combination of such inducements, provided there is a reasonable commercial balance of all relevant factors and interests in the circumstances.

B. Law

Duty of Directors

39 The law as it relates to the general duties of the directors of Canadian corporations is not controversial. The directors must exercise the common law fiduciary and statutory obligation (a) to act honestly and in good faith with a view to the best interests of the corporation, and (b) in doing so, to exercise the care, diligence and skill that a reasonably prudent person would exercise in comparable circumstances: see the *Canada Business Corporations Act*, R.S.C. 1985, c. C-[44], s. 122. In the context of a hostile take-over bid situation where the corporation is "in play" (i.e., where it is apparent there will be a sale of equity and/or voting control) the duty is to act in the best interests of the shareholders as a whole and to take active and reasonable steps to maximize shareholder value by conducting an auction. As Callaghan A.C.J.H.C. said, in *Corona Minerals Corp. v. CSA Management Ltd.* (1989), 68 O.R. (2d) 425 (Ont. H.C.), at p. 429:

> The purpose of an auction in the securities industry is to try and achieve the highest value for the shareholders of the target companies for their shares. That in my view is an acceptable purpose...

40 In the American authorities this shareholder maximization-through-auction duty is known as the "Revlon Duty", based on the decision of the Delaware Supreme Court in *Revlon Inc. v. MacAndrews & Forbes Holdings Inc.*, 506 A.2d 173 (U.S. Del. Super. 1985). At p. 182 of that report, the court said:

> The duty of the board had thus changed from the preservation of Revlon as a corporate entity to the maximization of the company's value at a sale for the stockholders' benefit. This significantly altered the board's responsibilities ... the directors' role changed from defenders of the corporate bastion to auctioneers charged with getting the best price for the stockholders at a sale of the company.

41 The directors, moreover, are obliged to exercise these duties and carry out the maximization process in a fashion which takes into account - and minimizes, to the fullest extent reasonably possible - the conflict of interest which is inherent in the position in which they find themselves. The company for which they are responsible is under attack. There is a natural tendency to be defensive. More importantly, there is a natural tendency to protect their own position

of management and control. Jobs and careers are at stake. Indeed, it was the evidence of Mr. Spafford of Wood Gundy that in every one of the several major take-over bid situations in which he has been involved in the past few years, the job of the chief executive officer of the target corporation has been lost.

42 The directors' position is not an enviable one in such circumstances. As Professor R.C. Clark of Harvard University Law School has expressed it:

> Directors and officers of a corporation whose shares are subject to a hostile takeover bid face a serious conflict of interest. Indeed, we could well conclude that *in no other context is the conflict of interest as serious as in the takeover situation.* Often the managers' jobs are at stake. The temptation to find that what is best for oneself is also best for the corporation and shareholders (for example, to assert that the company's stock is "undervalued" and that shareholders will eventually do better if the pending offer fails), the temptation to spend corporate resources extravagantly in the attempt to fend off the raider (it's always easier to spend other people's money), and the temptation to sacrifice the shareholders' interests (as by paying exorbitant amounts of greenmail), must be overwhelming. No human being can be expected to resist such temptations.
>
> R.C. Clark, *Corporate Law* (Boston: Little Brown, 1986) at pp. 588-589 (emphasis in original)

43 Retaining independent legal and financial advisors, and the establishment of independent or special directors' committees to assess and respond to the hostile bid, are the classic mechanisms to which boards of directors have traditionally resorted in order to cope with their difficult duties and conflicting position: *CBCA*, s. 123(4)(b); *OSC Policy* 9.1, Part VII, para 27; *Brant Investments Ltd. v. KeepRite Inc.* (1987), 60 O.R. (2d) 737 (Ont. H.C.), at pp. 754-759, aff'd (1991), 3 O.R. (3d) 289 (Ont. C.A.). Resort to these devices enables the directors to investigate and consider the circumstances - including the triggering bid, and the various alternatives available to the corporation in respect of it, having regard to the interests of the shareholders - with a degree of independence. In the end, they must make a decision and exercise their judgment in a informed and independent fashion, after a reasonable analysis of the situation and acting on a rational basis with reasonable grounds for believing that their actions will promote and maximize shareholder value: see, *820099 Ontario Inc. v. Harold E. Ballard Ltd.* (1991), 3 B.L.R. (2d) 113 at 123 (Ont. Gen. Div.), at p. 176; *Olympia & York Enterprises Ltd. v. Hiram Walker Resources Ltd.* (1986), 59 O.R. (2d) 254 (Ont. Div. Ct.), at pp. 270-273.

The Process, and Break Fees and Asset Agreements as Takeover Bid Inducements

44 CanWest argues that the WIC directors failed in the exercise of their duties in carrying out the process which led up to the Shaw Communications bid and the Pre-Acquisition Agreement. Counsel submit in this respect that the WIC directors,

- failed to manage the take-over bid process appropriately, and, in particular that they failed to establish a properly comprised independent or special committee to perform that function, as a mechanism for minimizing the inherent conflict in which a target company's directors and management find themselves;

- failed to pursue in good faith their stated intention to pursue an even-handed value maximization process for the overall benefit of the shareholders, and instead sought to fend off the Can West bid and to secure the success of the competing Shaw bid;

- failed to act with due care in pursuit of their stated objective of an even-handed value maximization process; and,

- that the directors are unable to discharge what Can West argues is the onus upon them of demonstrating "the entire fairness" of the transaction which resulted from the aforesaid defective process.

45 On the other hand, counsel for WIC and for Shaw Communications assert that the WIC directors acted in good faith, on reasonable grounds, and for the purpose of serving the best interests of the Company. They submit, in particular, that:

• The Break Fee and Radio Asset Option were reasonable and justifiable inducements to attract a necessary bidder to the process;

• The conduct of the WIC board was appropriate in the circumstances; and that,

• An auction is an auction.

46 I turn now to an analysis of these issues, and to a review of the relevant law relating to them.

47 The principles underlying the directors' approach to process in takeover bid situations have been outlined above, and I shall return to them in relation to the facts of this case in a moment. What of the agreement to provide a "break fee" and an asset purchase option to Shaw Communications as a part of that process, however? What are the legal ramifications of such inducements?

Break Fees

48 A break fee - or "bust-up fee", as it is sometimes called - is a payment employed by the target corporation for the purpose of enticing another competitive bidder to enter the fray. It is paid to the competitive bidder when its bid fails or is superceded by a better offer. Partly, the inducement is paid to compensate the bidder being wooed for its time, effort, costs and lost opportunity in putting forward the opposing bid; partly the break fee is purely and simply bait to lure another party into the arena in order to generate a free-for-all for the prize. Such fees are effective inducements, and they are common in take-over bid situations and accepted as proper techniques in appropriate circumstances. The Ontario, Alberta and British Columbia Securities Commissions have acknowledged this concept only a few days ago, in this particular takeover battle - on an application by Can West to cease trade the Shaw bid as being contrary to the public interest. On May 5, 1998, the Commissions stated:

> Although break-up fees have become a more or less usual feature of the take-over bid landscape, the quantum of a specific fee could, in our view, result in the agreement to pay such a fee being an improper defensive tactic. However a break-up fee in an appropriate amount could, in our view, be properly agreed to by a target company if it were necessary to agree to it in order to induce a competing bid to come forward.

49 In both *Corona Minerals Corp. v. GSA Management Ltd., supra*, and in *Everfresh Beverages Inc., Re* (January 4, 1996), Doc. 32-077978 (Ont. Gen. Div. [Commercial List]) this Court has accepted as valid transactions which involved break fees and which resulted in "excess value realized". I accept that break fees are appropriate in such circumstances where,

(a) as the Commissions have noted, they are "necessary ... in order to induce a competing bid to come forward";

(b) that bid represents a better value for the shareholders, and where

(c) the break fee represents a reasonable commercial balance between its potential negative effect as an auction inhibitor and its potential positive effect as an auction stimulator.

Asset Options

50. The WIC directors have granted Shaw an option to purchase WIC's radio assets as a further inducement to enter the bidding.

51 Asset options are a rarer species of inducement technique in takeover bid situations that are break fees, but they are not unknown. They have been used in Canadian and American takeover bid contexts in the past. Mr. Spafford of Wood Gundy and Mr. Buzzi of RBC DS both testified to this effect. Mr. Spafford identified the 1995 Labatt/Interbrew takeover and the 1997 Ault Foods/Parmalat Food takeover as two examples in which he had been involved where asset

options had been granted, as well as a break fee, in order to induce a competing bid. In the *Hiram Walker Resources* case, *supra*, the Court refused in the circumstances to set aside a transaction which involved the sale of the Hiram Walker distillery assets, representing approximately 47% of the company's total assets.

52 The use of asset options to obtain a better offer in takeover bid situations has been recognized by securities administrators in Canada in National Policy 62-202, and its predecessor National Policy 38. It is also recognized as a defensive tactic which may come under scrutiny in the circumstances described below. See NP 62-202, Part I (Take-over Bids -Defensive Tactics), article 1.1(1)-(6). Again, in their decision respecting this particular takeover situation on May 5, 1998, the Securities Commissions recognized the dichotomy applying to asset options, expressing the philosophy reflected in NP 62-202 in this way (at p. 31):

> A particular asset option may or may not be offensive, depending on whether it is necessary to obtain a competing bid and whether it has the effect of depriving shareholders of the ability to respond to a take-over bid or to a competing bid or is likely to deny or limit severely the ability of the shareholders of the target company to respond to a take-over bid or a competing bid.

53 In my view the granting of an asset purchase option (or "asset lock-up", as it is sometimes called, in the jargon of the trade) to a potential bidder may be proper and acceptable measure for a target corporation to adopt as a competitive-bid-stimulating inducement where - viewed in the context of the entire negotiated transaction, as in the case of break fees - it strikes a reasonable commercial balance between its potential negative effect as an auction inhibitor depressing shareholder value and its potential positive effect as an auction stimulator enhancing shareholder value. On which side of this dichotomy a particular asset lock-up agreement falls will depend upon the circumstances of each particular case. Without attempting to create an exhaustive list, the factors to be considered will include, for example:

> A. Whether the process by which the directors of the target company exercised their obligation to maximize shareholder value complied with their duties as target-corporation directors;
>
> B. Whether the overall commercial balance and proportion between the auction inhibiting and auction stimulating effect of such an agreement in the circumstances has been struck, i.e., whether the agreement is likely to preclude further bidding, in the sense of harming or significantly dampening the auction process, and thus deprive the shareholders of potential additional value;
>
> C. Whether the price for the optioned asset is within the range of reasonable value attributed to that asset, or whether it represents such a discount that it would result in a disproportionate erosion in the value of the corporation making it uneconomical for others to bid;
>
> D. Whether the competing bid induced by the asset lock-up agreement provides enough additional value to the shareholders to justify the granting of the option.

54 These principles, which I accept, may be gleaned from a number of the American authorities which have considered the subject, including: *Revlon Inc. v. MacAndrews & Forbes Holdings Inc., supra* at pp. 182-183; *Cottle v. Storer Communication Inc.*, 849 F.2d 570 (U.S. 11th Cir. Fla. 1988), at pp. 575-576; *Hanson Trust PLC v. ML SCM Acquisition Inc.*, 781 F.2d 264 (U.S. 2nd Cir. N.Y. 1986), at pp. 273-276 and 281; *Mills Acquisition Co. v. MacMillan Inc.*, 559 A.2d 1261 (U.S. Del. Super. 1989), at pp. 1285-1286. The basic rationale for and parameters governing asset lock-ups in takeover bid situations are well expressed in the following passage from the decision of Justice Moore in *Revlon, supra*, at p. 183:

> A lock-up is not *per se* illegal under Delaware law. ... Such options can entice other bidders to enter a contest for control of the corporation, creating an auction for the company and maximizing shareholder profit. Current economic conditions in the takeover market [may be such] that a "white knight" ... might only enter the bidding for the target company if it receives some form of compensation to cover the risks and costs involved. ... However,

> while those lock-ups which draw bidders into the battle benefit shareholders, similar measures which end an active auction and foreclose further bidding operate to the shareholders' detriment.

55 If an asset lock-up agreement is not *per se* illegal - as I agree it is not - it seems to me that a break fee is similarly not *per se* illegal, as I have already concluded. Furthermore, if neither inducement is *per se* illegal in and of itself, I do not think it can be said that they fall into that category when utilized together. Again, whether the tactic is appropriate or inappropriate will depend on the circumstances of the case. It is of considerable importance in these kinds of situations, however, that directors of target corporations be left with as much flexibility as possible to deal with the circumstances which face them, in order to carry out their duties to maximize shareholder value.

56 In this respect, the next issue of law to be addressed is regarding the circumstances in which a Court will second guess the business judgment of the parties and what are the standards to be applied to that consideration.

The Business Judgment Rule

57 In assessing whether or not directors have met their fiduciary and statutory obligations, as outlined earlier in these Reasons, Canadian courts have generally approached the subject on the basis of what has become known as the "business judgment rule". This rule is an extension of the fundamental principle that the business and affairs of a corporation are managed by or under the direction of its board of directors. It operates to shield from court intervention business decisions which have been made honestly, prudently, in good faith and on reasonable grounds. In such cases, the board's decisions will not be subject to microscopic examination and the Court will be reluctant to interfere and to usurp the board of director's function in managing the corporation. The oft-cited remarks of Anderson J. in *Brant Investments Ltd. v. KeepRite Inc.* (1987), 60 O.R. (2d) 737 (Ont. H.C.) - made in the context of an oppression remedy hearing - are apt in this regard. At pp. 759 - 760, he said:

> The jurisdiction [to review] is one which must be exercised with care. On the one hand the minority shareholder must be protected from unfair treatment; that is the clearly expressed intent of the section. On the other hand the court ought not to usurp the function of the board of directors in managing the company, nor should it eliminate or supplant the legitimate exercise of control by the majority.....
>
> ...Business decisions, honestly made, should not be subjected to microscopic examination. There should be no interference simply because a decision is unpopular with the minority.

58 In upholding the decision of Anderson J., and in commenting on that passage, Madam Justice McKinlay stated [(1991), 3 O.R. (3d) 289 (Ont. C.A.), at p. 320]:

> There can be no doubt that on an application under s. 234 the trial judge is required to consider the nature of the impugned acts and the method in which they were carried out. *That does not mean that the trial judge should substitute his own business judgment for that of managers, directors, or a committee such as the one involved in assessing this transaction. Indeed, it would generally be impossible for him to do so, regardless of the amount of evidence before him.* He is dealing with the matter at a different time and place; it is unlikely that he will have the background knowledge and expertise of the individuals involved; he could have little or no knowledge of the background and skills of the persons who would be carrying out any proposed plan; and it is unlikely that he would have any knowledge of the specialized market in which the corporation operated. *In short, he does not know enough to make the business decision required....*
>
> It is important to note that the learned trial judge did not say that business decisions honestly made should not be subjected to examination. What he said was that they should not be subjected to *microscopic* examination. In spite of those words, the learned trial judge did, in fact, scrutinize, in a very detailed and careful manner, the nature of the transaction in this case and the manner in which it was executed.
>
> (emphasis added)

59 These comments, although made in a different oppression remedy context are equally applicable in the context of a takeover bid/oppression remedy proceeding, in my view, and reflect the law in this jurisdiction on the "business judgment rule". See also *Olympia & York Enterprises Ltd. v. Hiram Walker Resources Ltd., supra*, at pp. 270-273; *Rogers Communications Inc. v. MacLean Hunter Ltd.* (1994), 2 C.C.L.S. 233 (Ont. Gen. Div. [Commercial List]); *Cede & Co. and Cinerama, Inc. v. Technicolor Inc.*, 1993 Fed. Sec. (CCH) ¶ 92,418 (2d Cir. Jan. 6, 1986).

60 The directors' actions are not to be judged against the perfect vision of hindsight, and should be measured against the facts as they existed at the time the impugned decision was made. In addition, the court should be reluctant to substitute its own opinion for that of the directors where the business decision was made in reasonable and informed reliance on the advice of financial and legal advisors appropriately retained and consulted in the circumstances. See *Rogers Communications Inc. v. MacLean Hunter Ltd., supra*, at p. 245; *Armstrong World Industries Inc. v. Arcand* (1997), 36 B.L.R. (2d) 171 (Ont. Gen. Div. [Commercial List]); *Olympia & York Enterprises Ltd. v. Hiram Walker Resources Ltd., supra* at pp. 270-273.

61 Mr. Tory submitted that I should apply an upgraded version of the "enhanced scrutiny" standard which is common in U.S. jurisdictions, and impose an onus on the WIC directors to demonstrate the "entire fairness" of the transaction. Where directors have mishandled their process, he argued, and breached either their duty to act in good faith or their duty to act with reasonable care, the business decision which is the product of their defective deliberations is not entitled to any deference. To uphold the transaction - particularly where, as he contends is the case here as between WIC and Shaw Communications, the transaction involves a related party - the directors have the burden of establishing the "entire fairness" of the transaction. He referred me to *Cede & Co. v. Technicolor Inc., supra*, and to *Hanson Trust PLC v. ML SCM Acquisition Inc., supra*, as examples of American authorities imposing the "entire fairness" onus on directors, while acknowledging that he was not aware of any Canadian authorities which had specifically applied such a test.

62 The Saskatchewan Court of Appeal appears to have come close to doing so, however, in *347883 Alberta Ltd. v. Producers Pipelines Inc.*, [1991] 4 W.W.R. 577 (Sask. C.A.). There, the directors of a target company had implemented a poison pill contemporaneously with an issuer bid, in a defensive response to the bid. Speaking on behalf of the Court, and in commenting on the subject of appropriate and inappropriate defensive measures on the part of directors, Sherstobitoff J.A. said (p. 595):

> In summary, when a corporation is faced with susceptibility to a take-over bid or an actual take-over bid, the directors must exercise their powers in accordance with their overriding duty to act bona fide and in the best interests of the corporation even though they may find themselves, through no fault of their own, in a conflict of interest situation. If, after investigation, they determine that action is necessary to advance the best interests of the company, *they may act, but the onus will be on them to show that their acts were reasonable in relation to the threat posed and were directed to the benefit of the corporation and its shareholders as a whole, and not for an improper purpose such as entrenchment of the directors.* (emphasis added)

63 To the extent that this statement may be said to impose an evidentiary burden on the directors of a target company to justify their actions and their business decisions, I think, respectfully, that it goes too far and does not represent the law in Ontario on these matters. In my view it places the initial burden in the wrong place; and it creates the potential for diluting to a very weak potion, the business judgment approach to review of directors decisions. For all of the reasons articulated by McKinlay J.A. in *Brant Investments Ltd. v. KeepRite Inc., supra*, this would not be a wise or practical development.

64 Even the American authorities which have applied an "entire fairness" test, have done so only after the plaintiff shareholder has *rebutted* the presumption in favour the directors' decision and has provided "evidence that directors, in reaching their challenged decision, breached any one of the *triads* of their fiduciary duty - good faith, loyalty or due care": see *Cede & Co. v. Technicolor Inc., supra* at 98,023. Mr. Tory urged me to adopt this approach. However, I am satisfied that the proper way to address the appropriateness of directors decisions in the context of a heated takeover bid situation

is through the judicious application of the "business judgment rule" as I have endeavoured to articulate at the beginning of this portion of these Reasons. That is, where business decisions have been made honestly, prudently, in good faith and on reasonable and rational grounds, the Court will be reluctant to interfere and to usurp the board of director's function in managing the corporation. In such cases, the board's decisions will not be subject to microscopic examination.

C. The Process, and the Negotiation of the WIC\Shaw Communications Agreement

65 In addition to the immediate negative reaction to the "unfriendly" and "coercive" CanWest bid by WIC, and the imposition of the poison pill, CanWest argues that the entire process by which the WIC/Shaw Communications agreement was negotiated was flawed and demonstrates a failure by the WIC directors to comply with their duties in the circumstances.

66 These complaints included the refusal to allow CanWest access to the data room until after Shaw Communications had made its bid (which I have rejected earlier), and the suggestion that the entire negotiation process leading up to the Pre-Acquisition Agreement was simply too hasty for the directors to have been able to comply with their obligations in a meaningful way (which I have also rejected). The most significant objections, however, relate to:

a) the composition and role of the Special Committee;

b) the negotiations themselves;

c) the nature and effect of the combined offering of a break fee and an asset purchase option to an already major shareholder, which is at least something of an insider;

d) the overall issue regarding "valuation" of the WIC radio assets; and,

e) the failure of the WIC directors to contact CanWest prior to entering into the agreement with Shaw Communications, particularly when its management was aware that CanWest had earlier expressed an interest in the WIC radio assets.

67 Some of these matters raise troubling concerns - particularly the composition of the Special Committee and the role of Mr. Lacey in its actions, the "insider" implications of Shaw Communications position, and the fact that the radio asset option is exercisable even without a superior offer and - as I read it, at least - even if the Shaw Communications bid is successful. Having considered all of the evidence, however, I have concluded on balance that the WIC directors cannot be said to have acted in a fashion contrary to their duty as directors to maximize shareholder value and that the combination of the break fee and radio asset option, as an inducement to entice Shaw Communications in as a bidder in the absence of any other competitive bid, was justified in the circumstances of this case.

68 I am satisfied there was no obligation on the part of WIC to go back to CanWest before entering into the agreement with Shaw Communications. This was a business and negotiating judgment call, and the WIC directors considered the advisability of doing so and, acting on professional advice, decided not to do so. They were entitled to make this judgment call.

The Evidence

69 I pause at this point to comment generally upon the nature of the evidence placed before the Court in this proceeding. I say "proceeding" because what took place was a hybrid between what began as an Application, supported by affidavit and documentary evidence, was supplemented at the Hearing by 2 $^{1}/_{2}$ days of *viva voce* evidence. The affidavits of the principal players served essentially as their examination in chief, and their cross-examinations were conducted in Court. The same was true of the several experts, who testified primarily as to the issue of "value" of the WIC radio assets. In this way, what would otherwise have been a very lengthy trial - and one that could not have been accommodated in the "real time" parameters existing before the expiry of the two bids tomorrow - was able to be completed in a concentrated, but

very telescoped, manner. The parties and their counsel are to be commended for the way in which this has been made possible, and for the excellence of the materials file and submissions made.

70 I have read the affidavit evidence, examined the supporting documentation, and listened very carefully to the *viva voce* testimony given by the witnesses. I have the advantage of the *viva voce* evidence being available in daily transcript form.

71 There is very little conflict in the evidence as to what actually happened during the takeover bid process, including that relating to the negotiation of the WIC/Shaw Communications agreement. The differences are as to the inferences which the parties invite the Court to draw from those facts. I have no hesitation in accepting - as I do - the evidence of Messrs. Strike, Lacey, Spafford, and Buzzi as to what transpired in the circumstances they outline. I accept the evidence of Mr. Lacey and Mr. Spafford as to the beliefs and motivations on WIC side of the controversy. The evidence does not support, in my opinion, an inference that they did not act honestly and in good faith, and I decline to draw any such conclusion. Mr. Buzzi was credible and reliable when he confined his evidence to matters within his sphere as financial advisor, but I give no weight whatever to his legal conclusions or - more aptly - to his evidence as to what the Shaw Communications intentions, motivations and understanding relating to the agreement are and were. He cannot speak for Shaw Communications.

72 Jim Shaw did not give evidence. As a result, the Court was deprived of the evidence of the principal of Shaw Communications who was "calling the shots" and who was directly involved in the negotiations. I am satisfied, from the public announcements attributed to Mr. Shaw - and not denied by anyone - that it is the intention of Shaw Communications to "run" WIC and to integrate WIC and Shaw Communications into "one big multimedia company"; moreover, it is the view of Shaw Communications that the radio assets are coming to it whether Shaw Communications is bested on the bid or successful on the bid. Jim Shaw made this latter comment in a media conference call on April 17th, and, indeed - as I read Articles 3.1 and 3.2 of the Pre-Acquisition Agreement - he is correct in taking that position. Nonetheless, in the end, I do not think it matters for purposes of the outcome of these proceedings.

The Special Committee

73 The WIC directors appointed a "Special Committee" to deal with and respond to the CanWest bid shortly after the bid was announced. This, as I have mentioned, is one of the standard and classic mechanisms whereby boards of directors and management of target corporations seek to minimize the inherent conflict in their position. It was the proper thing to do.

74 Mr. Rhys Eyton was appointed Chair of the Special Committee which also included as members two recently nominated directors of WIC - Peter Classon and Wendy Leaney - and the Chairman of the WIC board, Robert Brodie. However, the Special Committee also had as a member the senior representative of management in the Company, Mr. Lacey. Mr. Lacey is a director of WIC. He is also its President and Chief Executive Officer. He should not have been a member of the Special Committee, in my view.

75 Not only was Mr. Lacey a member of the Special Committee, however; he was in practical terms the member who was charged with the responsibility of leading its activities and, in particular, negotiating the Shaw Communications deal. The conflict is apparent. He is senior management. His job is on the line. Indeed, Mr. Spafford as much as told us during testimony that, based on his experience in many takeover bid situations, Mr. Lacey's job would be likely be gone following the outcome of the bid process! In addition to this inherently conflicting position, Mr. Lacey was placed in the position of negotiating with Mr. Shaw, who represented the existing 49.96% shareholder of controlling stock, which had openly declared its intention of running the Company. As Ms. Block and Mr. Tory submitted, he was negotiating with his potential boss. Or his potential employment executioner. Either way, his presence on the Special Committee, and the role he played, were not in keeping with the sort of independence which is the very *raison d'être* of such a committee. The OSC was critical of the composition and role of the Special Committee in its decision relating to the shareholders'

rights plan/poison pill, characterizing the committee as being "set up for the purposes of convenience only, and not as an independent committee", and stating:

> In our view, in a take-over bid context a committee which includes as an active participant the president and chief executive officer of the corporation and, as an observer and resource, a representative of a shareholder which has 50% of the votes, is not an independent committee. The fact that Mr. Lacey has a "golden parachute" agreement, does not in our view change this position.
>
> In these circumstances, it is our view that we must place less reliance on the review by the Special Committee of the Bid, and possible alternative methods of achieving a more beneficial result to shareholders, than we would if the Special Committee had been truly an independent committee.

76 The Securities Commissions had different evidence before them than I have had. I am not able to conclude on the evidence in these proceedings that the WIC Special Committee was "set up for the purposes of convenience only, and not as an independent committee". However, I agree with the Commissions' observations about the inappropriateness of the composition of the committee. I note in passing, that the representative of the 50% shareholder which sat with the Committee as "an observer and resource" was a representative of Cathton, not of Shaw. After the decision of the Commissions, that representative ceased his involvement with the Special Committee. Mr. Lacey, however - as is apparent - did not.

77 I have wrestled with whether this flaw in the composition of the Special Committee itself sufficiently taints the actions of that committee so that its conduct in receiving, negotiating and approving the Shaw Communications bid - and the board's decision based upon its recommendation -- are undermined completely. In the end, I find that they are not. Indeed - having regard to all of the evidence as to what transpired in the negotiation process, including the direct questions addressed at both the board and Special Committee levels, and having regard to the WIC/Shaw agreement as a whole (resulting, as it did, in a bid significantly superior to the initial CanWest bid) - I am satisfied that the Special Committee in fact conducted itself in a fashion that enabled the directors to carry out their stated objective of maximizing shareholder value.

78 A brief review of the evidence regarding the ebb and flow of the negotiations with Shaw Communications, and the considerations which were addressed by Mr. Lacey, Mr. Spafford (WIC's lead financial advisor) and the members of the Special Committee and the Board, will suffice to underline that conclusion.

Negotiations of the WIC/Shaw Communications Agreement

79 Neither Mr. Lacey, nor Mr. Spafford, nor the Special Committee, nor the Board rolled over and played dead when the Shaw Communications proposal was tendered. Although the time parameters were tight and intense, I find that the ultimate agreement was negotiated vigorously and in a fashion where the parties each bargained for the best they could get. In the result, what emerged was an agreement considerably more favourable to WIC, and accordingly to all of the WIC shareholders, than was the initial Shaw Communications proposal.

80 Mr. Lacey testified that the negotiations took place over a number of fronts, most particularly,

> a) the price to be paid per share, and whether or not there would be a cash pool to be drawn upon regardless of the number of WIC Class B shares tendered and acquired (this was significant because Shaw Communications was proposing a split in consideration in a range of a maximum 35% cash and 65% Shaw Class B Shares);
>
> b) the break fee; and,
>
> c) an asset purchase option which Shaw Communications was seeking with respect to *both* WIC's radio assets *and* WIC's specialty pay TV assets.

81 In the result, the price per share wavered between $43 and $44, and settled at $43.50; WIC was unsuccessful in negotiating a "cash pool", but it was successful in fending off Shaw Communication's attempt to acquire an option on the pay TV assets (WIC considered them too close to the "core" of its business); and the break fee price moved back and forth between $25 million and $40 million, before finalizing itself at the $30 million figure.

82 For those interested in the details of these negotiations, they are well summarized in the Shaw Communications factum, in the following passages (paragraph 17):

> The Shaw Offer was heavily negotiated over a three-day period commencing on April 15, 1998. The negotiations were intense, at arm's length and at times heated. The principal negotiations proceeded as follows:
>
> •April 15 - Shaw submitted a written proposal to the Special Committee offering a price of $43 per WIC Class B Share, payable 35% in cash and 65% in Shaw Class B Shares. In exchange for this offer, Shaw stated that it required as an inducement for its offer (i) a break fee of $25M; (ii) an irrevocable option to purchase the WIC radio assets at a price of $130M; and (iii) an irrevocable option to purchase the WIC specialty and pay television assets for $100M, all to be paid or granted in the event of a successful competing bid or certain other specified events. It was pointed out to the Special Committee that the Shaw Offer was structured such that it would not preclude the WIC board of directors from endorsing a superior proposal if such a proposal was forthcoming.
>
> • April 15 - WIC responded with its own term sheet outlining the following terms: (i) an offer price of $43 per WIC Class B Share, with a $350 million cash pool available to be drawn on regardless of the number of WIC Class B Shares tendered and acquired, (ii) deleting the asset option on WIC's specialty and pay television assets, (iii) the triggering event for any break fee or radio option would be the successful completion of a competing offer, not the making of a offer, and (iv) if a competing offer was successful, Shaw would be entitled to a break fee of either (A) $25 million or (B) $10 million and the right to buy WIC's radio assets at an exercise price which would be determined after the triggering of the option through the negotiation between the parties of the fair market value of the radio assets (i.e., an agreement to agree) or, failing agreement, by submitting the valuation to an arbitration process.
>
> • April 15 - Shaw responded that it was necessary to price the radio option before an agreement could be reached. The reason for this was that the exercise of the radio option would only arise in circumstances where Shaw was not the successful bidder, and Shaw was not prepared to negotiate a price on that option with CanWest, the party that Shaw believed to be the most likely to top Shaw's offer. Shaw insisted that WIC determine the fair market value of the radio assets as part of the negotiations so that the exercise price of the option was fixed.
>
> • April 16 - Shaw advised WIC that a fixed cash pool of $350 million regardless of the number of shares tendered was not acceptable and that an option on WIC's specialty and pay television assets was extremely important to Shaw.
>
> • April 16 - WIC replied with a new proposal whereby Shaw would bid $44 per WIC Class B Share. Under this proposal, WIC would grant Shaw a $30M break fee and would grant a radio option with an exercise price of $160M. There would be no option on the specialty and pay television assets.
>
> • April 16 - Shaw responded with a counter-offer of $43.50 per share, along with a break fee of $40M and a radio option at the price of $160M. Shaw did not insist on an option on the specialty and pay television assets.
>
> • April 16 - The parties were then able to agree on the terms of an offer whereby Shaw would offer a price of $43.50 per WIC Class B Share (the "Shaw Offer") and would receive a $30 million break fee (the "Break Fee") and an option for Shaw to buy WIC's radio assets for a price of $160 million (the "Radio Option") (collectively, the terms of which came to form the "Pre-Acquisition Agreement", which was executed by WIC and Shaw on April 17, 1998). No option was granted on WIC's speciality and pay television assets.

83 The WIC Special Committee met throughout the day on each of April 15 and 16, 1998. It was apprised of, and discussed the negotiations with Shaw Communications, and it received and considered the financial advice of Wood Gundy and the legal advice of its lawyers.

84 The following excerpts from the Minutes of the Meetings of the Special Committee held on April 15th and 16th reflect the matters to which the members of the Committee addressed themselves. I accept the evidence of Mr. Lacey and Mr. Spafford that they represent, at a minimum, what was discussed at those meetings:

> **April 15**
>
> David Mongeau and Paul Spafford [both of Wood Gundy] then addressed the Special Committee (after the Shaw representatives had presented their proposal and left the meeting). *There was a lot of discussion about the value of radio* and pay and about how solid the $43 offer was. Much would depend on the projected value of Shaw's shares following the bid. If the cash component was greater, the offer would be improved significantly. *David Mongeau then described the directors' mandate and alternatives regarding encouragement of other bids and the objective of the break-up fee. The economic consequences of the break-up fee have to be looked at whether it was so large as to prevent anyone else from coming forward with a bid.* He said the cash component was within the acceptable three to five percent range. The other significant feature of the bid was the lock-up on the radio and pay television divisions.
>
> John Lacey viewed their proposal as giving us three options:
>
> a) we could argue about the proposed $25 million break-up fee;
>
> b) we could get a good price for the radio and pay television divisions; or
>
> c) we could accept their offer.
>
> *There was a strong objection to paying a break-up fee as well as locking-up the radio pay televisions divisions. There was then a discussion about alternatives possibly involving a smaller break-up fee and a lock-up on assets but at fair market value.*
>
> (emphasis added)
>
> **April 16**
>
> John Lacey said that the Committee was called together because it should review certain improvements to Shaw Bid that have been negotiated. The price was now $43.50 for all the Class B Non-Voting shares; still 35% cash and 65% Shaw stock. If Shaw does not complete the acquisition, there is a $30 million break-up fee and the right to purchase the Radio Division for $160 million. The meeting was advised that Shaw's first position after abandonment of the inclusion of Pay TV was for a break-up fee of $40 million plus the right to purchase the Radio Division for $160 million. *It was felt that the offer now presented a $35 million improvement on the first offer.*
>
> *Wendy Leaney was concerned about the sale of the Radio Division without a valuation from CIBC Wood Gundy. Also $160 million is the low end of the numbers that John Lacey had produced as a range of values for the year 2000, namely $160-$200 million. John Lacey said that those numbers projected values almost two years hence and that certain assumptions were still anticipatory. The meeting was also advised by Paul Spafford and David Mongeau that the loss of the Radio Division would not deter NBC. The price of $160 million appeared to be in a range of 17.5 times 1998 EBITDA and 23.5 times 1997 EBITDA. John Lacey recommended it as a very good price.*
>
> (emphasis added)

85 I find, on the basis of the discussions which these Minutes reflect and the testimony of Mr. Lacey and Mr. Stafford, that the Special Committee - in spite of Mr. Lacey's conflict position - was carrying out its designed function to address and assess the WIC alternatives, weigh the varying financial considerations - including the relative value of the radio assets, the ranges of values presented and the concern over selling the radio division without a valuation from CIBC Wood Gundy (Ms. Leaney) - and the impact of the proposals on "preventing [someone else] from coming forward with a bid". It was Wood Gundy's advice that the proposed transaction would not be "auction ending".

86 On April 16th the WIC Board of Directors unanimously approved the agreement and authorized Mr. Lacey to finalize it. Again, the evidence of Mr. Lacey and Mr. Spafford - who both attended the meeting, and whose evidence I accept in this regard - and the Minutes of the Directors Meeting confirm that the Board considered and genuinely applied its collective mind to the pertinent questions necessary to fulfill its mandate as directors of a target company. The Minutes reflect the following discussions and considerations:

> **April 16**
>
> ***New Shaw Proposal***
>
> John Lacey presented the new Shaw proposal and described the material terms. The price was now $43.50 for all the Class B Non-Voting shares; still 35% cash and 65% Shaw stock. If Shaws do not complete the acquisition, there is a $30 million break-up fee and the right to purchase the Radio Division for $160 million. The meeting was advised that Shaw's first request after abandonment of the inclusion of Pay TV was for a break-up fee of $40 million plus the right to purchase the Radio Division for $140 million. *It was felt that this new offer was a $35 million improvement on the first offer.* John Lacey said that there was a noon deadline. He advised that the Special Committee unanimously approved this Offer. CIBC Wood Gundy was going to give an overall fairness opinion. As the Corporation's CEO, John Lacey was recommending this transaction.
>
> Paul Spafford then said that the Board should approve the transaction subject to receiving pre-merger agreement in definitive form and a fairness opinion from CIBC Wood Gundy which he said he now gave them orally. *He said they were comfortable that this Bid is materially higher than what was on the table. They are comfortable to be able to give an opinion that this proposal is fair from a financial point of view. It is now up the Board to determine that the other things Shaw has asked for are reasonable in the circumstances.* CIBC Wood Gundy advised that numerous precedents show 2.5%-5% of the value of the transaction as being a range for break-up fees. This fee is reasonable and normal in the circumstances. *As to the sale of Radio, the directors have to address the issue of whether the granting of an option to Shaw scares away other bidders. The directors have to make a judgment on "if WIC doesn't have Radio, will CanWest still be a bidder". He said he did not think it would take CanWest out of the bidder category. He added that it would not take the other potential bidder out of play.*
>
> He advised that they tried to get Radio to be valued at fair market value at the time of sale but Shaw would not go for the uncertainty of such a proposal. *He had not done the detail work on Radio as a stand alone asset to advise the directors that $160 million was fair market value but he said they do not think anyone will say for sure that it was sold too cheap. He did advise that this Offer was materially better than the Offer by CanWest.*
>
> (emphasis added)

"Value" for the WIC Radio Assets

87 Much evidence and argument in the proceedings were directed towards the issue of the price obtained by the WIC directors for the WIC radio assets. I do not find it necessary to review that evidence in detail because, on the evidence it seems to me that this is a subject upon which reasonable professional can - and did - differ.

88 CanWest called as its principal witness in this regard Dr. Arthur Gruen. Dr. Gruen has expertise in valuing radio and communications enterprises in the United States and in assessing the impact of changes in the marketplace on the price that may be paid for such publicly traded enterprises. He is an economist, but his Report in this case was constructed primarily on a statistical basis. He was asked to, and did, examine the impact of what was believed to be a forthcoming change in the Canadian regulatory regime to permit what are called "duopolies" in the radio business, on revenue multiples that would apply to the sale of radio assets. He then applied those conclusions to an estimate of the value of the WIC radio assets.

89 "Duopoly deregulation" - as I understand its basics - permits common ownership of AM and FM stations in a given market to increase from one AM station and one FM station to two of each. This type of deregulation occurred in the United States in 1992 - and was expanded in 1996 - and the common consensus is that it has led to great increases in radio revenues, coupled with the ability to reduce costs through economies of scale, and that these effects in turn have led to greater prices being paid for radio assets on the market. Dr. Gruen's theory is that, other factors in the Canadian marketplace remaining constant (including the peculiarities relating to Canada's own brand of regulation), the same thing will happen in Canada. As a result, he postulates that the value of WIC's radio assets is in the range of $195 million to $230 million (depending on margin improvements). He thus concluded that at $160 million price to be paid by Shaw Communications under the radio asset option did not "fully capture shareholder value".

90 Dr. Gruen's Report was vigorously attacked by counsel for WIC and for Shaw Communications on a number of grounds. As with all expert reports putting forth a range of values based upon a particular approach, it is vulnerable to some refutation. However, I don't think much turns on the attacks. I accept Dr. Gruen's Report and his evidence for what they purport to be: a statistical analysis of whether or not the price paid for the WIC radio would be positively affected by duopoly deregulation, and an effort to attribute a value to those assets on that basis. Even given that valuation, though, I do not think it translates into a conclusion that the radio asset option granted to Shaw Communications was unduly generous in the circumstances or so "off the dial" in terms of valuation that it cannot stand.

91 The Special Committee had before it a range of estimates of value with respect to the WIC radio assets, although to be sure it did not have a formally prepared valuation from Wood Gundy. WIC had earlier received an informal offer for the radio assets at $80 million. Its own internal management had prepared a Report which gave the assets a range of from $160 million to $240 million and a mid-point of $200 million. Mr. Lacey, who had been brought into WIC to improve its performance and who knew that the radio assets were "poorly managed" - as did, it seems, almost everyone else - thought that this range was too high. Mr. Spafford had had a Wood Gundy analyst prepare some informal (i.e. unwritten) assessments, and felt comfortable in advising the Special Committee and the Board that it was reasonable to accept the radio asset option at that price. Wood Gundy did give WIC and overall fairness opinion as to the WIC/ Shaw Communications agreement.

92 CanWest itself had indications from its own financial advisors, Midland Walwyn (on the one hand) and Roy Hennessy (on the other hand) that the value of the WIC radio assets ranged from about $60 million to about $142 million (Midland Walwyn) and about $100 million but perhaps buyable at $65-$75 million (Hennessy).

93 Having regard to all of the foregoing, and to the circumstances in which they found themselves - needing in a very short period of time to generate another bid before the April 20th expiry of the then CanWest bid, or leave the shareholders to that bid alone - I do not think it can be said that $160 million (or even a net of $130 million, after the break fee[3]) was an unreasonable price to place on the radio asset option in this fact situation.

The Combined Inducement of a $30 Million Break Fee and the Radio Asset Option

94 Earlier in these Reasons I have dealt at some length with the principles to be applied in considering the acceptability of break fees and asset purchase options as "defensive tactics" or "bid-inducing" tactics in the hotbed of a takeover bid situation. Neither is unlawful in and of itself; nor are they impermissible in combination, in principle. Each case must

be assessed on its own facts. In essence it is a question of balance, proportionality and commercial reasonableness in the overall context of the takeover bid and the directors mandate to enhance and maximize value for the shareholders as a whole.

95 Does the Pre-Acquisition Agreement which is the subject of attack in this case pass muster in this regard? I have concluded, and find, that it does.

96 There is no doubt that the WIC radio assets are attractive assets to all parties, including CanWest and that their value in a volatile market now reacting to the CRTC announcement of April 30th introducing duopoly deregulation into Canada is probably increasing. This may explain why CanWest has just recently announced that it is prepared to pay $200 million for the assets. However, the matter must be looked at in perspective, and from the viewpoint of the takeover bid situation as a whole and the WIC/Shaw Communications agreement in its entirety.

97 The WIC radio assets represent something less than 15% of WIC's total revenues and 12.8% of its total assets. The radio assets were acknowledged by all to have been underperforming. In 1997 they were responsible for only 0.6% of total operating income. WIC's core assets are its television assets and I am satisfied that it is these television assets - particularly the access which they provide to Alberta, the only English-speaking Province in which CanWest does not have a presence - which are the major attraction to CanWest and, indeed to other potential bidders. Although much of the focus in these proceedings has been on the WIC radio assets - because of the nature of the attack on the Pre-Acquisition Agreement - it must be remembered that this is not really what the takeover battle is about. The directors' obligation is to maximize shareholder value in the context of this overarching consideration. Bargaining away the radio assets, on balance and having regard to their proportionate contribution to the overall WIC picture, was reasonable in the circumstances.

Part III - Conclusion

The Oppression Remedy

98 The oppression remedy exists - in a significant way, at least - to protect the reasonable expectations of shareholders. I agree that in a hostile takeover bid environment, the reasonable expectations of the shareholders as a group is that the target company's directors and management will take appropriate steps to maximize shareholder value. As Farley J. noted, in *Rogers Communications Inc. v. MacLean Hunter Ltd.*, *supra*, at p. 245:

> It is reasonable that a target board not roll over and play dead. If it were completely passive, it would be soundly criticized for not doing anything to maximize the situation for the target organization.

99 In the same case, however, Farley J. held that relief under statutory oppression remedy provisions is not available to an applicant solely in its capacity as a *bidder* - "bitter" or otherwise -- but only in its capacity as a *shareholder: ibid*, at p. 247. See also *Benson v. Third Canadian General Investment Trust Ltd.* (1993), 14 O.R. (3d) 493 (Ont. Gen. Div. [Commercial List]). WIC and Shaw Communications submit that CanWest has come to court as a "bitter bidder", unhappy that the WIC directors have generated a superior bid to its own, and not as a shareholder, and therefore that it is not entitled to "oppression remedy" relief.

100 In the circumstances of this case, I would not preclude CanWest from having status as a complainant shareholder under the provisions of the *CBCA*. This case is different from that of *Rogers Communications*, for instance, where it was clear that the applicant's complaint was entirely as a bidder and not as a shareholder. Here, however, CanWest has raised issued that do go to prejudice on its part, and on the part of the WIC shareholders generally, if its assertions as to the process followed by the WIC directors and the effect of the Pre-Acquisition Agreement on shareholder value in the corporation are made out. That is sufficient to provide it with standing as a complainant shareholder, in my view. The fact that it also happens to be the initiating bidder in the takeover battle does not, in and of itself, deprive CanWest as shareholder from asserting a claim under the oppression remedy sections of the *CBCA*.

101 On the merits, however, I am not satisfied that a case for the granting of an oppression remedy has been made out.

102 What the *Act* proscribes is conduct on the part of the directors which is *unfairly* prejudicial to, or which *unfairly* disregards the interests of the complainant. The mere fact that the Shaw Communications bid - including the impugned break fee and asset option combination - may be "prejudicial" to CanWest, in the sense that it may create a playing field slightly tilted away from the first bidder, is not sufficient. The transaction must be "oppressive" or "*unfairly* prejudicial" to CanWest or "*unfairly* disregard" its interests before the Court's jurisdiction "to rectify the matters complained of" comes into play. In the circumstances of this case, I am satisfied that the WIC/Shaw transaction does not fall into those categories.

Disposition

103 In the final result, the Special Committee and the WIC directors were able to entice a competing bid from Shaw Communications, on the eve of the expiry of CanWest's then outstanding bid, and when there appeared to be no be no other bidder on the horizon. This increased offer represented an increase of something in the neighbourhood of $115 million in value over CanWest's $39 bid (depending on the trading value of the Shaw Class B Shares), and, according to Mr. Lacey, represented an offer that was about $39 million more than what had originally been proposed by Shaw Communications at the outset of the negotiations.

104 The break fee of $30 million represents 2.6% of the total Shaw offer, and by all accounts is well within the normal parameters for such inducements in the industry. In exchange for this break fee and an option of potentially attractive but nonetheless underperforming radio assets at a price reasonably negotiated in the circumstances, the Special Committee and the WIC directors have achieved a result which has benefited the shareholders as a group (including CanWest, in its capacity as a shareholder).

105 I conclude, in summary, that WIC and the WIC directors have complied with their fiduciary and statutory obligations, and endeavoured honestly and in good faith to achieve their stated objective of "maximizing the value of the Shareholders' investments in WIC". They acted with due care and caution. They retained, received and considered independent financial and legal advice. They applied their collective minds to that advice and to the circumstances which confronted them, and acted independently to the benefit of WIC and its shareholders as a whole. In such circumstances, the Pre-Acquisition Agreement which was an integral, reasonable and necessary part of achieving that favourable overall result, cannot be struck down. To do so might well eliminate the Shaw Communications bid from play whereas - like the Securities Commissions, and in spite of Mr. Strikes's somewhat equivocal protestations to the contrary - I am not convinced that such is the case with respect to the CanWest bid, if the Pre-Acquisition Agreement remains in place. Only time will tell, however.

106 Accordingly, the Application is dismissed. The respondents are entitled to their costs. I may be spoken to with respect to costs, if necessary.

107 Again, I am very grateful to counsel for the manner in which this proceeding has been prepared and put forward, and for the admirably high quality of their advocacy.

Application dismissed.

Footnotes

1 The phrase was initially coined by Farley J. in *Benson v. Third Canadian General Investment Trust Ltd.* (1993), 14 O.R. (3d) 493 (Ont. Gen. Div. [Commercial List]), at pp. 511-512.

2 Not surprisingly, none of the Class A shares was for sale.

3 There is an argument that need not be pursued in any detail to the effect that the "net" figure is more than $130 million because of the tax consequences that may be attributable to Shaw Communications in connection with receipt of the break fee.

End of Document

Tab 3

RBC Capital Markets®

RBC Dominion Securities Inc.
200 Bay Street, 4th Floor
P.O. Box 50
Royal Bank Plaza
Toronto, Ontario M5J 2W7
Telephone: (416) 842-2000

July 27, 2016

The Board of Directors
Lightstream Resources Ltd.
2800, 525 – 8th Avenue SW
Calgary, Alberta T2P 1G1

To the Board:

RBC Dominion Securities Inc. ("RBC"), a member company of RBC Capital Markets, understands that Lightstream Resources Ltd. (the "Company") has proposed a plan of arrangement under Section 192 of the *Canada Business Corporations Act* ("CBCA") pursuant to which, among other things, the Company's (i) US$650 million aggregate principal amount of 9.875% second priority senior secured notes due June 15, 2019 (the "Secured Notes"); (ii) US$254 million aggregate principal amount of 8.625% senior notes due February 1, 2020 (the "Unsecured Notes"); and (iii) common shares ("Common Shares") will be restructured pursuant to a recapitalization plan (collectively, the "Recapitalization"). The terms of the Recapitalization will be more fully described in a management information circular (the "Circular"), which will be mailed to each of the holders of the Secured Notes (the "Secured Noteholders"), Unsecured Notes (the "Unsecured Noteholders") and Common Shares (the "Shareholders") in connection with the Recapitalization.

The board of directors (the "Board") of the Company has retained RBC to provide advice and assistance to the Board in evaluating the Recapitalization, including the preparation and delivery to the Board of RBC's opinion (the "CBCA Opinion") in the form described in paragraph 4.04 of Industry Canada's Policy Statement 15.1 – *Policy of the Director Concerning Arrangements under Section 192 of the CBCA*. In connection with the Recapitalization, the Board has also requested that RBC prepare and deliver to the Board, a separate opinion as to the fairness of the Recapitalization from a financial point of view to the Company. RBC has not prepared a valuation of the Company or any of its securities or assets and the CBCA Opinion should not be construed as such.

Engagement

The Board initially contacted RBC regarding a potential advisory assignment in April 2016, and RBC was formally engaged by the Board through an agreement between the Company and RBC dated June 1, 2016 and amended on July 14, 2016 (collectively, the "Engagement Agreement"). The terms of the Engagement Agreement provide that RBC is to be paid a fee for its services as financial advisor, including fees that are contingent on the completion of the Recapitalization or certain other events. In addition, RBC is to be reimbursed for its reasonable out-of-pocket expenses and to be indemnified by the Company in certain circumstances. RBC consents to the inclusion of the CBCA Opinion in its entirety and a summary thereof in the Circular and to the filing thereof, as necessary, by the Company with the securities commissions or similar regulatory authorities in each province of Canada.

Relationship With Interested Parties

Neither RBC, nor any of its affiliates is an insider, associate or affiliate (as those terms are defined in the *Securities Act* (Ontario)) of the Company or any of its associates or affiliates. RBC and its affiliates have not been engaged to provide any financial advisory services nor has it participated in any financing involving the Company or any of its associates or affiliates, within the past two years, other than the services provided under the Engagement Agreement and as described herein. RBC and its affiliates have acted in the following capacities for the Company and its associates and affiliates: (i) financial advisor regarding a potential sale of or investment in the Company's East Pembina Cardium asset in 2014 and (ii) financial advisor and placement agent on a debt exchange of Unsecured Notes for Secured Notes and the issuance of an incremental US$200 million of Secured Notes in July 2015. There are no understandings, agreements or commitments between RBC and its affiliates and the Company or any of its associates or affiliates with respect to any future business dealings. RBC and its affiliates may, in the future, in the ordinary course of its business, perform financial advisory or investment banking services for the Company or any of its associates or affiliates. Royal Bank of Canada ("Royal Bank"), controlling shareholder of RBC, provides banking services to the Company in the normal course of business. Royal Bank currently holds CDN$27.1 million in the Company's revolving credit facility (the "Revolving Credit Facility").

RBC acts as a trader and dealer, both as principal and agent, in major financial markets and, as such, may have had and may in the future have positions in the securities of the Company or any of its associates or affiliates and, from time to time, may have executed or may execute transactions on behalf of such companies or clients for which it received or may receive compensation. As an investment dealer, RBC conducts research on securities and may, in the ordinary course of its business, provide research reports and investment advice to its clients on investment matters, including with respect to the Company or the Recapitalization.

Credentials of RBC Capital Markets

RBC is one of Canada's largest investment banking firms, with operations in all facets of corporate and government finance, corporate banking, mergers and acquisitions, equity and fixed income sales and trading and investment research. RBC Capital Markets also has significant operations in the United States and internationally. The CBCA Opinion expressed herein represents the opinion of RBC and the form and content herein have been approved for release by a committee of its directors, each of whom is experienced in merger, acquisition, divestiture and fairness opinion matters.

Scope of Review

In connection with our CBCA Opinion, we have reviewed and relied upon or carried out, among other things, the following:

1. the most recent draft, dated July 27, 2016, of the Circular (the "Draft Circular");
2. the most recent draft, dated July 26, 2016, of the summary of terms and conditions related to the Company's proposed new CDN$400 million revolving credit facility;
3. the most recent draft, dated July 27, 2016, of the backstop agreement to be entered into between the Company and certain Secured Noteholders;
4. the support agreement, dated July 12, 2016, entered into between the Company and members of the ad hoc committee of the Secured Noteholders, holding in aggregate approximately 91.5% of the Secured Notes, in respect of the Recapitalization;

5. the forbearance agreement, dated July 12, 2016, entered into between the Company, lenders to the Company under the Revolving Credit Facility and The Toronto-Dominion Bank, as administrative agent of the Revolving Credit Facility and the most recent draft, dated July 25, 2016, of the amendment thereto;
6. audited financial statements of the Company for each of the three years ended December 31, 2013 through 2015 and audited financial statements of PetroBakken Energy Ltd. ("PetroBakken") (a predecessor firm of the Company) for each of the two years ended December 31, 2011 and 2012;
7. management's discussion and analysis of the Company for each of the three years ended December 31, 2013 through 2015 and management's discussion and analysis of PetroBakken for each of the two years ended December 31, 2011 and 2012;
8. the unaudited interim report of the Company for the quarter ended March 31, 2016;
9. management's discussion and analysis of the Company for the quarter ended March 31, 2016;
10. the Notice of Annual Meeting of Shareholders and Management Information Circulars of the Company for each of the two years ended December 31, 2013 and 2014;
11. annual information forms of the Company for each of the two years ended December 31, 2014 and 2015;
12. unaudited projected financial statements for the Company on a consolidated basis prepared by management of the Company for the years ending December 31, 2016 through 2018, under various potential financing, asset sale and recapitalization alternatives;
13. discussions with senior management of the Company;
14. discussions with the Company's legal counsel;
15. discussions with (i) TD Securities Inc., financial advisor to the Company on the recent sale process for the Company's assets, and (ii) FTI Consulting Canada, Inc. ("FTI"), a financial advisor to the Company, on FTI's analysis of the liquidation and wind-up costs of the Company under a liquidation scenario;
16. the independent petroleum engineering report relating to the Company from Sproule Associates Limited, evaluating the Company's petroleum and natural gas reserves as of December 31, 2015 (the "Reserve Report");
17. analyses prepared by management of the Company, sensitizing the Reserve Report for alternate effective dates and commodity prices;
18. public information relating to the business, operations, financial performance and stock trading history of the Company and other selected public companies considered by us to be relevant;
19. the trading history of the Secured Notes and Unsecured Notes;
20. public information with respect to other transactions of a comparable nature considered by us to be relevant;
21. public information regarding the Canadian oil and gas industry;
22. representations contained in a certificate addressed to us, dated as of the date hereof, from senior officers of the Company as to the completeness and accuracy of the information upon which the CBCA Opinion is based; and
23. such other corporate, industry and financial market information, investigations and analyses as RBC considered necessary or appropriate in the circumstances.

RBC has not, to the best of its knowledge, been denied access by the Company to any information requested by RBC.

Assumptions and Limitations

With the Board's approval and as provided for in the Engagement Agreement, RBC has relied upon the completeness, accuracy and fair presentation of all of the financial (including, without limitation, the financial statements of the Company) and other information, data, advice, opinions or representations obtained by it from public sources, senior management of the Company, and their consultants and advisors (collectively, the "Information"). The CBCA Opinion is conditional upon such completeness, accuracy and fair presentation of such Information. Subject to the exercise of professional judgment and except as expressly described herein, we have not attempted to verify independently the completeness, accuracy or fair presentation of any of the Information.

Senior officers of the Company have represented to RBC in a certificate delivered as of the date hereof, among other things, that (i) the Information (as defined above) provided orally by, or in the presence of, an officer or employee of the Company or in writing by the Company or any of its subsidiaries or their respective agents to RBC for the purpose of preparing the CBCA Opinion was, at the date the Information was provided to RBC, and is complete, true and correct in all material respects, and did not and does not contain any untrue statement of a material fact in respect of the Company, its subsidiaries or the Recapitalization and did not and does not omit to state a material fact in respect of the Company, its subsidiaries or the Recapitalization necessary to make the Information or any statement contained therein not misleading in light of the circumstances under which the Information was provided or any statement was made; and that (ii) since the dates on which the Information was provided to RBC, except as disclosed in writing to RBC, there has been no material change, financial or otherwise, in the financial condition, assets, liabilities (contingent or otherwise), business, operations or prospects of the Company or any of its subsidiaries and no material change has occurred in the Information or any part thereof which would have or which would reasonably be expected to have a material effect on the CBCA Opinion.

In preparing the CBCA Opinion, RBC has made several assumptions, including that all of the conditions required to implement the Recapitalization will be met and that the disclosure provided or incorporated by reference in the Draft Circular with respect to the Company, its subsidiaries and affiliates and the Recapitalization is accurate in all material respects.

The CBCA Opinion is rendered on the basis of securities markets, economic, financial and general business conditions prevailing as at the date hereof and the condition and prospects, financial and otherwise, of the Company and its subsidiaries and affiliates, as they were reflected in the Information and as they have been represented to RBC in discussions with management of the Company. In its analyses and in preparing the CBCA Opinion, RBC made numerous assumptions with respect to industry performance, general business and economic conditions and other matters, many of which are beyond the control of RBC or any party involved in the Recapitalization.

The CBCA Opinion has been provided for the use of the Board and may not be used by any other person or relied upon by any other person other than the Board without the express prior written consent of RBC. The CBCA Opinion is given as of the date hereof and RBC disclaims any undertaking or obligation to advise any person of any change in any fact or matter affecting the CBCA Opinion which may come or be brought to RBC's attention after the date hereof. Without limiting the foregoing, in the event that there is any material change in any fact or matter affecting the CBCA Opinion after the date hereof, RBC reserves the right to change, modify or withdraw the CBCA Opinion.

RBC believes that its analyses must be considered as a whole and that selecting portions of the analyses or the factors considered by it, without considering all factors and analyses together,

could create a misleading view of the process underlying the CBCA Opinion. The preparation of a CBCA opinion is a complex process and is not necessarily susceptible to partial analysis or summary description. Any attempt to do so could lead to undue emphasis on any particular factor or analysis. RBC has not been engaged to provide and has not provided or prepared: (i) an opinion as to the fairness of the Recapitalization to the Secured Noteholders, Unsecured Noteholders or Shareholders; (ii) an opinion as to the relative fairness of the Recapitalization among or as between the Secured Noteholders, Unsecured Noteholders and Shareholders; or (iii) an opinion as to the ability of the Company after the implementation of the Recapitalization to repay (or refinance) the principal amount of its indebtedness (after giving effect to the Recapitalization), and the CBCA Opinion should not be construed as such. Additionally, the CBCA Opinion is not to be construed as a recommendation to any Secured Noteholder, Unsecured Noteholder or Shareholder as to whether to vote in favour of the Recapitalization.

CBCA Opinion Analysis

Approach to CBCA Opinion

Industry Canada's Policy Statement 15.1 – *Policy of the Director Concerning Arrangements under Section 192 of the CBCA* recommends that corporations seeking to implement a plan of arrangement pursuant to Section 192 of the CBCA that contemplates the compromise of debt, obtain an opinion as to whether "each class of security holders would be in a better position under the arrangement than if the corporation were liquidated."

For the purposes of the CBCA Opinion, RBC considered that the Secured Noteholders, Unsecured Noteholders and Shareholders would each be in a better financial position under the Recapitalization than if the Company were liquidated, if the estimated aggregate value of the consideration made available to the Secured Noteholders, Unsecured Noteholders and Shareholders under the Recapitalization, respectively, exceeds the estimated value such holders would receive if the Company were liquidated.

Conclusion

Based upon and subject to the foregoing, RBC is of the opinion that, as of the date hereof, the Secured Noteholders, Unsecured Noteholders and Shareholders would each be in a better position from a financial point of view under the Recapitalization than if the Company were liquidated.

Yours very truly,

RBC Dominion Securities Inc.

RBC DOMINION SECURITIES INC.

Tab 4

2015 ONSC 5557
Ontario Superior Court of Justice [Commercial List]

Nelson Education Ltd., Re

2015 CarswellOnt 13576, 2015 ONSC 5557, 258 A.C.W.S. (3d) 465, 29 C.B.R. (6th) 140

In the Matter of the Companies' Lenders Arrangement Act, R.S.C. 1985, c. C-36, as Amended

In the Matter of a Plan of Compromise or Arrangement of Nelson Education Ltd. and Nelson Education Holdings Ltd., Applicants

Newbould J.

Heard: August 13, 27, 2015
Judgment: September 8, 2015
Docket: CV15-10961-00CL

Counsel: Benjamin Zarnett, Jessica Kimmel, Caroline Descours for Applicants
Robert W. Staley, Kevin J. Zych, Sean Zweig for First Lien Agent and the First Lien Steering Committee
John L. Finnigan, D.J. Miller, Kyla E.M. Mahar for Royal Bank of Canada
Orestes Pasparaskis for Monitor

Subject: Insolvency

MOTION by company for approval of sale; MOTION by bank for order that amounts owing to it and portion of consent fee be paid by company prior to sale.

Newbould J.:

1 The applicants Nelson Education Ltd. ("Nelson") and Nelson Education Holdings Ltd. sought and obtained protection under the CCAA on May 12, 2015. They now apply for approval of the sale of substantially all of the assets and business of Nelson to a newly incorporated entity to be owned indirectly by Nelson's first ranked secured lenders (the "first lien lenders") pursuant to a credit bid made by the first lien agent. Nelson also seeks ancillary orders relating to the sale. The effect of the credit bid, if approved, is that the second lien lenders will receive nothing for their outstanding loans.

2 RBC is one of 22 first lien lenders, a second lien lender and agent for the second lien lenders. At the time of its motion to replace the Monitor, RBC did not accept that the proposed sale should be approved. RBC now takes no position on the sale approval motion other than to oppose certain ancillary relief sought by the applicants. RBC also has moved for an order that certain amounts said to be owing to it and their portion of a consent fee should be paid by Nelson prior to the completion of the sale. The applicants and the first lien lenders oppose the relief sought by RBC.

Nelson business

3 Nelson is a Canadian education publishing company, providing learning solutions to universities, colleges, students, teachers, professors, libraries, government agencies, schools, professionals and corporations across the country.

4 The business and assets of Nelson were acquired by an OMERS entity and certain other funds from the Thomson Corporation in 2007 together with U.S. assets of Thomson for U.S. $7.75 billion, of which US$550 million was attributed

to the Canadian business. The purchase was financed with first lien debt of approximately US$311.5 million and second lien debt of approximately US$171.3 million.

5 The maturity date under the first lien credit agreement was July 3, 2014 and the maturity date under the second lien credit agreement was July 3, 2015. Nelson has not paid the principal balances owing under either loan. It paid interest on the first lien credit up to the filing of this CCAA application. It has paid no interest on the second lien credit since April 2014. As of the filing date, Nelson was indebted in the aggregate principal amounts of approximately US$269 million, plus accrued interest, costs and fees, under the first lien credit agreement and approximately US$153 million, plus accrued interest, costs and fees, under the second lien credit agreement.

6 Because these loans are denominated in U.S. dollars, the recent decline in the Canadian dollar against the United States dollar has significantly increased the Canadian dollar balance of the loans. Nelson generates substantially all of its revenue in Canadian dollars and is not hedged against currency fluctuations. Based on an exchange rate of CAD/USD of 1.313, as of August 10, 2015, the Canadian dollar principal balances of the first and second lien loans are $352,873,910 and $201,176,237.

7 According to Mr. Greg Nordal, the CEO of Nelson, the business of Nelson has been affected by a general decline in the education markets over the past few years. Notwithstanding the industry decline over the past few years, Nelson has maintained strong EBITDA over each of the last several years.

Discussions leading to the sale to the first lien lenders

8 In March 2013, Nelson engaged Alvarez & Marsal Canada Securities ULC ("A&M"), the Canadian corporate finance arm of Alvarez & Marsal to assist it in reviewing and considering potential strategic alternatives. RBC, the second lien agent also engaged a financial advisor in March 2013 and the first lien steering committee engaged a financial advisor in June 2013. RBC held approximately 85% of the second lien debt.

9 Commencing in April 2013, Nelson and its advisors entered into discussions with stakeholders including the RBC as second lien agent, the first lien steering committee and their advisors. Nelson sought to achieve as its primary objective a consensual transaction that would be supported by all of the first lien lenders and second lien lenders. These discussions took place until September 2014. No agreement with the first lien lenders and second lien lenders was reached.

10 In April 2014, Nelson and the second lien lenders agreed to two extensions of the cure period under the second lien credit agreement in respect of the second lien interest payment due on March 31, 2014, to May 30, 2014. In connection with these extensions, Nelson made a partial payment of US$350,000 in respect of the March interest payment and paid certain professional fees of the second lien lenders. Nelson requested a further extension of the second lien cure period beyond May 30, 2014, but the second lien lenders did not agree. Thereafter, Nelson defaulted under the second lien credit agreement and failed to make further interest payments to the second lien lenders.

11 The first lien credit agreement matured on July 3, 2014. On July 7, 2014, Nelson proposed an amendment and extension of that agreement and solicited consent from its first lien lenders. RBC, as one of the first lien lenders was prepared to consent to the Nelson proposal, being a consent and support agreement, but no agreement was reached with the other first lien lenders and it did not proceed.

12 In September, 2014, Nelson proposed in a term sheet to the first lien lenders a transaction framework for a sale or restructuring of the business on the terms set out in a term sheet dated September 10, 2014 and sought their support. In connection with the first lien term sheet, Nelson entered into a first lien support agreement with first lien lenders representing approximately 88% of the principal amounts outstanding under the first lien credit agreement. The consenting first lien lenders comprised 21 of the 22 first lien lenders, the only first lien lender not consenting being RBC. Consent fees of approximately US$12 million have been paid to the consenting first lien lenders.

13 The first lien term sheet provided that Nelson would conduct a comprehensive and open sale or investment sales process (SISP) to attempt to identify one or more potential purchasers of, or investors in, the Nelson business on terms that would provide for net sale or investment proceeds sufficient to pay in full all obligations under the first lien credit agreement or that was otherwise acceptable to first lien lenders holding at least 66 2/3% of the outstanding obligations under the first lien credit agreement. If such a superior offer was not identified pursuant to the SISP, the first lien lenders would become the purchaser and purchase substantially all of the assets of Nelson in exchange for the conversion by all of the first lien lenders of all of the debt owing to them under the first lien credit agreement into a new first lien term facility and for common shares of the purchaser.

14 In September 2014, the company engaged A&M to assist with the SISP. By that time, A&M had been advising the Company for over 17 months and had gained an understanding of the Nelson Business and the educational publishing industry. The SISP was structured as a two-phase process.

15 Phase 1 involved (i) contacting 168 potential purchasers, including both financial and strategic parties located in Canada, the United States and Europe, and 11 potential lenders to ascertain their potential interest in a transaction, (ii) initial due diligence and (iii) receipt by Nelson of non-binding letters of interest ("LOIs"). The SISP provided that interested parties could propose a purchase of the whole or parts of the business or an investment in Nelson.

16 Seven potential purchasers submitted LOIs under phase 1, six of which were offers to purchase substantially all of the Nelson business and one of which was an offer to acquire only the K-12 business. Nelson reviewed the LOIs with the assistance of its advisors, and following consultation with the first lien steering committee and its advisors, invited five of the parties that submitted LOIs to phase 2 of the SISP. Phase 2 of the SISP involved additional due diligence, data room access and management presentations aimed at completion of binding documentation for a superior offer.

17 Three participants submitted non-binding offers by the deadline of December 19, 2014, two of which were for the purchase of substantially all of the Nelson business and one of which was for the acquisition of the K-12 business. All three offers remained subject to further due diligence and reflected values that were significantly below the value of the obligations under the first lien credit agreement.

18 On December 19, 2014, one of the participants advised A&M that it required additional time to complete and submit its offer, which additional time was granted. An offer was subsequently submitted but not ultimately advanced by the bidder.

19 Nelson, with the assistance of its advisors, maintained communications throughout its restructuring efforts with Cengage Learnings, the company that has the U.S. business that was sold by Thomson and which is a key business partner of Nelson. Cengage submitted an expression of interest for the higher education business that, even in combination with the offer received for the K-12 business, was substantially lower than the amount of the first lien debt. In February 2015, Cengage and Nelson terminated discussions about a potential sale transaction.

20 Ultimately, phase 2 of the SISP did not result in a transaction that would generate proceeds sufficient to repay the obligations under the first lien credit agreement in full or would otherwise be supported by the first lien lenders. Accordingly, with the assistance of A&M and its legal advisors, and in consultation with the first lien steering committee, Nelson determined that it should proceed with the sale transaction pursuant to the first lien support agreement.

Sale transaction

21 The sale transaction is an asset purchase. It will enable the Nelson business to continue as a going concern. It includes:

> (a) the transfer of substantially all of Nelson's assets to a newly incorporated entity to be owned indirectly by the first lien lenders;

(b) the assumption by the purchaser of substantially all of Nelson's trade payables, contractual obligations and employment obligations incurred in the ordinary course and as reflected in its balance sheet, excluding some obligations including the obligations under the second lien credit agreement and an intercompany promissory note of approximately $102.3 million owing by Nelson to Nelson Education Holdings Ltd.;

(c) an offer of employment by the purchaser to all of Nelson's employees; and

(d) a release by the first lien lenders of all of the indebtedness owing under the first lien credit agreement in exchange for: (i) 100% of the common shares of a newly incorporated entity that will own 100% of the common shares of the purchaser, and (ii) the obligations under a new US$200 million first lien term facility to be entered into by the Purchaser.

22 The relief sought by the applicants apart from the approval of the sale transaction involves ancillary relief, including authorizing the distribution from Nelson's cash on hand to the first lien lenders of outstanding fees and interest, effecting mutual releases of parties associated with the sale transaction, and deeming a shareholders' rights agreement to bind all shareholders of the purchaser. This ancillary relief is opposed by RBC.

Analysis

(i) Sale approval

23 RBC says it takes no position on the sale, although it opposes some of the terms and seeks an order paying the second lien lenders their pre-filing interest and expense claims. Whether RBC is entitled to raise the issues that it has requires a consideration of the intercreditor agreement of July 5, 2007 made between the agents for the first lien lenders and the second lien lenders.

24 Section 6.1(a) of the intercreditor agreement provides that the second lien lenders shall not object to or oppose a sale and of the collateral and shall be deemed to have consented to it if the first lien claimholders have consented to it. It provides:

> The Second Lien Collateral Agent on behalf of the Second Lien Claimholders agrees that it will raise no objection or oppose a sale or other disposition of any Collateral free and clear of its Liens and other claims under Section 363 of the Bankruptcy Code (or any similar provision of any other Bankruptcy Law or any order of a court of competent jurisdiction) if the First Lien Claimholders have consented to such sale or disposition of such assets and the Second Lien Collateral Agent and each other Second Lien Claimholder will be deemed to have consented under Section 363 of the Bankruptcy Code (or any similar provision of any other Bankruptcy Law or any order of a court of competent jurisdiction) to any sale supported by the First Lien Claimholders and to have released their Liens in such assets.
>
> (underlining added)

25 Section 6.11 of the intercreditor agreement contained a similar provision. RBC raises the point that for these two sections to be applicable, the first lien claimholders must have consented to the sale, and that the definition of first lien claimholders means that all of the first lien lenders must have consented to the sale. In this case, only 88% of the first lien lenders consented to the sale, the lone holdout being RBC. The definition in the intercreditor agreement of first lien claimholder is as follows:

> **"First Lien Claimholders"** means, at any relevant time, the holders of First Lien Obligations at that time, including the First Lien Collateral Agent, the First Lien Lenders, any other "Secured Party" (as defined in the First Lien Credit Agreement) and the agents under the First Lien Loan Documents.

26 The intercreditor agreement is governed by the New York law and is to be construed and enforced in accordance with that law. The first lien agent filed an opinion of Allan L. Gropper, a former bankruptcy judge in the Southern

District of New York and undoubtedly highly qualified to express proper expert opinions regarding the matters in issue. Mr. Gropper did not, however, discuss the principles of interpretation of a commercial contract under New York law, and in the absence of such evidence, I am to take the law of New York so far as contract interpretation is concerned as the same as our law. In any event, New York law regarding the interpretation of a contract would appear to be the same as our law. See *Cruden v. Bank of New York*, 957 F.2d 961 (U.S. C.A. 2nd Cir. 1992) and *Rainbow v. Swisher*, 72 N.Y.2d 106, 531 N.Y.S. 775, 527 N.E.2d 258 (U.S. N.Y. Ct. App. 1988). Mr. Gropper did opine that the sections in question are valid and enforceable in accordance with their terms. [1]

27 The intercreditor agreement, like a lot of complex commercial contracts, appears to have a hodgepodge of terms piled on, or added to, one another, with many definitions and exceptions to exceptions. That is what too often appears to happen when too many lawyers are involved in stirring the broth. It is clear that there are many definitions, including a reference to First Lien Lenders, which is defined to be the Lenders as defined in the First Lien Loan Documents, which is itself a defined term, meaning the First Lien Credit Agreement and the Loan Documents. The provisions of the first lien credit agreement make clear that the Lenders include all those who have lent under that agreement, including obviously RBC.

28 Under section 8.02(d) of the first lien credit agreement, more than 50% of the first lien lenders (the "Required Lenders") may direct the first lien agent to exercise on behalf of the first lien lenders all rights and remedies available to. In this case 88% of the first lien lenders, being all except RBC, directed the first lien agent to credit bid all of the first lien debt. This credit bid was thus made on behalf of all of the first lien lenders, including RBC.

29 While the definition of First Lien Claimholders is expansive and refers to both the First Lien Collateral Agent (the first lien agent) and the First Lien Lenders, suggesting a distinction between the two, once the Required Lenders have caused a credit bid to be made by the First Lien Collateral Agent, RBC in my view is taken to have supported the sale that is contemplated by the credit bid.

30 It follows that RBC is deemed under section 6.11 of the intercreditor agreement to have consented to the sale supported by the first lien claimholders. It is nevertheless required that I determine whether the sale and its terms should be approved. It is also important to note that no sale agreement has been signed and it awaits an order approving the form of Asset Purchase Agreement submitted by Nelson in its motion materials.

31 This is an unusual CCAA case. It involves the acquisition of the Nelson business by its senior secured creditors under a credit bid made after a SISP conducted before any CCAA process and without any prior court approval of the SISP terms. The result of the credit bid in this case will be the continuation of the Nelson business in the hands of the first lien lenders, a business that is generating a substantial EBITDA each year and which has been paying its unsecured creditors in the normal course, but with the extinguishment of the US $153 million plus interest owed to the second lien lenders.

32 Liquidating CCAA proceedings without a plan of arrangement are now a part of the insolvency landscape in Canada, but it is usual that the sale process be undertaken after a court has blessed the proposed sale methodology with a monitor fully participating in the sale process and reporting to the court with its views on the process that was carried out [2] . None of this has occurred in this case. One issue therefore is whether the SISP carried out before credit bid sale that has occurred involving an out of court process can be said to meet the *Soundair* [3] principles and that the credit bid sale meets the requirements of section 36(3) of the CCAA.

33 I have concluded that the SISP and the credit bid sale transaction in this case does meet those requirements, for the reasons that follow.

34 Alvarez & Marsal Canada Inc. was named the Monitor in the Initial Order over the objections of RBC, but shortly afterwards on the come-back motion by RBC, was replaced as Monitor by FTI Consulting Inc. The reasons for this change are contained in my endorsement of June 2, 2015. There was no suggestion of a lack of integrity or competence on the part of A&M or Alvarez & Marsal Canada Inc. In brief, the reason was that A&M had been retained by Nelson in

2013 as a financial advisor in connection with its debt situation, and in September 2014 had been retained to undertake the SISP process that has led to the sale transaction to the first lien lenders. I did not consider it right to put Alvarez & Marsal Canada Inc. in the position of providing independent advice to the Court on the SISP process that its affiliate had conducted, and that it would be fairer to all concerned that a different Monitor be appointed in light of the fact that the validity of the SISP process was going to be front and centre in the application of Nelson to have the sale agreement to the first lien lenders approved. Accordingly FTI was appointed to be the Monitor.

35 FTI did a thorough review of all relevant facts, including interviewing a large number of people involved. In its report to the Court the Monitor expressed the following views:

> (a) The design of the SISP was typical of such marketing processes and was consistent with processes that have been approved by the courts in many CCAA proceedings;
>
> (b) The SISP allowed interested parties adequate opportunity to conduct due diligence, both A&M and management appear to have been responsive to all requests from potentially interested parties and the timelines provided for in the SISP were reasonable in the circumstances;
>
> (c) The activities undertaken by A&M were consistent with the activities that any investment banker or sale advisor engaged to assist in the sale of a business would be expected to undertake;
>
> (d) The selection of A&M as investment banker would not have had a detrimental effect on the SISP or the value of offers;
>
> (e) Both key senior management and A&M were incentivised to achieve the best value available and there was no impediment to doing so;
>
> (f) The SISP was undertaken in a thorough and professional manner;
>
> (g) The results of the SISP clearly demonstrate that none of the interested parties would, or would be likely to, offer a price for the Nelson business that would be sufficient to repay the amounts owing to the first lien lenders under the first lien credit agreement
>
> (h) The SISP was a thorough market test and can be relied on to establish that there is no value beyond the first lien debt.

36 The Monitor expressed the further view that:

> (a) There is no realistic prospect that Nelson could obtain a new source of financing sufficient to repay the first lien debt;
>
> (b) An alternative debt restructuring that might create value for the second lien lenders is not a viable alternative at this time;
>
> (c) There is no reasonable prospect of a new sale process generating a transaction at a value in excess of the first lien debt;
>
> (d) It does not appear that there are significant operational improvements reasonably available that would materially improve profitability in the short-term such that the value of the Nelson business would increase to the extent necessary to repay the first lien debt and, accordingly, there is no apparent benefit from delaying the sale of the business.

37 *Soundair* established factors to be considered in an application to approve a sale in a receivership. These factors have widely been considered in such applications in a CCAA proceeding. They are:

(a) whether sufficient effort has been made to obtain the best price and that the receiver or debtor (as applicable) has not acted improvidently;

(b) whether the interests of all parties have been considered;

(c) the efficacy and integrity of the process by which offers have been obtained; and

(d) whether there has been unfairness in the working out of the process.

38 These factors are now largely mirrored in section 36(3) of the CCAA that requires a court to consider a number of factors, among other things, in deciding to authorize a sale of a debtor's assets. It is necessary to deal briefly with them.

(a) Whether the process leading to the proposed sale or disposition was reasonable in the circumstances. In this case, despite the fact that there was no prior court approval to the SISP, I accept the Monitor's view that the process was reasonable.

(b) Whether the monitor approved the process leading to the proposed sale or disposition. In this case there was no monitor at the time of the SISP. This factor is thus not strictly applicable as it assumes a sale process undertaken in a CCAA proceeding. However, the report of FTI blessing the SISP that took place is an important factor to consider.

(c) Whether the monitor filed with the court a report stating that in its opinion the sale or disposition would be more beneficial to the creditors than a sale or disposition under a bankruptcy. The Monitor did not make such a statement in its report. However, there is no reason to think that a sale or disposition under a bankruptcy would be more beneficial to the creditors. The creditors negatively affected could not expect to fare better in a bankruptcy.

(d) The extent to which the creditors were consulted. The first lien steering committee was obviously consulted. Before the SISP, RBC, the second lien lenders' agent, was consulted and actively participated in the reconstruction discussions. I take it from the evidence that RBC did not actively participate in the SISP, a decision of its choosing, but was provided some updates.

(e) The effects of the proposed sale or disposition on the creditors and other interested parties. The positive effect is that all ordinary course creditors, employees, suppliers and customers will be protected. The effect on the second lien lenders is to wipe out their security and any chance of their loans being repaid. However, apart from their being deemed to have consented to the sale, it is clear that the second lien lenders have no economic interest in the Nelson assets except as might be the case some years away if Nelson were able to improve its profitability to the point that the second lien lenders could be paid something towards the debt owed to them. RBC puts this time line as perhaps five years and it is clearly conjecture. The first lien lenders however are not obliged to wait in the hopes of some future result. As the senior secured creditor, they have priority over the interests of the second lien lenders.

There are some excluded liabilities and a small amount owing to former terminated employees that will not be paid. As to these the Monitor points out that there is no reasonable prospect of any alternative solution that would provide a recovery for those creditors, all of whom rank subordinate to the first lien lenders.

(f) Whether the consideration to be received for the assets is reasonable and fair, taking into account their market value. The Monitor is of the view that the results of the SISP indicate that the consideration is fair and reasonable in the circumstances and that the SISP can, and should, be relied on for the purposes of such a determination. There is no evidence to the contrary and I accept the view of the Monitor.

39 In the circumstances, taking into account the *Soundair* factors and the matters to be considered in section 36(3) of the CCAA, I am satisfied that the sale transaction should be approved. Whether the ancillary relief should be granted is a separate issue, to which I now turn.

(ii) Ancillary claimed relief

(a) Vesting order

40 The applicants seek a vesting order vesting all of Nelson's right, title and interest in and to the purchased assets in the purchaser, free and clear of all interests, liens, charges and encumbrances, other than the permitted encumbrances and assumed liabilities contemplated in the Asset Purchase Agreement. It is normal relief given in an asset sale under the CCAA and it is appropriate in this case.

(b) Payment of amounts to first lien lenders

41 As a condition to the completion of the transaction, Nelson is to pay all accrued and unpaid interest owing to the first lien lenders and all unpaid professional fees of the first lien agent and the first lien lenders outstanding under the first lien credit agreement. RBC does not oppose this relief.

42 If the cash is not paid out before the closing, it will be an asset of the purchaser as all cash on hand is being acquired by the purchaser. Thus the first lien lenders will have the cash. However, because the applicant is requesting a court ordered release by the first lien lenders of all obligations under the first lien credit agreement, the unpaid professional fees of the first lien agent and the first lien lenders that are outstanding under the first lien credit agreement would no longer be payable after the closing of the transaction. Presumably this is the reason for the payment of these prior to the closing.

43 These amounts are owed under the provisions of the first lien credit agreement and have priority over the interests of the second lien lenders under the intercreditor agreement. However, on June 2, 2015 it was ordered that pending further order, Nelson was prevented from paying any interest or other expenses to the first lien lenders unless the same payments owing to the second lien lenders. Nelson then chose not to make any payments to the first lien lenders. It is in effect now asking for an order nunc pro tunc permitting the payments to be made. I have some reluctance to make such an order, but in light of no opposition to it and that fact that it is clear from the report of the Monitor that there is no value in the collateral for the second lien lenders, the payment is approved.

(c) Releases

44 The applicants request an order that would include a broad release of the parties to the Asset Purchase Agreement as well as well as other persons including the first lien lenders.

45 The Asset Purchase Agreement has not been executed. In accordance with the draft approval and vesting order sought by the applicants, it is to be entered into upon the entry of the approval and vesting order. The release contained in the draft Asset Purchase Agreement in section 5.12 provides that the parties release each other from claims in connection with Nelson, the Nelson business, the Asset Purchase Agreement, the transaction, these proceedings, the first lien support agreement, the supplemental support agreement, the payment and settlement agreement, the first lien credit agreement and the other loan documents or the transactions contemplated by them. Released parties are not released from their other obligations or from claims of fraud. The release also does not deal with the second lien credit agreement or the second lien lenders.

46 The first lien term sheet made a part of the support agreement contained terms and conditions, but it stated that they would not be effective until definitive agreements were made by the applicable parties and until they became effective. One of the terms was that there would be a release "usual and customary for transactions of this nature", including a release by the first lien lenders in connection with "all matters related to the Existing First Lien Credit Agreement, the

other Loan Documents and the transactions contemplated herein". RBC was not a party to the support agreement or the first lien term sheet.

47 The release in the Asset Purchase Agreement at section 5.12 provides that "each of the Parties on behalf of itself and its Affiliates does hereby forever release...". "Affiliates" is defined to include "any other Person that directly or indirectly...controls...such Person". The party that is the purchaser is a New Brunswick numbered company that will be owned indirectly by the first lien lenders. What instructions will or have been given by the first lien lenders to the numbered company to sign the Asset Purchase Agreement are not in the record, but I will assume that the First Lien Agent has or will authorize it and that RBC as a first lien lenders has not and will not authorize it.

48 Releases are a feature of approved plans of compromise and arrangement under the CCAA. The conditions for such a release have been laid down in *ATB Financial v. Metcalfe & Mansfield Alternative Investments II Corp.*, 2008 ONCA 587 (Ont. C.A.) at paras. 43 and 70. Third party releases are authorized under the CCAA if there is a reasonable connection between the third party claim being compromised in the plan and the restructuring achieved by the plan. In *Metcalfe*, Blair J.A. found compelling that the claims to be released were rationally related to the purpose of the plan and necessary for it and that the parties who were to have claims against them released were contributing in a tangible and realistic way to the plan[4] .

49 While there is no CCAA plan in this case, I see no reason not to consider the principles established in *Metcalfe* when considering a sale such as this under the CCAA, with any necessary modifications due to the fact that it is not a sale pursuant to a plan. The application of those principles dictates in my view that the requested release by the first lien lenders should not be ordered.

50 The beneficiaries of the release by the first lien lenders are providing nothing to the first lien lenders in return for the release. The substance of the support agreement was that Nelson agreed to try to fetch as much as it could through a SISP but that if it could not get enough to satisfy the first lien lenders, it agreed to a credit bid by the first lien lenders. Neither Nelson nor the first lien agent or supplemental first lien agent or any other party gave up anything in return for a release from the first lien lenders. So far as RBC releasing a claim that it may have as a first lien lender against the other first lien lenders, nothing has been provided to RBC by the other first lien lenders in return for such a release. RBC as a first lien lender would be required to give up any claim it might have against the other parties to the release for any matters arising prior to or after the support agreement while receiving nothing in return for its release.

In the circumstances, I decline to approve the release by the first lien lenders requested by the applicants to be included in the approval and vesting order.

(d) Stockholders and Registration Rights Agreement

51 The applicants seek to have a Stockholders and Registration Rights Agreement declared effective and binding on all persons entitled to receive common shares of Purchaser Holdco in connection with the transaction as though such persons were signatories to the Stockholders and Registration Rights Agreement.

52 The Stockholders and Registration Rights Agreement is a contract among the purchaser's parent company, Purchaser Holdco, and the holders of Purchaser Holdco's common shares. After implementation of the transaction, the first lien lenders will be the holders of 100% of the shares of Purchaser Holdco. The Stockholders and Registration Rights Agreement was negotiated and agreed to by Purchaser Holdco and the First Lien Steering Committee (all first lien lenders except RBC). The First Lien Steering Committee would like RBC to be bound by the agreement. The evidence of this is in the affidavit of Mr. Nordal, the President and CEO of Nelson, who says that based on discussions with Mr. Chadwick, the First Lien Steering Committee requires that all of the first lien lenders to be bound to the terms of the

Stockholders and Registration Rights Agreement. This is of course double hearsay as Mr. Chadwick acts for Nelson and not the First Lien Steering Committee.

The effect of what is being requested is that RBC as a shareholder of Purchaser Holdco would be bound to some shareholder agreement amongst the shareholders of Purchaser Holdco. While the remaining 88% of the shareholders of Purchaser Holdco might want to bind RBC, I see nothing in the record that would justify such a confiscation of such shareholder rights. I agree with RBC that extending the Court's jurisdiction in these CCAA proceedings and exercising it to assist the purchaser's parent company with its corporate governance is not appropriate. The purchaser and its parent company either have the contractual right to bind all first lien lenders to terms as future shareholders, or they do not.

RBC Motion

(a) Second lenders' pre-filing interest and second lien agent's fees

53 RBC seeks an order that directing Nelson to pay to RBC in its capacity as the second lien agent the second lien interest outstanding at the filing date of CDN$1,316,181.73 and the second lien fees incurred prior to the filing date of US$15,365,998.83.

54 Mr. Zarnett in argument conceded that these amounts are owed under the second lien credit agreement. There are further issues, however, being (i) whether they continue to be owed due to the intercreditor agreement (ii) whether RBC is entitled under the intercreditor agreement to request the payment and (iii) whether RBC is entitled to be paid these under the intercreditor agreement before the first lien lenders are paid in full.

55 There is a distinction between a lien subordination agreement and a payment subordination agreement. Lien subordination is limited to dealings with the collateral over which both groups of lenders hold security. It gives the senior lender a head start with respect to any enforcement actions in respect of the collateral and ensures a priority waterfall from the proceeds of enforcement over collateral. It entitles second lien lenders to receive and retain payments of interest, principal and other amounts in respect of a second lien obligation unless the receipt results from an enforcement step in respect of the collateral. By contrast, payment subordination means that subordinate lenders have also subordinated in favour of the senior lender their right to payment and have agreed to turn over all money received, whether or not derived from the proceeds of the common collateral [5] . The intercreditor agreement is a lien subordination agreement, as stated in section 8.2.

56 Nelson and the first lien agent say that RBC has no right to ask the Court to order any payments to it from the cash on hand prior to the closing of the transaction. They rely on the language of section 3.1(a)(1) that provides that until the discharge of the first lien obligations, the second lien collateral agent will not exercise any rights or remedies with respect to any collateral, institute any action or proceeding with respect to such remedies including any enforcement step under the second lien documents. RBC says it is not asking to enforce its security rights but merely asking that it be paid what it is owed and is permitted to receive under the intercreditor agreement, which does not subordinate payments but only liens. It points to section 3.1(c) that provides that:

> (c) Notwithstanding the foregoing (i.e. section 3.1(a)(1)) the Second Lien Collateral Agent and any Second Lien Claimholder may (1)... and may take such other action as it deems in good faith to be necessary to protect its rights in an insolvency proceeding" and (4) may file any... motions... which assert rights... available to unsecured creditors...arising under any insolvency... proceeding.

57 My view of the intercreditor agreement language and what has occurred is that RBC has not taken enforcement steps with respect to collateral. It has asked that payments owing to it under the second lien credit agreement up to the date of filing be paid.

58 Payment of what the second lien lenders are entitled to under the second lien credit agreement is protected under the intercreditor agreement unless it is as the result of action taken by the second lien lenders to enforce their security. Section 3.1(f) of the intercreditor agreement provides as follows:

> (f) Except as set forth is section 3.1(a) and section 4 to the extent applicable, nothing in this Agreement shall prohibit the receipt by the Second Lien Collateral Agent or any Second Lien Claimholders of the required payments of interest, principal and other amounts owed in respect of the Second Lien Obligations or receipt of payments permitted under the First Lien Loan Documents, including without limitation, under section 7.09(a) of the First Lien Credit Agreement, so long as such receipt is not the direct or indirect result of the exercise by the Second Lien Collateral Agent or any Second Lien Claimholders of rights or remedies as a secured creditor (including set off) or enforcement in contravention of this Agreement. ... (underlining added).

59 Section 3.1(a) prohibits the second lien lenders from exercising any rights or remedies with respect to the collateral before the first liens have been discharged. Section 4 requires any collateral or proceeds thereof received by the first lien collateral agent from a sale of collateral to be first applied to the first lien obligations and requires any payments received by the second lien lenders from collateral in connection with the exercise of any right or remedy in contravention of the agreement must be paid over to the first lien collateral agent.

60 It do not agree with the first lien collateral agent that payment to RBC before the sale closes of amounts owing pre-filing under the second lien credit agreement would be in contravention of section 4.1. That section deals with cash from collateral being received by the first lien collateral agent in connection with a sale of collateral, and provides that it shall be applied to the first lien obligations until those obligations have been discharged. In this case, the cash on hand before any closing will not be received by the first lien collateral agent at all. It will be received after the closing by the purchaser.

61 The first lien collateral agent has made a credit bid on behalf of the first lien lenders. Pursuant to section 3.1(b), that credit bid is deemed to be an exercise of remedies with respect to the collateral held by the first lien lenders. Under the last paragraph of section 3.1(c), until the discharge of the first lien obligations has occurred, the sole right of the second lien collateral agent and the second lien claimholders with respect to the collateral is to hold a lien on the collateral pursuant to the second lien collateral documents and to receive a share of the proceeds thereof, if any, after the discharge of the first lien obligations has occurred. That provision is as follows:

> Without limiting the generality of the foregoing, unless and until the discharge of the First Lien Obligations has occurred, except as expressly provided in Sections 3.1(a), 6.3(b) and this Section 3.1(c), the sole right of the Second Lien Collateral Agent and the Second Lien Claimholders with respect to the Collateral is to hold a Lien of the Collateral pursuant to the Second Lien Collateral Documents for the period and to the extend granted therein and to receive a share of the proceeds thereof, if any, after the Discharge of First Lien Obligations has occurred.

62 RBC points out that its rights under section 3.1(f) to receive payment of amounts owing to the second lien lenders is not subject to section 3.1(c) at all. It is not suggested by the first lien collateral agent that this is a drafting error, but it strikes me that it may be. The provision at the end of section 3.1(c) is inconsistent with section 3.1(f) as section 3.1(c) is not an exception to section 3.1(f).

63 Both the liens of the first lien lenders and the second lien lenders are over all of the assets of Nelson. Cash is one of those assets. Therefore if payment were now made to RBC from that cash, the cash would be paid to RBC from the collateral for amounts owing under the second lien credit agreement before the obligations to the first lien lenders were discharged. The obligations to the first lien lenders will be discharged when the sale to the purchaser takes place and the first lien obligations are cancelled.

64 There is yet another provision of the intercreditor agreement that must be considered. It appears to say that if a judgment is obtained in favour of a second lien lender after exercising rights as an unsecured creditor, the judgment is to be considered a judgment lien subject to the intercreditor agreement for all purposes. Section 3.1(e) provides:

(e) Except as otherwise specifically set forth in Sections 3.1(a) and (d), the Second Lien Collateral Agent and the Second Lien Claimholders may exercise rights and remedies as unsecured creditors against the Company or any other Grantor that has guaranteed or granted Liens to secure the Second Lien Obligations in accordance with the terms of the Second Lien Loan Documents and applicable law; provided that in the event that any Second Lien Claimholder becomes a judgment creditor in respect of Collateral as a result of its enforcement of its rights as an unsecured creditor with respect to the Second Lien Obligations, **such judgment Lien** shall be subject to the terms of this Agreement for all purposes (including in relation to the First Lien Obligations) as the other Liens securing the Second Lien Obligations are subject to this Agreement. (Emphasis added).

65 What exactly is meant by a "judgment Lien" is not stated in the intercreditor agreement and is not a defined term. If an order is made in this CCAA proceeding that the pre-filing obligations to the second lien collateral agent are to be paid from the cash on hand that Nelson holds, is that a "judgment Lien" meaning that it cannot be exercised before the first lien obligations are discharged? In this case, as the first lien obligations will be discharged as part of the closing of the transaction, does that mean that once the order is made approving the sale and the transaction closes, the cash on hand will go to the purchaser and the judgment Lien will not be paid? It is not entirely clear. But the section gives some indication that a judgment held as a result of the second lien agent exercising rights as an unsecured creditor cannot be used to attach collateral contrary to the agreement if the first lien obligations have not been discharged.

66 I have been referred to a number of cases in which statements have been made as to the need for the priority of secured creditors to be recognized in CCAA proceedings, particularly when distributions have been ordered. While in this case we are not dealing with a distribution generally to creditors, the principles are well known and undisputed. However, in considering the priorities between the first and second lien holders in this case, the intercreditor agreement is what must govern, even with all of its warts.

67 In this case, the cash on hand held by Nelson is collateral, and subject to the rights of the first lien lenders in that collateral. An order made in favour of RBC as second lien agent would reduce that collateral. The overall tenor of the intercreditor agreement, including section 3.1(e), leads me to the conclusion that such an order in favour of RBC should not be made. I do say, however, that the issue is not at all free from doubt and that no credit should be given to those who drafted and settled the intercreditor agreement as it is far from a model of clarity. I decline to make the order sought by RBC.

68 I should note that RBC has made a claim that that Nelson and the first lien lenders who signed the First Lien Support Agreement acted in bad faith and disregarded the interests of the second lien lenders under the intercreditor agreement. RBC claims that the first lien lenders induced Nelson to breach the second lien credit agreement and that this breach resulted in damages to the second lien agent in the amounts of US$15,365,998.83 on account of interest and CDN$1,316,181.73 on account of fees. RBC says that these wrongs should be taken into account in considering whether the credit bid should be accepted and that the powers under section 11 of the CCAA should be exercised to order these amounts to be paid to RBC as second lien agent.

69 I decline to do so. No decision on this record could be possibly be made as to whether these wrongs took place. The claim for inducing breach of contract surfaced in the RBC factum filed just two days before the hearing and it would be unfair to Nelson or the first lien lenders to have to respond without the chance to fully contest these issues. Moreover, even the release sought by the applicants would not prevent RBC or any second lien lender from bringing an action for wrongs committed. RBC is able to pursue relief for these alleged wrongs in a separate action.

(b) Consent fee

70 The first lien lenders who signed the First Lien Support Agreement were paid a consent fee. That agreement, and particularly the term sheet made a part of it, provided that those first lien lenders who signed the agreement would be paid a consent fee.

71 RBC contends that because the consent fee was calculated for each first lien lender that signed the First Lien Support Agreement on the amount of the loans that any consenting first lien lenders held under the first lien credit agreement, the consent fee was paid on account of the loans and thus because all first lien lenders were to be paid equally on their loans on a pro rata basis, RBC is entitled to be paid its share of the consent fees.

72 Section 2.14 of the first lien credit agreement provides in part, as follows:

> If, other than as expressly provided elsewhere herein, **any Lender shall obtain on account of the Loans made by it**, or the participations in L/C Obligations and Swing Line Loans held by it, **any payment** (whether voluntary, involuntary, through the exercise of any right of setoff, or otherwise) **in excess of its ratable share** (or other share contemplated hereunder) thereof, such Lender shall immediately (a) notify the Administrative Agent of such fact, and (b) purchase from the other Lenders such participations in the Loans made by them and/or such subparticipations in the participations in L/C Obligations or Swing Line Loans held by them, as the case may be, as shall be necessary to cause such purchasing Lender to share the excess payment in respect of such Loans or such participations, as the case may be, pro rata with each of them ... [emphasis added].

73 RBC says that while the section refers to a first lien lender obtaining a payment "on account" of its loan, U.S. authorities under the U.S. Bankruptcy Code have held that the words "on account of" do not mean "in exchange for" but rather mean "because of." As the consent payments are calculated on the amount of the loan of any first lien lender who signed the term sheet, RBC says that they were made because of their loan and thus RBC is entitled to its share of the consent fees that were paid by virtue of section 2.14 of the first lien credit agreement.

74 I do not accept that argument. The consent fees were paid because the consenting first lien lenders signed the First Lien Support Agreement. The fact that their calculation depended on the amount of the loan made by each consenting first lien lender does not mean they were made because of the loan. RBC declined to sign the First Lien Support Agreement and is not entitled to a consent fee.

Conclusion

75 An order is to go in accordance with these reasons. As there has been mixed success, there shall be no order as to costs.

Company's motion granted; bank's motion dismissed.

Footnotes

1 I do not think that Mr. Gropper's views on what particular sections of the agreement meant is the proper subject of expert opinion on foreign law. Such an expert should confine his evidence to a statement of what the law is and how it applies generally and not express his opinion on the very facts in issue before the court. See my comments in *Nortel Networks Corp., Re* (2014), 20 C.B.R. (6th) 171 (Ont. S.C.J. [Commercial List]) para. 103.

2 See *Nortel Networks Corp., Re* (2009), 55 C.B.R. (5th) 229 (Ont. S.C.J. [Commercial List]) at paras. 35-40 and *Brainhunter Inc., Re*, [2009] O.J. No. 5207 (Ont. S.C.J. [Commercial List]) at paras. 12-13.

3 *Royal Bank v. Soundair Corp.* (1991), 7 C.B.R. (3d) 1 (Ont. C.A.).

4 This case does not involve a plan under the CCAA. One of the reasons for this may be that pursuant to section 6.9(b) of the intercreditor agreement, in the event the applicants commence any restructuring proceeding in Canada and put forward a plan, the applicants, the first lien lenders and the second lien lenders agreed that the first lien lenders and the second lien lenders should be classified together in one class. The second lien lenders agreed that they would only vote in favour of a plan if it satisfied one of two conditions, there was no contractual restriction on their ability to vote against a plan.

5 See 65 A.B.A. Bus Law. 809-883 (May 2010).

End of Document

Tab 5

2011 ABQB 214
Alberta Court of Queen's Bench

Kerr Interior Systems Ltd., Re

2011 CarswellAlta 508, 2011 ABQB 214, [2011] 10 W.W.R. 159, [2011] A.W.L.D. 2318, 200 A.C.W.S. (3d) 930, 43 Alta. L.R. (5th) 386, 517 A.R. 186, 79 C.B.R. (5th) 1

In the Matter of the Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36, as amended

And In the Matter of the Plan of Compromise or Arrangement of
Kerr Interior Systems Ltd. and Composite Building Systems Inc.

J.E. Topolniski J.

Judgment: March 30, 2011
Docket: Edmonton 0703-14357

Counsel: Darren Bieganek for Applicant
James Hanley for Respondent

Subject: Insolvency; Corporate and Commercial

APPLICATION by debtors for further meeting of creditors to reconsider plan of arrangement made pursuant to *Companies' Creditors Arrangement Act* after court sanction and part performance.

***J.E. Topolniski J.*:**

I. Introduction

1 This case concerns the court's jurisdiction to authorize debtors to call a further meeting of creditors to reconsider a plan of arrangement (the "Plan") made pursuant to the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36 ("*CCAA*") after court sanction and part performance. The Plan called for payment of $2,600,000.00, including a first installment of $260,000.00 (the "Payment").

2 Kerr Interior Systems Ltd. ("Kerr") and Composite Building Systems Inc. ("Composite") (collectively the "Debtors") obtained an initial *CCAA* order granting them the usual stay of proceedings and protections on November 7, 2007 ("Initial Order"). Kerr's primary business is the supply and installation of commercial steel stud and drywall load bearing frames. Composite was in the business of fabricating the steel panels installed by Kerr, but ceased operating and transferred its assets to Kerr sometime between the fall of 2009 and the spring of 2010. It is unclear whether Composite is back in business today.

3 The restructuring followed a fairly typical course of proceedings under the *CCAA*. There was a period of time dedicated to reorganization and formulating the Plan, followed by a favourable creditor vote and an order sanctioning the Plan (the "Sanction Order"). The restructuring went sideways when the Debtors defaulted after making the first of four instalment payments due under the Plan.

4 Claiming that an unexpected downturn in the economy, difficulty collecting accounts receivable, the strain of servicing secured debt, and the obligations of a related entity (that is not part of the *CCAA* proceeding) have created insurmountable impediments to their ability to carry on in business and to satisfy their obligations under the Plan, the Debtors want to present another offer to their creditors. If successful in their bid for another creditors' meeting, they

propose to ask their creditors to accept a global payment of $520,000.00 (comprised of the Payment and an additional $260,000.00 to be paid at a later unspecified date). The Debtors are cognizant that they can pursue restructuring under the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3 or by making a further *CCAA* filing, but they consider those avenues too expensive and unnecessary.

5 In a rather cursory report to the court, BDO Canada Limited (the "Monitor") expressed the view that the Debtors appear to be acting in good faith and their application "does not seem to be unreasonable" in light of economic conditions.

6 Two creditors oppose the application, Winroc, a division of Superior Plus LP ("Winroc"), and Descon Mechanical Protostatix Engineering. A third creditor, Kenroc Building Materials Ltd. ("Kenroc"), voiced support for Winroc's position (collectively the "Opposing Creditors"). The Opposing Creditors argue that the court does not have jurisdiction to call a further meeting of creditors at the post-sanction stage of the proceedings and, in any event, the relief sought is a collateral attack on the Sanction Order. They submit that to authorize a further meeting of the creditors would open the floodgates to such applications and result in uncertainty in *CCAA* proceedings.

7 There are no reported cases directly on point. The outcome of this application hinges on statutory interpretation and the analysis of reported cases involving analogous situations.

II. The Issues

8 The following two issues arise on this application:

1. Does the court have jurisdiction to call a further meeting of creditors following the court's sanctioning of the Plan?

2. If yes, should the court direct a further meeting of creditors on the facts of this case?

III. Factual Context

9 On January 31, 2008, the Debtors' unsecured creditors voted in favour of the Plan, which provided for a global payment of $2,600,000.00 to be paid in four instalments of varying amounts. On the application for court approval of the Plan, Kenroc and Winroc were unsuccessful in arguing that they should not be listed under the Plan as unsecured creditors but rather as secured creditors with builders' lien claims in Saskatchewan or, alternatively that they should be put in a separate voting class and, in any event, were entitled to the $150,000.00 paid into court by a third party to discharge their builders' liens. On April 4, 2008, Bielby J. (as she then was) granted the Sanction Order (2008 ABQB 286, 449 A.R. 185 (Alta. Q.B.)).

10 Kenroc and Winroc appealed the Sanction Order to the Alberta Court of Appeal, which ruled (2009 ABCA 240, 457 A.R. 274 (Alta. C.A.)) that they met the test for classification as secured creditors (by way of lien or trust) and that they were entitled to the $150,000.00 that had been paid into court. The Sanction Order and Plan otherwise remained unaffected.

11 The Debtors made the first instalment payment under the Plan, the $260,000.00 Payment, but failed to make the second instalment of $720,000.00. They have since unsuccessfully sought informal creditor approval to alter the Plan. One year later and despite the Debtors' default, no creditor has sought to vacate the stay of proceedings.

12 In November 2007, when the Debtors crafted their proposal to the creditors, their combined value was $2,700,000.00, comprised of accounts receivable ($1,900,000.00) and other assets ($800,000.00). They considered that an offer of $2,400,000.00 (or 50 cents on the dollar) was reasonable for all concerned. At the creditors' meeting, they topped up the offer by $200,000.00, offering a global payment of $2,600,000.00. The creditors agreed to that deal.

13 What is known of the Debtors' affairs since the Sanction Order includes the following:

(a) Kerr had 13 to 15 salaried employees in 2008-2009. That number increased to 50 by the fall of 2010.

(b) The Debtors' combined 2008 revenue was $14,000,000. Profits were two to three percent.

(c) Kerr's asset value in 2009 was $4,800,000.00. The Debtors' combined revenue in 2009 was $8,000,000.00. Kerr enjoyed a $167,055.00 profit, while Composite lost $571,307.00 that year.

(d) By May 31, 2010:

(i) Composite was out of business;

(ii) Kerr had revenue of $6,500,000.00, with a profit of $79,809.00;

(ii) Kerr's accounts receivable stood at $1,790,000.00, $600,000.00 to $700,000.00 of which likely was stale dated. Kerr considers all but $100,000.00 of its three major accounts receivable (totalling $585,000.00) to be potentially collectible; and

(iv) $2,200,000.00 of Kerr's accounts payables are owed to related parties, either to Composite or numbered companies owned or controlled by Kerr's shareholders.

(e) At present, Kerr has work in progress and is cautiously optimistic about future revenues. It is unclear whether Composite is operating again.

14 The Debtors point to the obligations of 1005559 Alberta Ltd. ("1005559"), a related company, as another impediment to their ability to fulfill the terms of the Plan. They submit that the following transactions are germane to the present application:

(a) 1005559 borrowed $3,900,000.00 to buy and renovate a building for the Debtors' use (the "Building"). Of that amount, $3,000,000.00 was still owing at the date of the Initial Order. 1005559 sold the Building for an unknown sum. It also created a $100,000.00 builders' lien fund for persons claiming for work done on renovations to the Building.

(b) 1005559 pledged its assets in favour of the Royal Bank of Canada under a general security agreement to secure a $1,800,000.00 loan to the Debtors (the general security agreement subsequently was assigned to a takeout financier).

(c) 1005559 granted a $2,000,000.00 mortgage to an investor group that had threatened litigation. The court was not advised as to the composition of this investor group or the party threatened by litigation.

15 Darryl Wiebe, a shareholder, director and officer of Kerr, was questioned about why Kerr wanted to reduce the Debtors' obligations under the Plan when it had saleable assets to fund the Plan and the economy was improving. His response was: "[w]ell, frankly we'd like to get it out of our hair."

IV. Legislative Context

16 Sections 4 to 7 and 11 of the *CCAA* are relevant to this application.

17 Section 4, which concerns the court ordering a meeting of creditors to consider compromises with unsecured creditors, reads:

4. Where a compromise or an arrangement is proposed between a debtor company and its unsecured creditors or any class of them, the court may, on the application in a summary way of the company, of any such creditor or of

> the trustee in bankruptcy or liquidator of the company, order a meeting of the creditors or class of creditors, and, if the court so determines, of the shareholders of the company, to be summoned in such manner as the court directs.

18 Section 5 is identical except that it concerns a compromise or an arrangement between the debtor company and its secured creditors.

19 Section 6 deals with court sanction of compromises. It outlines a number of restrictions on when a plan of arrangement can be sanctioned, none of which are relevant to this inquiry. However, ss. 6(1)(a) is of relevance. It refers to modification of a proposed compromise or arrangement at a meeting of creditors, stating:

> 6(1) If a majority in number representing two thirds in value of the creditors, or the class of creditors, as the case may be - other than, unless the court orders otherwise, a class of creditors having equity claims, - present and voting either in person or by proxy at the meeting or meetings of creditors respectively held under sections 4 and 5, or either of those sections, agree to any compromise or arrangement either as proposed or as altered or modified at the meeting or meetings, the compromise or arrangement may be sanctioned by the court and, if so sanctioned, is binding
>
> > (a) on all the creditors or the class of creditors, as the case may be, and on any trustee for that class of creditors, whether secured or unsecured, as the case may be, and on the company; and ...

20 Section 7 concerns the adjournment of creditors' meetings when amendments to a compromise or plan of arrangement are proposed. It reads:

> 7. Where an alteration or a modification of any compromise or arrangement is proposed at any time after the court has directed a meeting or meetings to be summoned, the meeting or meetings may be adjourned on such term as to notice and otherwise as the court may direct, and those directions may be given after as well as before adjournment of any meeting or meetings, and the court may in its discretion direct that it is not necessary to adjourn any meeting or to convene any further meeting of any class of creditors or shareholders that in the opinion of the court is not adversely affected by the alteration or modification proposed, and any compromise or arrangement so altered or modified may be sanctioned by the court and have effect under section 6.

21 Section 11, which describes the court's plenary jurisdiction, provides that:

> 11. Despite anything in the *Bankruptcy and Insolvency Act* or the *Winding-up and Restructuring Act*, if an application is made under this Act in respect of a debtor company, the court, on the application of any person interested in the matter, may, subject to the restrictions set out in this Act, on notice to any other person or without notice as it may see fit, make any order that it considers appropriate in the circumstances.

V. Analysis

22 Statutes are to be interpreted purposively and contextually. The words used are to be read in their entire context and in their grammatical and ordinary sense harmoniously with the scheme of the legislation, its object and with Parliament's intention (*Rizzo & Rizzo Shoes Ltd., Re*, [1998] 1 S.C.R. 27 (S.C.C.) at para. 21, (1998), 221 N.R. 241 (S.C.C.); *Bell ExpressVu Ltd. Partnership v. Rex*, 2002 SCC 42 (S.C.C.) at para. 26, [2002] 2 S.C.R. 559 (S.C.C.)). Every word is presumed to make sense and to have a specific role to play in advancing the *CCAA*'s purpose (*Placer Dome Canada Ltd. v. Ontario (Minister of Finance)*, 2006 SCC 20 (S.C.C.) at para 45, [2006] 1 S.C.R. 715 (S.C.C.), citing R. Sullivan, *Driedger on the Construction of Statutes*, 3rd ed. (Toronto: Butterworths, 1994) at p. 159).

23 The *CCAA* is remedial legislation. Its goals include the following:

> (i) permitting debtors to continue in business and, where possible, avoid the social and economic costs of liquidation (*Ted Leroy Trucking Ltd., Re*, 2010 SCC 60 (S.C.C.) at para. 15 [hereinafter Century Services Inc.]);

(ii) balancing stakeholder interests (*Nova Metal Products Inc. v. Comiskey (Trustee of)* (1990), 1 O.R. (3d) 289, 1 C.B.R. (3d) 101 (Ont. C.A.); *Air Canada, Re* (2004), 47 C.B.R. (4th) 189 (Ont. S.C.J. [Commercial List]); and

(iii) protecting creditors' interests and permitting an orderly administration of the debtor's affairs (*Meridian Development Inc. v. Toronto Dominion Bank* (1984), 53 A.R. 39, 52 C.B.R. (N.S.) 109 (Alta. Q.B.)).

(iv) rehabilitating companies that are key elements in a complex web of interdependent economic relationships in order to avoid the negative consequences of liquidation (*Century Services Inc.* at para. 18).

24 In this vein, Parliament is said to have understood in adopting the *CCAA* that liquidation of an insolvent company is harmful for most of those it affects, notably creditors and employees. Corporate reorganization under the *CCAA* serves the public interest by facilitating corporate survival (*Century Services Inc.* at paras. 17 and 18).

25 Proceedings under the *CCAA* are designed to be flexible and responsive, with a view to providing fairness, certainty and stability for the stakeholders. The *CCAA* is to be liberally interpreted to achieve those ends.

26 *CCAA* jurisdiction is conferred on superior courts vested with inherent and equitable jurisdiction. The present jurisprudential trend is for courts to employ their inherent and equitable jurisdiction only as a tool of last resort when the language of the *CCAA* cannot be interpreted to anchor an intended measure to be taken in the *CCAA* proceedings (G. R. Jackson and J. Sarra, "Selecting the Judicial Tool to Get the Job Done: An Examination of Statutory Interpretation, Discretionary Power and Inherent Jurisdiction in Insolvency Matters" in J. P. Sarra, ed., *Annual Review of Insolvency Law 2007* (Toronto: Thomson Carswell, 2008) 41 at 42, cited in *Century Services Inc.* at para. 65).

27 Extensive amendments to the *CCAA* in 2008 (2007, c. 36) codified various measures previously undertaken by the court through the exercise of what was referred to in *Century Services Inc.*. at paras. 62 and 63 as "creative use of authority" and "judicial innovation;" for example, imposing priority charges for critical suppliers or debtor in possession ("DIP") financing (now termed "interim financing") and releasing claims against third parties.

28 With these contextual considerations and directives in mind, I now turn to an analysis of ss. 4 to 7 and 11 of the *CCAA* and the relevant authorities in order to assess whether this court has the discretion to call a further meeting of the Debtors' creditors and, if it does, whether the court should exercise that discretion in the circumstances of this case.

29 Calling a meeting of creditors pursuant to s. 4 or 5 is discretionary. A refusal to summon a creditors' meeting often is attributable to the court's determination that the compromise or plan of arrangement is contrary to the creditors' interests (*Avery Construction Co., Re*, [1942] 4 D.L.R. 558, 24 C.B.R. 17 (Ont. S.C.)), it is doomed to failure due to a lack of creditor support (*Fracmaster Ltd., Re*, 1999 ABQB 379, 11 C.B.R. (4th) 204 (Alta. Q.B.), aff'd 1999 ABCA 178, 11 C.B.R. (4th) 230 (Alta. C.A.)), or there is no reasonable chance the debtor will be able to continue in business (*First Treasury Financial Inc. v. Cango Petroleums Inc.* (1991), 78 D.L.R. (4th) 585, 3 C.B.R. (3d) 232 (Ont. Gen. Div.)).

30 The court's sanction of a compromise or plan of arrangement under s. 6 also is discretionary. A compromise or plan of arrangement is enforceable only if and when sanctioned by the court (*Cable Satisfaction International Inc. v. Richter & Associés inc.* (2004), 48 C.B.R. (4th) 205 (C.S. Que.)), although court sanction is not necessary to bind the parties to an inter-creditor agreement in a compromise or plan of arrangement (*Air Canada, Re* (2004), 2 C.B.R. (5th) 4 (Ont. S.C.J. [Commercial List]) at para. 6).

31 Section 6 expressly permits court sanction of a compromise or plan of arrangement amended at the creditors' meeting, so long as the required majority of those voting in person or by proxy at the creditors' meeting agreed to the amended plan. It is clear from this section that amendments to the plan may be proposed at the meeting and the plan as amended may be put to a vote.

32 Pursuant to s. 7, where an amendment to the plan is proposed after the creditors' meeting has been scheduled, the meeting may be adjourned on such term as to notice or otherwise as directed by the court, presumably to allow the

creditors more time to consider the proposed amendment. Use of the term "adjourned" implies that the creditors' meeting has not yet been held or that the vote has not yet been taken as otherwise there would be nothing to adjourn.

33 If the court is of the opinion that the proposed amendment does not adversely affect a particular class of creditors, the court has the discretion under s. 7 to direct that the meeting of that class need not be adjourned or a further meeting of that class need not be convened. Again, the reference to adjournment implies that the meeting of and voting by the creditors or class of creditors have not yet occurred, whereas use of the phrase "convene any further meeting" suggests that the meeting and vote of the creditors or particular class of creditors have taken place. It is not clear whether the provisions of s. 7 relating to proposed non-prejudicial amendments apply once the court has sanctioned the plan.

34 Section 7 does not address whether the court can convene a further meeting of creditors to consider a proposed substantive amendment once the creditors' meeting and vote have taken place. Further, the section is silent as to whether the court can convene a further meeting of the creditors to consider such a proposal once the plan has received court sanction - the issue which arises on this application.

35 A review of case law relating to amendments made under s. 7 is instructive as to the nature and timing of permissible court intervention after the creditors' vote has taken place.

36 Section 7 has been interpreted as allowing substantive (i.e prejudicial) amendments only at the pre-vote stage. In *Central Guaranty Trustco Ltd., Re* (1993), 21 C.B.R. (3d) 139 (Ont. Gen. Div. [Commercial List])), Farley J. commented (at para. 11):

> ... In ***Algoma Steel Corp. v. Royal Bank of Canada*** (1992), 8 O.R. (3d) 449, the Court of Appeal determined that there were exceptional circumstances (unrelated to the Plan) which allowed it to adjust a Plan where no interest was adversely affected. The same cannot be said here. FSTQ aside from s. 11(c) of the *CCAA* also raised s. 7. I am of the view that s. 7 allows an amendment after an adjournment — but not after a vote has been taken.

37 Section 7 also has been interpreted as permitting judicial amendments of a technical non-prejudicial nature at the sanction stage (*Wandlyn Inns Ltd., Re* (1992), 15 C.B.R. (3d) 316 (N.B. Q.B.)). Even then, the court's jurisdiction to allow a judicial amendment must be exercised sparingly, in exceptional circumstances, and only if permitted by the *CCAA* (*Algoma Steel Corp. v. Royal Bank* (1992), 11 C.B.R. (3d) 11 (Ont. C.A.), at 15; *Sammi Atlas Inc., Re* (1998), 3 C.B.R. (4th) 171 (Ont. Gen. Div. [Commercial List]) at para. 6). The court's jurisdiction does not extend to modifying plans of arrangement simply because a person is dissatisfied with the existing plan (*Daon Development Corp., Re* (1984), 10 D.L.R. (4th) 216 (B.C. S.C.) at para. 9.

38 In Houlden and Morawetz's *Bankruptcy and Insolvency Law of Canada*, 4th ed., vol. 4 (Toronto: Carswell, 2009) at p. 11-69, N§48, the authors observe that: "[a]lthough it would seem that once the plan has been sanctioned by the court, the court has no power to make any alterations or modifications in it, there are cases where orders have been made altering or modifying a plan after it has been sanctioned." They then cite a number of authorities, including those discussed below.

39 In *Northland Properties Ltd., Re* (1989), 74 C.B.R. (N.S.) 231 (B.C. S.C. [In Chambers]), a *CCAA* debtor successfully applied five months after the sanction order to rectify a unilateral mistake made by it in electing a mortgage rate under the plan of arrangement. The court focussed its analysis on whether this type of unilateral mistake was subject to rectification. In any event, the circumstances in that case are distinguishable from the situation here of a default at the implementation stage of *CCAA* proceedings.

40 *Royal Heaters Ltd., Re* (1947), 30 C.B.R. 199 (C.S. Que.) concerned a series of post-sanction applications by a *CCAA* debtor for orders extending the time to make payments and temporarily suspending payments under the plan of arrangement. The debtor in that case, like the Debtors here, claimed that economic conditions had impaired its ability to honour its obligations under the plan. While the amendments clearly were prejudicial, the majority of the creditors

in number and value consented to at least one of the extensions. Without discussing its jurisdiction to approve the amendments, the court granted the extensions, observing that it was in the interest of the creditors to do so.

41 In *Keddy Motor Inns Ltd., Re* (1992), 13 C.B.R. (3d) 262, 113 N.S.R. (2d) 431 (N.S. T.D. [In Chambers]), a sanctioned plan of arrangement specified certain payment dates that could not be complied with because of an extant appeal. Without reference to ss. 7 or 11, the court approved a change in those dates.

42 In *Algoma Steel Corp. v. Royal Bank* (1992), 8 O.R. (3d) 449 (Ont. C.A.), leave to appeal to S.C.C. refused (1992), 10 O.R. (3d) xv (note) (S.C.C.), the Ontario Court of Appeal considered whether the existence of a sanctioned plan of arrangement under the *CCAA* prevented the court from permitting the applicant to sue the debtor to the limited extent of certain insurance proceeds. The court determined that the power to amend the plan in the manner sought could be found, by inference, in what is now s. 11.02 (the stay provision) of the *CCAA*. It was argued in that case that having regard to the commercial realities reflected by the *CCAA*, the power to allow an action to proceed could only be exercised before the creditors' vote. The court held that, as a matter of principle, there was no reason to suggest the court's power was limited in that way, although given "the primacy accorded by the Act to agreement among the affected actors, the jurisdiction of the court is to be exercised sparingly and in exceptional circumstances only, if the result of the exercise is to amend the plan, even in merely a technical way." It commented that it would be an unacceptable exercise of jurisdiction if the effect of granting the applicant leave to sue the debtor would be to make any assets other than the insurance proceeds vulnerable to possible execution. It noted that the proposed amendment to the plan was insignificant and technical only as far as the other creditors were concerned.

43 The applicant creditor in *Ontario v. Canadian Airlines Corp.*, 2001 ABQB 983, 306 A.R. 124 (Alta. Q.B.) sought a declaration that the portion of the debt owed to it which was secured by letters of credit was not compromised by the plan of arrangement which had received court sanction. In the alternative, it asked for an order varying the plan to permit the liability secured by the letters of credit to be considered a secured claim and directing that the debtor was liable for the full amount of that liability up to the value of the letters of credit. The court dealt with the issue as one of interpretation and application of the plan, rather than its amendment.

44 However, in *obiter dicta*, Madam Justice Romaine expressed the view (at para. 61) that the court retains jurisdiction at the post-sanction stage to direct amendment to the plan, reasoning that:

> The *CCAA* authorizes the court to amend a plan in appropriate circumstances, where there are compelling reasons to do so. Although the Act does not expressly state that such amendment could take place after the Plan is sanctioned, as pointed out in ***Algoma***, *supra* there is no reason to suggest that the *CCAA* "contemplates a role for the court as a mere rubber stamp or one that is simply administrative rather than judicial" (p.103). While the circumstances justifying an amendment after a sanction hearing ought to be truly exceptional, in recognition of the potential violence done to the laudable goal of commercial certainty, there is no reason why subsequent amendments should be conclusively foreclosed in every case, without examination of the particular circumstances.

45 Romaine J. commented at para. 56 that ss. 6 and 7 offer no guidance on whether a court-sanctioned plan may subsequently be amended. However, at para. 57, she noted:

> As mentioned, the *CCAA* confers broad discretion on the court and is to be afforded a large and liberal interpretation: ***Re Canadian Airlines Corp.***, *supra* at para 95 (Q.B); ***Chef Ready Foods Ltd. v. Hongkong Bank of Canada*** (1990), 51 B.C.L.R. (2d) 84 (C.A.). It is silent, however, on many procedural issues. Given the lack of legislative guidance, the courts have used the basic purpose of the *CCAA* as a guide to its application and the exercise of its discretion in disposing of applications under the Act: ***Re Canadian Airlines Corp.***, *supra* at para. 95. The keynote concepts of fairness and reasonableness have been recognized as the driving force behind the *CCAA* and the court's interpretation and application of the Act: ***Re Canadian Airlines Corp.*** at para. 95, ***Re Canadian Airlines Corp.***, *supra* at p. 9.

46 In concluding that amendment of the plan would recognize the concepts of fairness and reasonableness to a greater extent than would interpreting the plan in the manner advocated by the debtor, Romaine J. took into consideration that the claims procedure in that case had been unique in that it allowed the debtor to unilaterally categorize its creditors and required that any creditor which did not agree with the classification file a dispute note. She also considered that the applicant creditor had not become aware that the debtor was rejecting its claim as being out of time until the last day and that no evidence of the creditor's position was presented to the court at the sanction hearing. In addition, she noted that no creditor or debtor prejudice would result from the sought after amendment.

47 As the proposed amendment in *Ontario* was non-prejudicial to the debtor and creditors, the court's jurisdiction to make the amendment might have been based on s. 7 or the court's plenary jurisdiction as set out in s. 11.

48 Madam Justice Romaine again was asked to consider amending a plan of arrangement at the post-sanction stage in *Teragol Investments Ltd. v. Hurricane Hydrocarbons Ltd.*, 2005 ABQB 324, 382 A.R. 383 (Alta. Q.B.). In refusing the application, she commented (at para. 21) that a post-sanction amendment should be limited to truly exceptional circumstances as such an amendment has the potential to do violence to the goal of commercial certainty.

49 In *Century Services Inc.*, the first case in which the Supreme Court of Canada was asked to directly interpret the provisions of the *CCAA*, Deschamps J., for the majority, discussed the source of the court's authority during *CCAA* proceedings and the boundary between the court's statutory authority under the Act and the residual authority under its inherent and equitable jurisdiction when supervising a reorganization. She noted that appellate courts were of the view that while lower courts might be purporting to rely on their inherent jurisdiction, in fact they were simply construing the authority supplied by the *CCAA* itself, citing *Skeena Cellulose Inc., Re*, 2003 BCCA 344, 13 B.C.L.R. (4th) 236 (B.C. C.A.) at paras. 45-47 and *Stelco Inc., Re* (2005), 75 O.R. (3d) 5 (Ont. C.A.) at paras. 31-33. She affirmed that the appropriate approach for a court to take is to rely first on a purposive and liberal interpretation of the *CCAA* text before turning to inherent or equitable jurisdiction to anchor measures taken in a *CCAA* proceeding. She accepted (at para. 66) that in most cases the issuance of an order in a *CCAA* proceeding should be considered to be an exercise in statutory interpretation, given the expansive interpretation the language of the statute is capable of supporting. The example she referred to was s. 11 of the *CCAA*, which was amended to make explicit the discretionary authority of the court under the *CCAA* and to endorse the broad reading of *CCAA* authority developed by the jurisprudence.

50 Deschamps J. instructed (at paras. 69 and 70) that while the *CCAA* explicitly provides for certain orders, the general language of the Act should not be read as being restricted by the availability of more specific orders. She indicated that the court should take into consideration appropriateness, good faith, and due diligence when exercising *CCAA* authority, explaining that:

> Appropriateness under the *CCAA* is assessed by inquiring whether the order sought advances the policy objectives underlying the *CCAA*. The question is whether the order will usefully further efforts to achieve the remedial purpose of the *CCAA* — avoiding the social and economic losses resulting from liquidation of an insolvent company. I would add that appropriateness extends not only to the purpose of the order, but also to the means it employs. Courts should be mindful that chances for successful reorganizations are enhanced where participants achieve common ground and all stakeholders are treated as advantageously and fairly as the circumstances permit.

51 Given a plain and contextual reading of the *CCAA*, augmented by guidance provided by the case law, I conclude that:

> (a) The courts' supervisory function ends only when the plan has been fully implemented or has failed. Parliament must have intended that the court retain jurisdiction to address issues that could arise during implementation of the plan, including whether to summon a further creditors' meeting after the creditors' vote or court sanction. Section 7 does not grant that jurisdiction. However, the court's discretionary authority under s. 11 is broad enough to encompass such a direction.

(b) In accordance with *Century Services Inc.*, the court's general discretionary authority under s. 11 should not be interpreted as being restricted by the more specific authority set out in s. 7.

(c) When exercising its authority under s. 11, the court must consider the good faith of the applicant, whether due diligence has been exercised and the appropriateness of making the order sought. In regard to the latter, the court should consider whether the relief sought advances the objectives of the *CCAA* and all relevant policy concerns.

(d) Parliament's intention could not have been to introduce uncertainty and instability to the process. On the contrary, stability, certainty and fairness for all are the recognized goals of the *CCAA*. The effect of the sanction order is relevant as it binds the parties and cements commercial certainty. Once sanctioned, creditors can take their contract with the debtor "to the bank" (for all that may be worth where, as in the present case, plan implementation is staged). In balancing the policy objectives of the *CCAA*, Parliament must have intended that while calling a further meeting of the creditors should remain an option, under certain circumstances, at any stage of the proceedings, once the creditors have voted and the plan has been sanctioned, the court should do so only in exceptional circumstances - circumstances well beyond foreseeable risks such as ordinary business risks.

(e) While each case must be determined on its unique facts, at a minimum, the court should consider the following non-exhaustive list of considerations (many of which overlap and all of which rest on the applicant to establish) before summoning a further meeting of the creditors at the post-sanction stage to vote on a proposed amendment to the plan:

(i) Is the plea for relief made in good faith?

(ii) Has it been made in a timely fashion?

(iii) Would granting the relief advance the policy objectives underlying the *CCAA*?

(iv) Would granting the relief enhance the public's confidence in the *CCAA* process?

(v) Would granting the relief otherwise serve the ends of justice?

(vi) What is the level of creditor support?

VI. Application to the Present Case

A. Is the Plea for Relief Made in Good Faith?

52 There was a lack of cogent evidence establishing that the Debtors have no hope of meeting their obligations under the Plan unless the creditors' meeting is allowed and the proposed amendment is passed.

53 It appears that the Debtors banked on a steady flow of work and the payment of certain receivables to fund the second installment due under the Plan. Neither transpired. However, since the fall of 2010, Kerr has experienced an increase in its work. It is unclear whether Composite is back in business today.

54 Mr. Weibe indicated that he is "cautiously optimistic" about the Debtors' future and, as evidenced by his answers given during cross-examination on his affidavit, the Debtors want matters with their pre-*CCAA* creditors to end; they want to get it "out of [their] hair." Doubtless, this is a common sentiment for any company in the process of restructuring.

55 While I accept that the Debtors have suffered some negative effects from a downturn in the economy, nevertheless I find it curious, and indeed troubling, that:

(i) since formulating the Plan their workforce has more than quadrupled;

(ii) they chose to rely (at least in part) on the impact of 1005559's debts to support their plea for relief;

(iii) the evidence fails to show that they have taken all reasonable steps to fund the Plan, including downsizing and selling non-essential assets.

56 In the result, despite the Monitor's comment (as stated in its fifth report to the court) that it is "... unaware of any facts to suggest that the Management of the Companies are not acting in good faith with respect to their creditors...", I am not so certain. In this regard, I am mindful that the Monitor's comment preceded the cross-examination on affidavit of Mr. Weibe that fleshed out much of the evidence that I have referred to in relation to this factor.

B. Is the Application Timely?

57 There is no suggestion that the Debtors delayed in bringing this application. The real concern is whether it is premature.

C. Would Granting the Relief Advance the Policy Objectives Underlying the CCAA?

58 The facts of this case reveal a tension between the objectives of facilitating restructuring and providing stability, certainty and fairness for all of the stakeholders. Avoiding a second, costly insolvency proceeding by allowing the Debtors to present a revised compromise, proposal, or plan of arrangement is a laudable goal. However, this would involve a tradeoff. The creditors voted on the Plan. Their agreement was cemented by the Sanction Order. They were entitled to rely on the deal and may have altered their own circumstances as a result of it. The Plan amendment proposed by the Debtors would see an eighty percent reduction in the amount the creditors originally accepted. So radical is this proposed change that it is more reasonably viewed as a completely new deal rather than an amendment.

59 While granting the relief would permit the creditors the opportunity to say whether the Debtors' proposed new deal is acceptable, other considerations also must be weighed. A non-exhaustive list of those considerations includes:

(i) the creditors' right to receive current financial information prepared in accordance with the requirements of s. 10(2);

(ii) meaningful compliance with the Monitor's duty to review the Debtors' s. 10(2) financial information as to its reasonableness (s.23(1)(b));

(iii) meaningful compliance with the Monitor's duty to report to the court about the fairness and reasonableness of the proposal (s. 23(1)(i));

(vi) the court's consideration of whether the proposal is workable (see *Royal Bank v. Fracmaster Ltd.*, 1999 ABCA 178, 244 A.R. 93 (Alta. C.A.), confirming *Royal Bank v. Fracmaster Ltd.*, 1999 ABQB 425, 245 A.R. 138 (Alta. Q.B.) in relation to a ss. 4 or 5 application).

These deficiencies might well be addressed by imposing conditions, but the benefit of that approach should be assessed contextually.

60 The demise of the Debtors is not a certainty if the relief is not granted. They can attempt to make another deal with their creditors in alternate insolvency proceedings, whether under the *BIA* or possibly another filing under the *CCAA*. As noted in L.W. Houlden and G.B. Morawetz's *Bankruptcy and Insolvency Law of Canada* (Toronto: Carswell, 2009), 4th ed. (rev'd), vol. 4, p. 11-28, there is nothing in the statute barring a second application. While the court in *Norseman Products Ltd., Re* (1949), 30 C.B.R. 71, [1950] O.W.N. 81 (Ont. S.C.) commented that a debtor company cannot claim the benefit of the *CCAA* more than once as this would lead to abuse, relying on *Comptoir coopératif du combustible Ltée, Re* (1935), 17 C.B.R. 124 (C.S. Que.), restructuring cases such as *Algoma Steel* suggest that a subsequent filing is appropriate where the statute affords an opportunity for a company to attempt to devise a revised business plan to

address its financial distress. Such proceedings come at a price, but given the Debtors' work on its propose revised deal to date and the cost of complying with conditions to address informational concerns, that price is likely less than might otherwise be incurred.

61 In the result, the Debtors have not shown that the policy objectives underlying the *CCAA* would be advanced or that the process would be served by granting them the opportunity to present their proposal to their creditors.

D. Would Granting the Relief Enhance the Public's Confidence in the CCAA Process?

62 The Debtors have experienced economic trouble which has been caused, at least in part, by a downturn in the condominium development industry. However, downturns in the condominium market, especially in the boom and bust economy of Alberta, are a foreseeable and ordinary business risk. There has been insufficient evidence presented establishing that this downturn is truly exceptional or was unforeseeable.

63 Similarly, the impact of the Debtors' secured obligations is not a basis for finding exceptional circumstances. These obligations were known long ago when the Plan was formulated. Although 1005559 is not a part of the group which sought *CCAA* protection, it is a related entity and its performance influences that of the Debtors. Alone or in combination with the Debtors' secured obligations, the obligations of 1005559 do not constitute an extraordinary circumstance.

64 The public's confidence in the *CCAA* process is necessarily grounded in fairness and stability for all of the stakeholders. Allowing the Debtors an opportunity for what, essentially, would be a second kick at the *CCAA* can after defaulting on their obligations would not, in all of the circumstances, further this objective.

E. Would Granting the Relief Serve the Ends of Justice?

65 Assessing whether the relief sought would serve the ends of justice entails many of the same considerations as determining whether it would advance the policy objectives underlying the *CCAA*. In addition, factors such as whether a unilateral mistake has been made may be taken into account, as in *Northland Properties Ltd., Re*

66 In the present case, directing a further meeting of the creditors is not necessary to meet the ends of justice.

F. What is the Level of Creditor Support?

67 The Opposing Creditors oppose granting of the application. There is no evidence of the level of creditor support to the proposed amendment. However, I understand that the creditors were canvassed informally, an approach which presumably failed.

68 After weighing the various factors, I find that the Debtors have failed to meet the high threshold required of them on this application.

VII. Conclusion

69 The Debtors are in default of their obligations under the Plan. Claiming that a downturn in the economy, the weight of secured debt and the obligations of a related party preclude them from living up to their obligations, they want another chance to escape bankruptcy by presenting their creditors with a proposed amendment to the Plan. The proposed amendment is to reduce the Debtors' obligation under the Plan by eighty percent. In essence, it is a new deal.

70 A purposive and contextual interpretation of s. 11 of the *CCAA* vests the court with discretion to grant the relief sought. However, the threshold for summoning a further meeting of creditors after court sanction is high and to succeed the debtor must establish truly extraordinary circumstances.

71 In making its determination, the court should consider whether the debtor's application is made in good faith and whether granting the relief would advance the policy objectives of the *CCAA*, serve and enhance the public's confidence

in the process or otherwise serve the ends of justice. The court should also consider the degree of creditor support for the application.

72 The Debtors in the present case have not met the high threshold required for the court to exercise its discretion to order a further meeting of the creditors to be called at this late juncture. Accordingly, the application is dismissed and the creditors are at liberty to apply to lift the stay and pursue their remedies. The parties may speak to me within 30 days if they are unable to agree on costs.

Application dismissed.

End of Document

Tab 6

2006 CarswellOnt 406
Ontario Superior Court of Justice [Commercial List]

Stelco Inc., Re

2006 CarswellOnt 406, [2006] O.J. No. 276, 14 B.L.R. (4th) 260, 17 C.B.R. (5th) 78

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 STELCO INC. AND THE OTHER APPLICANTS LISTED IN SCHEDULE "A"

APPLICATION UNDER THE COMPANIES' CREDITORS ARRANGEMENT ACT, R.S.C. 1985, c. C-36, AS AMENDED

Farley J.

Heard: January 17, 18, 20, 2006
Judgment: January 20, 2006
Docket: 04-CL-5306

Counsel: Michael Barrack, James D. Gage, Geoff R. Hall for Applicants
Robert Thornton, Kyla Mahar for Monitor
Peter Jervis, George Glezos, Karen Kiang for Equity Holders
John Varley for Salaried Employees
David Jacobs for USW Locals 8782, 5328
Aubrey Kauffman for Tricap Management Ltd.
Kevin Zych, Rick Orzy for 8% and 10.4% Stelco Bondholders
Lawrence Thacker for Directors of Stelco
Sharon White for USW Local 1005
Ken Rosenberg for USW International
Kevin McElcheran for GE
Gale Rubenstein, Fred Myers for Superintendent of Financial Services
Derrick Tay for Mittal
David R. Byers, Sean Dunphy for CIT Business Credit as DIP and ABL Lender
V. Gauthier for BABC Global Finance
L. Edwards for EDS Canada Inc.
Peter Jacobsen for Globe & Mail
Paul Macdonald, Andy Kent for Sunrise, Appalloosa
Murray Gold, Andrew Hatnay for Salaried Retirees
Flaviano Stanc for himself

Subject: Corporate and Commercial; Insolvency; Civil Practice and Procedure

CROSS-MOTION by shareholder group for adjournment of arrangement implementation for 60 days.

***Farley J.*:**

1 The Applicants (collectively "Stelco") moved for:

(a) a declaration that Stelco has complied with the provisions of the *Companies' Creditors Arrangement Act* ("CCAA") and the orders of this court made in this CCAA proceeding;

(b) a declaration that the Stelco plan of arrangement pursuant to the CCAA and the reorganization of Stelco Inc. ("S") under the *Canada Business Corporations Act* ("CBCA") (collectively the "Plan") as voted on by the affected creditors of Stelco is fair and reasonable;

(c) an order sanctioning and approving the Plan; and

(d) an order extending the Stay Period and Stay Date in the Initial Order until March 31, 2006.

2 This relief was unopposed by any of the stakeholders except for various existing shareholders of S (who may also be employees or retirees of Stelco). In particular there was organized objection to the Plan, especially as in essence the Plan would eliminate the existing shareholders, by a group of shareholders (AGF Management Ltd., Stephen Stow, Pollitt & Co., Levi Giesbrecht, Joe Falco and Phil Dawson) who have styled themselves as "The Equity Holders" ("EH"). On December 23, 2005 the EH brought in essence a cross motion seeking the following relief:

(a) An order extending the powers of the Monitor, Ernst & Young, in order to conduct a sale of the entire Stelco enterprise as a going concern through a sale of the common shares or assets of Stelco on such terms and conditions as are considered fair;

(b) An order authorizing and directing the Monitor to implement and to take all steps necessary to complete and fulfill all requirements, terms, conditions and steps of such a sale;

(c) An order authorizing and directing the Monitor to conduct the sale process in accordance with a plan for the sale process approved by the court;

(d) An order directing the Monitor to retain such fully independent financial advisors and other advisors as necessary to conduct this sale process;

(e) An order confirming that the powers granted herein to the Monitor supersede any provision of any prior Order of this Court made in the within proceedings to the extent that such provision of any prior order is inconsistent with or contradictory to this order, or would otherwise limit or hinder the power and authority granted to the Monitor;

(f) An order directing Stelco and its directors, officers, counsel, agents, professional advisors and employees, and its Chief Restructuring Officer, to cooperate fully with the Monitor with regard to this sale process, and to provide the Monitor with such assistance as may be requested by the Monitor or its independent advisors;

(g) In the alternative, an order suspending the sanctioning of the Proposed Plan of Arrangement, approved by the creditors on December 9, 2005, for a period of two months from the date of such order, so that the Monitor may conduct the independent sale process that may result in a more profitable outcome for all stakeholders, including the Equity Holders;

(h) In the further alternative, an order lifting the *Companies' Creditors Arrangement Act* stay of proceedings in respect of Stelco without approving the Plan of Arrangement, as approved by the creditors on December 9, 2005, pursuant to such terms as are just and are directed by court; and

(i) Such further and other relief as counsel may advise and this Honourable Court may permit.

3 In its factum, the EH requested that the court adjourn approval of the Plan for 60 days and direct the Monitor to conduct an independent sale process for the shares of S. In the attendances on January 17 and 18, 2006, the EH then

asked that approval of the Plan be adjourned for 30 days in order to see if there were expressions of interest for the shares of S forthcoming in the interim.

4 I indicated that I would defer my consideration of the adjournment request until after I had had submissions on the motions before me as set out above. I also indicated that while there did not appear to be any concern by anyone including the EH as to the first two elements concerning CCAA plan sanctioning as discussed in *Algoma Steel Inc., Re* (2001), 30 C.B.R. (4th) 1 (Ont. S.C.J. [Commercial List]) at p. 3:

> In a sanction hearing under the *Companies' Creditors Arrangement Act* ("CCAA") the general principles to be applied in the exercise of the court's discretion are:
>
> (a) There must be strict compliance with all statutory requirements and adherence to the previous orders of the court;
>
> (b) All materials filed and procedures carried out must be examined to determine if anything has been done or purported to be done which is not authorized by the CCAA; and
>
> (c) The Plan must be fair and reasonable.
>
> See *Northland Properties Ltd., Re* (1988), 73 C.B.R. (N.S.) 175 (B.C. S.C.), affirmed *Northland Properties Ltd. v. Excelsior Life Insurance Co. of Canada* (1989), 73 C.B.R. (N.S.) 195 (B.C. C.A.) at p. 201; *Campeau Corp., Re* (1992), 10 C.B.R. (3d) 104 (Ont. Gen. Div.) at p. 109; *Olympia & York Developments Ltd. v. Royal Trust Co.* (1993), 12 O.R. (3d) 500 (Ont. Gen. Div.) at p. 506; *Sammi Atlas Inc., Re* (1998), 3 C.B.R. (4th) 171 (Ont. Gen. Div. [Commercial List]), at pp. 172-3; *Canadian Airlines Corp., Re*, [2000] 10 W.W.R. 269 (Alta. Q.B.), leave to appeal dismissed, [2000] 10 W.W.R. 314 (Alta. C.A. [In Chambers]).

it would not be sufficient to only deal in this hearing with the third test of whether the Plan was fair and reasonable (including the aspect of "fair, reasonable and equitable" as discussed in *Sammi Atlas Inc., Re* [1998 CarswellOnt 1145 (Ont. Gen. Div. [Commercial List])]). Rather the court also had to be concerned as to whether the Plan was implementable. In other words, it would be futile and useless for the court to approve a plan which stood no reasonable prospect of being implemented. That concern of the court had been raised by my having been alerted by the Monitor in its 46th Report at paragraphs 8-9:

> 8. The Monitor has had discussions with the proposed ABL lenders, Tricap, the Province and Stelco regarding the status of the ABL Loan and the Bridge Loan. The Monitor has been advised that the parties are continuing to work at resolving issues that are outstanding as at the date of this Forty-Sixth Report. However, all of the parties remain optimistic that acceptable solutions to the outstanding issues will be found and implemented.
>
> 9. In the Monitor's view, the principal issues to be resolved include:
>
> (a) the corporate structure of Stelco, which could involve the transfer of assets of some of the operations or divisions of the Applicants to new affiliates; and
>
> (b) satisfying the ABL lenders and Tricap as to the priority of the new financing.
>
> These issues need to be resolved primarily among the proposed ABL lenders, Tricap and Stelco and will also involve the Province insofar as they affect pension and related liabilities.

5 I was particularly disquieted by the lack of progress in dealing with these outstanding matters despite the passage of 39 days since the Plan was positively voted on December 9, 2005. I do appreciate that Christmas, Hanukkah and New Year's were celebrated in this interval and that there had been a certain "negotiation fatigue" leading up to the December 9th revisions to the Plan and that I have advocated that counsel, other professionals and litigation participants balance

their lives and pay particular attention to family and health. However I find it unfortunate that there would appear to have been such a lengthy hiatus, especially when the workers at Stelco continued (as they have for the past two years while Stelco has been under CCAA protection) to produce steel in record amounts. I therefore demanded that evidence be produced forthwith to demonstrate to my satisfaction that progress was real and substantial so that I could be satisfied about implementability. As a side note I would observe that in the "normal" case, sanction orders are typically sought within two or three days of a positive creditor vote so that it is not unusual for documentation to be sorted out for a month before a plan is implemented with a closing.

6 The EH filed material to support its submission that the Plan is not fair, reasonable and equitable because it is alleged that there is currently sufficient value in Stelco to fully satisfy the claims of affected and unaffected creditors and to provide at least some value to current shareholders. The EH prefers to have a search for some entity to take out the current shareholders for "value". Fabrice Taylor, a chartered financial analyst with Pollit & Co. swore an affidavit on the eve of this hearing which was sent electronically to the service list on January 16, 2006 at approximately 7:30 p.m. In that affidavit, he states:

> 2. The Dofasco bidding war has highlighted a crucial fact about steel asset valuations, notably that strategic buyers place a much higher value on them than public market investors. Attached as Exhibit "1" is an article entitled "Restructuring of steel industry revives investors' interest", published in the Financial Times on December 14, 2005.
>
> 3. I, along with Murray Pollitt and a number of Stelco shareholders, have spent the past three months attempting to attract strategic buyers and/or equity investors in Stelco. These strategic buyers and equity investors are mostly international. Some had already considered buying Stelco or had made bids for the company but had stopped following the story some months ago. Others were not very familiar with Stelco.
>
> 4. Three factors hindered our efforts. First, Stelco is under CCAA protection, a complicated situation involving multiple players and interests (unions, politics, pensions) that is difficult to understand, particularly for foreigners. Second, there has not been enough time for these strategic buyers or equity investors to deepen their understanding or to perform due diligence. Finally, the Dofasco bid process, while providing emphatic evidence that steel assets are increasingly valuable, hinders certain strategic buyers and financial institutions interested in participating in Stelco because they are distracted and/or conflicted by the Dofasco sale. I have been advised by some of the participants in the Dofasco negotiations that they would be willing to carefully consider a Stelco transaction once the Dofasco sale has been resolved.
>
> 5. The Forty Fifth Report of the Monitor confirmed that Stelco had not received any offers in the last several months. The report does not answer the question of whether the company or its financial advisors have in fact attempted to attract any offers. I believe that Stelco would have received expressions of interest had the company made efforts to attract offers, or had the Dofasco sale been resolved earlier. I believe that the Monitor should be authorized, for a period of at least 60 days, to canvas interest in a sale of Stelco before the approval of the proposed plan of restructuring.

7 No satisfactory explanation was forthcoming as to why this affidavit, if it needed to be filed at all, was not served and filed by December 23, 2005, in accordance with the timetable which the EH and the other stakeholders agreed to. Certainly there is nothing in the affidavit which is such late breaking news that this deadline could not have been met, let alone that it was served mere hours before the hearing commenced on January 17, 2006. Aside from the fact that the financing arrangements forming the basis of the Plan contained "no shop" covenants which would make it inappropriate and a breach to try to attract other offers, the foregoing excerpts from the Taylor affidavit clearly illustrate that despite apparently diligent efforts by the EH, no one has shown any real or realistic interest in Stelco. Reading between the lines and without undue speculation, it would appear that the efforts of the EH were merely politely rebuffed.

8 Certainly Stelco is not Dofasco, nor is it truly a comparable (as opposed to a contrastor). Stelco has been a wobbly company for a long time. Further as I indicated in my October 3, 2005 endorsement, in the preceding 20 months under

the CCAA protection, Stelco has become "shopped worn". The unusual elevation of steel prices in the past two years has helped Stelco avoid the looming liquidity crisis which it anticipated in its CCAA filing on January 29, 2004. However even this financial transfusion has not allowed it to become a healthy company or truly given it a burgeoning war chest to weather bad times the way that other steel companies (including some in Canada) have so benefited. The redness of the visage of Stelco is not a true indication of health and well being; rather it seems that it is rouge to mask a deep pallor.

9 I am satisfied on the evidence of Hap Stephen, the Chief Restructuring Officer of Stelco and of the Monitor that there has been compliance with all statutory requirements and adherence to previous orders of the court and further that nothing has been done or purported to be done that is not authorized by the CCAA.

10 The next question to be dealt with is whether the Plan is fair, reasonable and equitable. I was advised that creditors of the affected creditor classes representing approximately 90% in value of each class voted on the Plan. The Monitor reported at para. 19 of its 44th Report as to the results of the vote held December 9th as follows:

Class of Affected Creditors	Percentage in favour by Number	Percentage in favour by Dollar Value
Stelco	78.4%	87.7%
Stelwire	89.01%	83.47%
Stelpipe	94.38%	86.71%
CHT Steel	100%	100%
Welland Pipe	100%	100%

11 This favourable vote by the affected creditors is substantially in excess of the statutory two-thirds requirement. By itself that type of vote, particularly with such a large quorum present, would ordinarily be very convincing for a court not interfering with the informed decisions of business people. With that guideline, plus the aspect that a plan need not be perfect, together with the lack of any affected creditor opposition to the Plan being sanctioned and the fact that the Plan including its ingredients and nature and amount of compromise compensation to be given to affected creditors having been exhaustively negotiated in hard bargaining by the larger creditor groups who are recognized as generally being sophisticated and experienced in this area, and the consideration of the elements in the next paragraph, it would seem to me that the Plan is fair, reasonable and equitable vis-à-vis the affected creditors and I so find. See *Sammi Atlas Inc., Re*, at p. 173; *T. Eaton Co., Re* (1999), 15 C.B.R. (4th) 311 (Ont. S.C.J. [Commercial List]) at p. 313; *Olympia & York Developments Ltd. v. Royal Trust Co.* (1993), 12 O.R. (3d) 500 (Ont. Gen. Div.) at p. 510.

12 I also think it helpful to examine the situation pursuant to the analysis which Paperny J. did in *Canadian Airlines Corp., Re* (2000), 20 C.B.R. (4th) 1 (Alta. Q.B.), leave to appeal refused (2000), 20 C.B.R. (4th) 46 (Alta. C.A. [In Chambers]). That proceeding also involved an application pursuant to the corporate legislation, the *Business Corporations Act (Alberta)*, concerning the shares and shareholders of Canadian Airlines. In that case, Paperny J. found the following factors to be relevant:

> (a) the composition of the vote: claims must have been properly classified, with no secret arrangements to give an advantage to a creditor or creditors; approval of the plan by the requisite majority of creditors is most important (in the case before me of Stelco: the challenge to classification was dismissed; there was no suggestion of secret arrangements; and, as discussed above, the quorum and size of the positive vote were very high);
>
> (b) anticipated receipts in liquidation or bankruptcy: it is helpful if the Monitor or other disinterested person has prepared a liquidation analysis (in Stelco, the Monitor determined that on liquidation, affected creditor recovery would likely range from 13 to 28 cents on the dollar; it should also be observed that Stelco has engaged in extensive testing of the market as to possible capital raising or sale with the aid of established firms and professionals of great experience and had come up dry.);
>
> (c) alternatives to the proposed plan: it is significant if other options have been explored and rejected as unworkable (in Stelco; see comment in (b));

(d) oppression of the rights of certain creditors (in Stelco, this was not a live issue as nothing of this sort was alleged);

(e) unfairness to shareholders (in Stelco, this will be dealt with later in my reasons; however allow me to observe that the interests of shareholders becomes engaged if they are not so far underwater that there is a reasonable prospect in the foreseeable future that the fortunes of a company would otherwise likely be turned around so that they would not continue to be submerged); and

(f) the public interest: the retention of jobs for employees and the support of the plan by the company's unions is important (in Stelco, the Plan does not call for reductions in employment; there is provision for continuation of the capital expenditure program and its funding; an important enterprise for the municipal and provincial levels of government would be preserved with continuing benefits for those communities; an important customer and supplier would continue in the industry and maintain competition; the USW International Union and its locals (except for local 1005) supported the Plan and indeed were instrumental in bringing Tricap Management Limited to the table (local 1005's position was that it did not wish to engage in the CCAA process in any meaningful way as it was content to rely upon its existing collective agreement which now still has several months to go before expiring).

However that is not the end of that issue: what of the shareholders?

13 Is the Plan fair, reasonable and equitable for the existing shareholders of S? They will be wiped out under the Plan and their shares eliminated. New equity will be created in which the existing shareholders will not participate. They have not been allowed to vote on the Plan.

14 It is well established that a reorganization pursuant to s. 191 of the CBCA may be made in conjunction with a sanction order under the CCAA and that such a reorganization may result in the cancellation of existing shares of the reorganized corporation based on those shares/equity having no present value (in the sense of both value "now" and the likelihood of same having value in the reasonably foreseeable future, absent the reorganization including new debt and equity injections and permitted indulgences or other considerations and adjustments). See *Beatrice Foods Inc., Re* (1996), 43 C.B.R. (4th) 10 (Ont. Gen. Div. [Commercial List]) at para. 10-15; *Laidlaw, Re* (2003), 39 C.B.R. (4th) 239 (Ont. S.C.J.); *Algoma Steel Inc., Re* at para. 7; *Cable Satisfaction International Inc. v. Richter & Associés inc.* (2004), 48 C.B.R. (4th) 205 (C.S. Que.) at p. 217. The Dickenson Report, which articulated the basis for the reform of corporate law that resulted in the enactment of the CBCA, described the object of s. 191 as being:

> to enable the court to effect any necessary amendment to the articles of the corporation in order to achieve the objective of the reorganization without having to comply with all the formalities of the Draft Act, particularly shareholder approval of the proposed amendment (emphasis added): R.W.V. Dickenson, J.L. Howard, L. Getz, *Proposals for a New Business Corporations Law for Canada*, vol. 1 (Ottawa: Information Canada. 1971) at p. 124.

15 The fairness, reasonableness and equitable aspects of a plan must be assessed in the context of the hierarchy of interests recognized by insolvency legislation and jurisprudence. See *Canadian Airlines Corp., Re* at pp. 36-7 where Paperny J. stated:

> Where a company is insolvent, only the creditors maintain a meaningful stake in its assets. Through the mechanism of liquidation or insolvency legislation, the interests of shareholders are pushed to the bottom rung of the priority ladder. The expectations of creditors and shareholders must be viewed and measured against an altered financial and legal landscape. Shareholders cannot reasonably expect to maintain a financial interest in an insolvent company where creditors' claims are not being paid in full. It is through the lens of insolvency that the court must consider whether the acts of the company are in fact oppressive, unfairly prejudicial or unfairly disregarded. CCAA proceedings have recognized that shareholders may not have "a true interest to be protected" because there is no reasonable prospect of economic value to be realized by the shareholders given the existing financial misfortunes of

> the company: *Royal Oak Mines Ltd.*, *supra*, para. 4., *Re Cadillac Fairview Inc.* (March 7, 1995), Doc. B28/95 (Ont. Gen. Div. [Commercial List]), and *T. Eaton Company*, *supra*.
>
> To avail itself of the protection of the CCAA, a company must be insolvent. The CCAA considers the hierarchy of interests and assesses fairness and reasonableness in that context. The court's mandate not to sanction a plan in the absence of fairness necessitates the determination as to whether the complaints of dissenting creditors and shareholders are legitimate, bearing in mind the company's financial state. The articulated purpose of the Act and the jurisprudence interpreting it, "widens the lens" to balance a broader range of interests that includes creditors and shareholders and beyond to the company, the employees and the public, and tests the fairness of the plan with reference to its impact on all of the constituents.
>
> It is through the lens of insolvency legislation that the rights and interests of both shareholders and creditors must be considered. The reduction or elimination of rights of both groups is a function of the insolvency and not of oppressive conduct in the operation of the CCAA. The antithesis of oppression is fairness, the guiding test for judicial sanction. If a plan unfairly disregards or is unfairly prejudicial it will not be approved. However, the court retains the power to compromise or prejudice rights to effect a broader purpose, the restructuring of an insolvent company, provided that the plan does so in a fair manner.

16 The question then is does the equity presently existing in S have true value at the present time independent of the Plan and what the Plan brings to the table? If it does then the interests of the EH and the other existing shareholders must be considered appropriately in the Plan. This is fairly put in K.P. McElcheran, *Commercial Insolvency in Canada* (Toronto, Lexis Nexis Canada Inc.: 2005) at p. 290 as:

> If, at the time of the sanction hearing, the business and assets of the debtor have a value greater than the claims of the creditors, a plan of arrangement would not be fair and reasonable if it did not offer fair consideration to the shareholders.

17 However if the shareholders truly have no economic interest to protect (keeping in mind that insolvency and the depth of that insolvency may vary according to which particular test of insolvency is applied in respect of a CCAA proceeding: as to which, see *Stelco Inc., Re*, [2004] O.J. No. 1257 (Ont. S.C.J. [Commercial List]), leave to appeal dismissed [2004] O.J. No. 1903 (Ont. C.A.), leave to appeal dismissed [2004 CarswellOnt 5200 (S.C.C.)] No. 30447). In *Cable Satisfaction*, Chaput J. at p. 218 observed that when shareholders have no economic interest to protect, then they have no claim to a right under the proposed arrangement and the "[m]ore so when, as in the present case, the shareholders are not contributing to any of the funding required by the Plan." I do note in the case of the Stelco Plan and the events leading up to it, including the capital raising and sale processes, that despite talk of an equity financing by certain shareholders, including the EH, no concrete offer ever surfaced.

18 If the existing equity has no true value at present, then what is to be gained by putting off to tomorrow (the ever present and continuous problem in these proceedings of manãna — which never comes) what should be done today. The EH speculate, with no concrete basis for foundation as demonstrably illustrated by the eve of hearing Taylor affidavit discussed above, that something good may happen. I am of the view that that approach was accurately described in court by one counsel as a desperation Hail Mary pass and the willingness of someone, without any of his own chips, in the poker game willing to bet the farm of someone else who does have an economic interest in Stelco.

19 I also think it fair to observe that in the determination of whether someone has an economic value, that analysis should be conducted on a reasonable and probable basis. In a somewhat different but applicable context, I observed in *New Quebec Raglan Mines Ltd. v. Blok-Andersen*, [1993] O.J. No. 727 (Ont. Gen. Div. [Commercial List]) at p. 3:

> The "highest price" is not the price which could be derived on the basis of the most optimistic and risky assumptions without any regard as to their likelihood of being realized. It also seems to me that prudence would involve a consideration that there be certain fall back positions. Even in betting on horses, the most savvy and luckiest punter

> will not continue to stake all his winnings of the previous race on the next (and so on). If he does, he will go home wearing the barrel before the last race is run.

Alternatively there is a saying: "If wishes were horses, then beggars would ride."

20 Unless I were to now dismiss the motion for sanctioning and approving the Plan because I found that it was not implementable and/or that it was not fair, reasonable and equitable to the existing shareholders (based upon the proviso that I did determine that the existing shareholders did have a valid present material equity of value), then I see no reason not to dismiss the motion of the EH concerning its request for an adjournment and its request for a further sale (or other related disposition) process. Allow me to observe that no matter how well intentioned the motion of the EH in that regard, I find that that request to be lacking in any valid substance. Rather, the evidence presented was in essence a chimera. I think it fair to observe that, with all the capital raising and sales processes to date which Stelco has undertaken in conjunction with its experienced and well placed professional advisers together with its Chief Restructuring Officer and the Monitor, the bushes have been exhaustively and well beaten as to any real possible interest. Despite three months of what one must presume to be diligent efforts, the EH have come up with nothing concrete. I do not find that the three factors mentioned by Taylor in his late-blooming affidavit of January 16th to be remotely close to convincing. The first two, if taken at face value, would lead one to the conclusion that no one has the time, interest or ability to take an interest in Stelco in any meaningful timeframe. The third presumes that the losing bidder for Dofasco, be it Arcelor or ThyssenKrupp, will almost automatically want Stelco — and at a price and upon terms which would result in present equity being attributed value. I must say in fairness that this is wishful thinking as neither of these warring bidders pursued any interest in Stelco during the previous processes. It is neither clear nor obvious why mere municipal proximity of Dofasco to Stelco's Hilton Works in Hamilton would now ignite any interest in Stelco.

21 I also think it fair to observe that not proceeding with the sanction hearing now and indeed starting a brand new search for someone who will think Stelco so worthwhile that it will offer such a large amount (with or without onerous conditions) is akin to someone coming into court when a receiver is seeking court approval on a sale — and that someone being allowed to know the price and conditions — and then being able to make an offer for a price somewhat higher. (I reiterate that here we do not even have an offer or a price.) I do not see that such a procedure would be consistent with the principles laid out in *Royal Bank v. Soundair Corp.* (1991), 7 C.B.R. (3d) 1 (Ont. C.A.). Given that the affected creditors have rather resoundingly voted in favour of the Plan, all in accordance with the provisions of the CCAA and the Court orders affecting the sanction, I would be of the view that if the existing equity has no value, then the EH's request in this respect would, if granted, be of significant detriment to the integrity of the insolvency system and regime. I would find that inappropriate to attempt to justify proceeding along that line.

22 Allow me to return to the pivotal point concerning the question of whether the Plan is fair, reasonable and equitable, vis-à-vis the existing equity. The EH retained Navigant Consulting which relied upon the views of Metal Bulletin Research ("MBR") which, *inter alia*, predicted a selling spot price of hot roll steel at $525 U.S. per ton. Navigant's conclusion in its December 8, 2005 report was that the value of residual shareholder equity was between $1.1 to $1.3 billion or a per share value of between $10.76 and $12.71. However, when Stelco pointed out certain deficiencies in this analysis, Navigant took some of these into account and reduced its assessment of value to between $745 million to $945 million for residual shareholder value on per share value of $7.29 to $9.24, using a discounted cash flow ("DCF") approach. Navigant tested the DCF approach against the EBITDA approach. It is interesting to note that on the EBITDA analysis approach Navigant only comes up to a conclusion that the equity is valued at $8 million to $83 million or $0.09 to $0.81 per share. If the Court were to accept that as an accurate valuation, or something at least of positive value even if not in that neighbourhood, then I would have to take into account existing shareholder interests in determining whether the Plan was fair, reasonable and equitable — and not only vis-à-vis the affected creditors but also vis-à-vis the interests of the existing shareholders given that at least some of their equity would be above water. I understand the pain and disappointment of the existing shareholders, particularly those who have worked hard and long with perhaps their life savings tied up in S shares, but regretfully for them I am not able to come to a conclusion that the existing equity has a true positive value.

23 The fight in the Stelco CCAA proceedings has been long and hard. No holds have been barred as major affected creditors have scrapped to maximize their recovery. There were direct protracted negotiations between a number of major affected creditors and the new equity sponsors under the Plan, all of whom had access to the confidential information of Stelco pursuant to Non Disclosure Agreements. These negotiations established a value of $5.50 per share for the *new* common shares of a *restructured* Stelco. That translates into an enterprise value (not an equity value since debt/liabilities must be taken into consideration) of $816.6 million for Stelco, or a recovery of approximately 65% for affected creditors. The parties engaged in these negotiations are sophisticated experienced enterprises. There would be no particular reason to believe that in the competition involved here that realistic values were ignored. Further, the affected creditors generally were rather resoundingly of the view by their vote that an anticipated 65% recovery was as good as they could reasonably expect.

24 The 45th Report of the Monitor had a chart of calculations to determine the level of recovery of affected creditors at various assumed enterprise values up to and including the top end of Navigant's range of enterprise value (as contrasted with residual equity value). At the high end of Navigant's range of revised enterprise value, $1.6 billion, the Monitor calculated that affected creditors would still not receive full recovery of their claims.

25 The EH cited the sale of the EDS Canada claim to Tricap as being at a premium as evidence in support of Navigant's conclusion. However, the fact was that this claim was purchased not at a premium, but rather at a discount. That would be confirmation of the opposite of which the EH has been contending.

26 Despite a very comprehensive capital raising and asset sale process, with the market alerted and well canvassed, and with the ability to conduct due diligence, no interested party came forwarded to conclude a deal. Even since the December 9, 2005 vote when the terms of the Plan were available, no interested party has come forward with any expression of interest which would attribute value to the existing shareholders.

27 Stelco's experts, UBS and BMO Nesbit Burns, both have given opinions that there is no value to the existing equity. Their expert opinions were not challenged by cross-examination. Both these advisors are large sophisticated institutions; both have extensive experience in the steel industry.

28 UBS calculated the enterprise value of Stelco as being in the range of $550 million to $750 million; BMO Nesbitt Burns at $650 million to $850 million. On that basis the unsecured creditors would receive less than full recovery of their claims, which would lead to the conclusion that there is no value for the existing shareholders. The Monitor commissioned an independent estimate of the enterprise value from its affiliate, Ernst & Young Orenda Corporate Finance Inc's Valuation Group. That opinion came in at $635 million to $785 million.

29 I would note that Farley Cohen, the principal author of the Navigant report, does not have experience in dealing with integrated steel companies. I find it unusual that he would have customized his approach in calculating equity value by not deducting the Asset Based Lenders loan. Brad Fraser of BMO Nesbitt Burns stated that such customization was contrary to the practice at his firms both present and past and that the Navigant's approach was internally inconsistent with respect thereto as to 2005 to 2009 cash flows as contrasted with terminal value. The Navigant report appears to have forecasted a high selling price for steel combined with low costs for imports such as coal and scrap, which would be contrary to historical complementary movements between steel prices and these inputs.

30 Navigant relies on an average price of $525 US per ton as provided by MBR. This is a single source as to this forecast. While a single analyst may come up with a forecast which is shown by the passage of time to be dead on accurate, it would seem to me to be more realistic and prudent to rely on the consensus approach of considering the views of a greater number of "representative" analysts, especially when prices appear volatile for the foreseeable future. That consensus approach allows for consideration of the way that each analyst looks at the market and the factors and weights to be given. The UBS opinion reviewed the pricing forecast of eight analysts and BMO Nesbitt Burns' ten analysts. Interestingly, MBR's choice of a price at the top of the band would seem at odds as the statements on the MBR website

foreseeing downward pressure on steel prices in 2006 because of falling prices in China; although this inconsistency was pointed out, there was no response forthcoming.

31 Navigant estimated Stelco's financial performance for the last quarter of 2005 and made a significant upward adjustment. However, the actual experience would appear to indicate that such an adjustment would overstate Stelco's results by $124 million.

32 Navigant's DCF approach involved a calculation of Stelco's enterprise value by adding the present value of a stream of cash flow from the present to 2009 and the present value of the terminal value determined as at 2009 so that the terminal value represents the majority (60% approximately) of enterprise value as calculated by Navigant. MBR chose a 53-year average steel price despite significant changes over that time in the industry. However, coal and scrap costs were determined as at 2009. This produced the anomalous result that steel prices are rising while costs are falling. This would imply great structural difficulties (economically and functionally) in the steel industry generally and a lack of competition. A terminal value EBITDA margin for Stelco would then be implied at approximately 26% or some 11% higher than the EBITDA margin actually achieved by Stelco in the first quarter of 2005, the most profitable quarter in the history of Stelco.

33 Interestingly, since Navigant's approach in fact would decrease calculated value, UBS and BMO Nesbitt Burns used a weighted average cost of capital ("WACC") for Stelco in the range of 10% to 14%; Navigant used 24%. A higher WACC will result, all other things being equal, in a lower enterprise value. Navigant considered that there should be a 10% to 15% company-specific premium because of the risks associated with Stelco vis-à-vis the higher steel prices forecast by MBR. This would appear to imply that there was recognition that either MBR was aggressive in its forecasting or that price volatility would caution one to use consensus forecasting. Colin Osborne, a senior executive of Stelco, with considerable experience in the steel industry provided direct evidence on the substantial differences between each of Stelco, AK Steel, U.S. Steel and Algoma. Mr. Cohen acknowledged in cross-examination that these differences made Dofasco a more valuable company than Stelco. As set out at para. 74 of the Stelco Factum:

> 74. The specific difference identified by Mr. Osborne which made Dofasco unique include but are not limited to:
>
> (a) non-union, flexible work environment (vs. Stelco, Algoma, AK Steel and U.S. Steel);
>
> (b) legacy costs which are very low due to non-conventional profit sharing, which limits liability (vs. Stelco, AK Steel, Algoma and U.S. Steel);
>
> (c) high historical cap-ex spend per ton (vs. Stelco, Algoma and U.S. Steel);
>
> (d) a flexible steelmaking stream in terms of a hybrid EAF and blast furnace BOF stream in Hamilton and a mini-mill operation in the U.S. (vs. Stelco, Algoma, U.S. Steel and AK Steel which are all blast furnace based steel makers);
>
> (e) a value added product mix focused on coated products and tubing (vs. Stelco and Algoma which focus on hot roll); and
>
> (f) a strong raw material position with excess iron ore and self-sufficiency in coke (Algoma, Stelco and AK Steel all have dependence to various degrees on either iron ore or coke or both).

Dofasco and Stelco are not in my view fungible. There are incredible differences between these two enterprises, to the disadvantage of Stelco.

34 The reply affidavit of Mr. Fraser of BMO Nesbitt Burns calculated the effect of all of the acknowledged corrections to the initial Navigant report and other adjustments. The result of this exercise was a conclusion by him that there was no value available for existing shareholders. This, along with all the other affidavits provided on the Stelco side, was not cross-examined on.

35 While not referred to in the Factum of EH, there were a number of quite serious allegations raised in material filed by the EH against management of Stelco concerning bias and manipulation. Mr. Osborne responded to each of these allegations; he was not cross-examined. I find it unfortunate that such allegations appear to have been made on an unsubstantiated shotgun approach.

36 The position of the EH is that certain of the features of the Plan should be assumed as transportable directly and without change into a scenario where some insolvency rescuer emerges on the scene as the equivalent of a White Knight, one it would seem which has been awakened from slumber. I am of the view that presumes too much. For example, I take it that the Province would not automatically accept this potential newcomer without question; nor would it likely relish the resumption of weeks of hard bargaining. I would think it unwise, impudent and high stakes poker (with other peoples' money) to speculate as did Taylor in para. 41 of his December 23, 2005 affidavit:

> 41. Were Stelco to emerge from CCAA protection and were the province to carry out its threat to revoke Stelco's entitlement to the benefit of section 5.1 the end result would likely be a liquidation of the company. The Province would be responsible for a substantial portion of Stelco's pension promise. It would clearly not be in the Province's self-interest to force Stelco into liquidation. It was, in other words, an obvious bluff. Yet the notion of calling this bluff does not appear to have crossed management's mind.

This should be contrasted with the views of the Monitor in its 44th Report at para. 61:

> 61. It should also be noted that the Pension Plan Funding Arrangements and the $150 million New Province Note embodied in the Approved Plan were agreed to by the Province only in the context of the terms of the Approved Plan and, in particular, the capital structure, liquidity and other elements contemplated therein. The Province has advised that its proposed financing and the Pension Plan Funding Arrangements should not be assumed to be available if any of the elements of the Approved Plan are changed.

37 The end result is that given the above analysis, I have no hesitation in concluding that it would be preferable to rely upon the analysis of UBS, BMO Nesbitt Burns and Ernst & Young Orenda, both as to their direct views as to the enterprise value of existing Stelco and as to their criticism of the Navigant and MBR reports concerning Stelco. Therefore, I conclude that the existing shareholders cannot lay claim to there being any existing equity value. Given that conclusion, it would be inappropriate to justify cutting in these existing shareholders for any piece of the emergent restructured Stelco. If that were to happen, especially given the relative values and the depth of submersion of existing equity, then it would be unfair, unreasonable and inequitable for the affected creditors.

38 That then leaves the remaining question: Does it appear likely that the Plan will be implementable? I have been advised on Wednesday, January 18th that I would receive executed term sheets (which would address the issues raised by the Monitor discussed above) by 5 p.m., Friday, January 20th.

39 The motion and adjournment request of the EH is dismissed.

40 There was a request to extend the stay to March 31, 2006. I am of the view that it would be sufficient and desirable to extend the stay (subject, of course, to further extension) to March 3, 2006.

41 I have received the term sheets together with the Monitor's 48th Report by the 5 p.m. January 20th deadline and find them satisfactory as demonstrating to my analysis and satisfaction that the Plan is implementable as discussed above, subject to a comeback provision if anyone wishes to dispute the implementability issue (the onus remaining on Stelco). My decision today re: implementability should in no way be taken as deciding any corporate reorganization issue or anything of that or related nature. I therefore sanction and approve the Plan.

Motion dismissed.

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Tab 7

2016 ONCA 662
Ontario Court of Appeal

U.S. Steel Canada Inc., Re

2016 CarswellOnt 14104, 2016 ONCA 662

In the Matter of the Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36, As Amended

In the Matter of a Proposed Plan of Compromise or Arrangement with Respect to U.S. Steel Canada Inc.

George R. Strathy C.J.O., P. Lauwers J.A., M.L. Benotto J.A.

Heard: March 17, 2016
Judgment: September 9, 2016
Docket: CA C61331

Counsel: Gordon Capern, Kristian Borg-Olivier, Denise Cooney, for Appellant, United Steel, Paper and Forestry, Rubber, Manufacturing, Energy, Allied Industrial and Service Workers International Union
Andrew Hatnay, Barbara Walancik, for Non-union retirees and active employees of U.S. Steel Canada Inc.
Tamryn Jacobson, for Her Majesty the Queen in Right of Ontario and Superintendent of Financial Services (Ontario)
Michael E. Barrack, Jeff Galway, John Mather, for Respondent, United States Steel Corporation
Sharon Kour, for U.S. Steel Canada Inc.

Subject: Civil Practice and Procedure; Insolvency

APPEAL by union of judgment finding that court had no jurisdiction to apply American doctrine of equitable subordination.

George R. Strathy C.J.O.:

1 U.S. Steel Canada Inc. ("USSC") is in *CCAA* [1] protection. Its former employees claim that its American parent, United States Steel Corporation ("USS"), ran the company into insolvency to further its own interests. An issue arose in the court below as to whether the *CCAA* judge could apply an American legal doctrine called "equitable subordination" to subordinate USS's claims to the appellant's claims.

2 The *CCAA* judge held he had no jurisdiction to do so. For reasons different than the ones he gave, I agree, and would dismiss the appeal.

FACTUAL BACKGROUND

3 USS is one of the largest steel producers in North America. In 2007, it acquired Stelco, which was in *CCAA* protection at the time, and changed its name to USSC.

4 Seven years later, on September 16, 2014, USSC was again granted *CCAA* protection by order of the Superior Court of Justice (Commercial List).

5 The *CCAA* judge made a Claims Process Order on November 13, 2014, establishing a procedure for filing, reviewing and resolving creditors' claims against USSC.

6 The order set out a separate procedure for resolving claims of approximately $2.2 billion by USS against USSC. Most of the claims arose from USS's acquisition and reorganization of Stelco and from advances of working capital. Those claims were to be determined by the court, rather than by the Monitor.

7 USS filed its proofs of claims. The Monitor recommended they be approved and USS moved for court approval of the claims.

8 Notices of Objection were filed by four parties: (a) the Province of Ontario and the Superintendent of Financial Services in his capacity as administrator of the Pension Benefits Guarantee Fund; (b) the United Steelworkers, Locals 8782 and 1005; (c) Representative Counsel to the Non-USW Active Salaried Employees and Non-USW Salaried Retirees; and (d) Robert Milbourne, a former president of Stelco, and his wife, Sharon Milbourne, both of whom are beneficiaries of a pension agreement with USSC.

9 These objections overlapped to some extent. The *CCAA* judge had to develop a procedure to address the objections. He had to decide whether they should be dealt with within the *CCAA* process, outside it, or not at all.

10 The Province made two allegations. The first was that loans by USS to USSC should be characterized as shareholders' equity, because of the circumstances in which they were made. They should therefore be subordinated to all other claims pursuant to s. 6(8) of the *CCAA*[2] (the "Debt/Equity Objection"). Second, the Province argued that the security for the loans should be invalidated pursuant to provincial and federal fraudulent assignment and fraudulent preference legislation (the "Security Objection"). USS disputed both allegations, but was content to have the issues determined under the Claims Process Order.

11 The Union made objections similar to the Province's, but it added a third based on oppression and breach of fiduciary duty arising out of USS's conduct in relation to the Canadian plants, pensioners, pension plan members and beneficiaries (the "Conduct Objections").

12 The *CCAA* judge described the Conduct Objections as allegations that USS caused USSC to underperform, thereby requiring it to incur significant debt and to be unable to meet its pension obligations. The Union sought, among other things, an order subordinating the USS claims in whole or in part to its claims.

13 The Milbournes' objections were based on USS's alleged conduct and relied primarily on the doctrine of equitable subordination. They asked that the USS claims be dismissed entirely or subordinated to the claims of the other unsecured creditors.

14 The *CCAA* judge scheduled a motion to establish a litigation plan for USS's motion for approval of its claims against USSC. The parties agreed that the Security Objection and the Debt/Equity Objection could be determined pursuant to the Claims Process Order and within the *CCAA* proceedings.[3]

15 The primary disagreement concerned the procedure and timing for the determination of the other objections. The Union argued that the Conduct Objections should be resolved as part of the Claims Process Order and that an evidentiary record was required to do so. USS and USSC took the position that the Conduct Objections should be litigated outside the *CCAA* claims process.

16 The *CCAA* judge found that some of the claims of the Union and the Milbournes could be approached as third party claims against USS for oppression for the purpose of s. 241 of the *Canada Business Corporations Act*, R.S.C. 1985, c. C-44, and for breach of fiduciary duty. He found that neither the Claims Process Order nor the *CCAA* contemplated that such claims would be addressed by or would be relevant to a plan of arrangement or compromise under the *CCAA*. The third party claims fell outside the claims process unless specifically incorporated into the restructuring plan as approved by the parties or otherwise ordered.

17 The *CCAA*, he said at para. 65, "is directed towards the creation, approval and implementation of a plan of arrangement or compromise proposed between a debtor company and its secured and unsecured creditors". It did not contemplate incorporation of inter-creditor claims into any plan of arrangement or compromise or into the voting process in respect of any proposed plan.

18 He concluded, at para. 84, that under s. 11 the court had authority to order the remaining claims of the Union and the Milbournes, except the claim for equitable subordination, to be "determined by a process within the *CCAA* proceedings, other than the process contemplated by the Claims Process Order, if the Court is of the opinion that, on balance, such action is likely to further the remedial purpose of the *CCAA*." He held that those claims could be determined within the *CCAA* proceedings, rather than in a separate action in the Superior Court, but not under the Claims Process Order. He noted that the court retained jurisdiction to order that the claims be continued outside the *CCAA* if it was determined that pursuing them within the process would no longer further the remedial process of the *CCAA*.

19 He held, however, that he had no jurisdiction under the *CCAA* to apply the doctrine of equitable subordination. Before turning to his reasons, I will explain the doctrine of equitable subordination.

EQUITABLE SUBORDINATION

20 Equitable subordination was developed as an equitable remedy in American insolvency law to subordinate a creditor's claim based on its inequitable conduct. The principles were articulated in *Mobile Steel Co., Re*, 563 F.2d 692 (U.S. C.A. 5th Cir. 1977), which set out a three-part test:

a. the claimant must have engaged in some type of inequitable conduct;

b. the misconduct must have resulted in injury to creditors of the bankrupt or conferred an unfair advantage on the claimant; and

c. equitable subordination of the claim must not be inconsistent with the provisions of the bankruptcy statute.

21 Paragraph 105(a) of the U.S. *Bankruptcy Code* authorizes bankruptcy courts to use equitable principles to alter the provisions of Title 11 or to prevent an abuse of process. One year after *Mobile Steel*, the *Code* was amended to give legislative effect to equitable subordination: *Bankruptcy Reform Act*, 11 U.S.C. §510(c)(1).

22 The Supreme Court of Canada considered the doctrine on two occasions. In both, the court found it unnecessary to determine whether equitable subordination should be applied, because the underlying facts did not meet the test: *Canada Deposit Insurance Corp. v. Canadian Commercial Bank*, [1992] 3 S.C.R. 558 (S.C.C.), at p. 609; and *Indalex Ltd., Re*, 2013 SCC 6, [2013] 1 S.C.R. 271 (S.C.C.), at para. 77. This court also found it unnecessary to decide the issue in *Olympia & York Developments Ltd. v. Royal Trust Co.* (1993), 14 O.R. (3d) 1 (Ont. C.A.).

23 The availability of the doctrine has been considered in various Canadian superior courts at the trial level, in various contexts and with inconclusive results: see *General Chemical Canada Ltd., Re*, [2006] O.J. No. 3087 (Ont. S.C.J. [Commercial List]), (in the context of the *Bankruptcy and Insolvency Act*, R.S.C., 1985, c. B-3); *Christian Brothers of Ireland in Canada, Re* (2004), 69 O.R. (3d) 507 (Ont. S.C.J. [Commercial List]), (in the context of the *Winding-up and Restructuring Act*, R.S.C. 1985, C. W-11, as amended).

24 In *AEVO Co. v. D & A Macleod Co.* (1991), 4 O.R. (3d) 368 (Ont. Bktcy.), Chadwick J. rejected the application of equitable subordination in Canadian law, observing, at p. 372, that to introduce the doctrine would create chaos and would lead to challenges to security agreements based on the conduct of the secured creditor. In *I. Waxman & Sons Ltd., Re* (2008), 89 O.R. (3d) 427 (Ont. S.C.J. [Commercial List]), Pepall J. queried, at para. 33, whether statutory priorities should be upset by a doctrine "divorced from its legal home". This observation was followed, however, with the comment that "a vibrant legal system must be responsive to new developments in the law and the need for reform. Jurisprudence from other jurisdictions often provides the impetus or basis for much needed legal developments."

25 On the other hand, the Newfoundland and Labrador Supreme Court (Trial Division) applied the doctrine in a bankruptcy case in *Lloyd's Non-Marine Underwriters v. J.J. Lacey Insurance Ltd.*, 2009 NLTD 148, 291 Nfld. & P.E.I.R. 149 (N.L. T.D.).

26 The Supreme Court of Canada's silence on the issue of equitable subordination in *CDIC* and *Indalex* cannot be taken, as the *CCAA* judge appears to have thought, as an outright rejection of the doctrine. In my view, the Supreme Court simply left the issue for another day.

27 It is unnecessary to decide that issue in order to resolve this appeal. The only issue is whether the *CCAA* judge was right in deciding that he had no jurisdiction to grant equitable subordination under the *CCAA*, assuming the remedy is available in Canadian law.

SUBMISSIONS AND ANALYSIS

A. PROCEDURAL OBJECTION

28 The appellant's first submission is procedural. It claims that it was unnecessary for the *CCAA* judge to determine whether he had jurisdiction to grant equitable subordination. The Union essentially says it was blindsided. It says it made no submissions on the doctrine of equitable subordination and the *CCAA* judge did not indicate that he was going to address the issue in the context of the scheduling motion. It was inappropriate and unnecessary for the court to shut the door on a novel and controversial remedy without a full factual record.

29 The respondent acknowledges that equitable subordination was not a central issue in the oral submissions before the *CCAA* judge, but points out that it was raised in some of the factums and memoranda filed before and after the hearing. The *CCAA* judge was required to determine what conduct-based inter-creditor claims would be litigated, either under the Claims Process Order or under the *CCAA*. He was entitled to determine whether he had jurisdiction to grant equitable subordination within the *CCAA*.

30 I do not accept the appellant's submission. The issue of equitable subordination was plainly before the *CCAA* judge in submissions made before and after the hearing. The Milbournes' factum made extensive submissions on equitable subordination and argued that it, along with fiduciary duty and oppression, were "live issues which should be the subject matter of a robust evidentiary record and subject to a fair and thorough due process in this court". The Union's factum suggested that some of USS's unsecured claim could be subordinated to the claims of other creditors "on account of a breach of fiduciary duty, a finding of oppression, *or otherwise*." USSC's factum argued that the Union's claim for equitable subordination should be rejected and that suitable remedies were available outside the Claims Process. In supplementary written submissions, the Union argued, in response to USSC's submissions, that the determination of the issue of equitable subordination should await an evidentiary record.

31 Moreover, the issue before the *CCAA* judge was not simply scheduling. The motion sought directions on the extent and nature of production and discovery with respect to the various objections. The Union argued that the objections had to be resolved before there could be approval of a plan of restructuring, a sale process or a distribution to creditors. The allegations that USS's claims should be re-characterized, invalidated, disallowed or subordinated had to be resolved and the *CCAA* judge had to determine a process for their resolution. Some might be dealt with under the Claims Process Order and some might be dealt with outside that Order but nevertheless in the *CCAA* proceedings. Some might not be dealt with under the *CCAA* at all.

32 The *CCAA* judge was plainly aware that a determination of the inter-creditor claims could have implications for the approval of any subsequent reorganization, sale of the business or credit bid. It was appropriate for him to consider whether the court had jurisdiction to address those claims and, if so, how and when.

33 An evidentiary record was unnecessary. The *CCAA* judge was not deciding whether equitable subordination applied on the facts of this case. The issue was whether he had jurisdiction to grant equitable subordination under the *CCAA*.

34 I turn now to the question whether the *CCAA* judge correctly held that he had no jurisdiction under the *CCAA* to order equitable subordination of USS's claims.

B. JURISDICTION TO ORDER EQUITABLE SUBORDINATION

35 I will begin by summarizing the *CCAA* judge's reasons on this issue. I will then set out the submissions of the parties, identify the standard of review, describe the methodology I will use and apply that methodology to the legislation.

(1) The CCAA judge's reasons

36 The *CCAA* judge noted that although the *CCAA* gives authority to re-characterize debt as equity and to invalidate a preference or assignment, there is no express provision conferring jurisdiction to grant equitable subordination. He was of the view that any jurisdiction to do so would have to be found in s. 11, which provides that "the court ... may, subject to the restrictions set out in this Act ... make any order that it considers appropriate in the circumstances."

37 He observed that there is no Canadian case law supporting that authority and, when given the occasion to confirm the existence of equitable subordination on two occasions, the Supreme Court of Canada had declined to do so: *Canada Deposit Insurance Corp.*; and *Indalex*. He suggested that one might infer from this that the Supreme Court had rejected the principle of equitable subordination.

38 He found, however, that to the extent the issue remained open, the *CCAA* evidenced an intention to exclude equitable subordination. When Parliament amended the legislation in 2009, it gave authority under s. 6(8) to subordinate debt as being in substance equity, but it did not enact any provision to subordinate a claim based on the conduct of the creditor. Nor had it drafted s. 36.1, which permitted the court to invalidate preferences and assignments, broadly enough to permit the court to make an order for equitable subordination. These provisions, he said, were "restrictions set out in this Act", limiting the court's broad discretion under s. 11. Parliament's failure to include equitable subordination in the remedies introduced in 2009 must be taken as indicative of an intention to exclude the operation of the doctrine under the *CCAA*. This, he said, was a policy decision the court must respect.

(2) The submissions of the parties

39 The appellant submits the *CCAA* judge had jurisdiction to grant equitable subordination pursuant to s. 11 of the *CCAA* in the absence of express "restrictions" on that jurisdiction. He erred in implying restrictions based on Parliament's failure to amend the legislation.

40 The respondent submits that Canadian courts have all the tools they need to assess, review and, where necessary, subordinate or invalidate creditors' claims in a manner consistent with the underlying legislation, without the need for equitable subordination. Some of these tools are the result of the 2009 amendments to the *BIA* and the *CCAA*. Parliament might have expanded those amendments to incorporate equitable subordination or some other conduct-based remedy, but declined to do so. The court should not invoke a controversial doctrine that Parliament declined to adopt when it had the opportunity to do so.

(3) The standard of review

41 The parties agree that the applicable standard of review is correctness: *Housen v. Nikolaisen*, 2002 SCC 33 (S.C.C.), at para. 8; and *ATB Financial v. Metcalfe & Mansfield Alternative Investments II Corp.*, 2008 ONCA 587, 92 O.R. (3d) 513 (Ont. C.A.), at para. 40.

(4) Framework for analysis

42 In *Ted Leroy Trucking Ltd., Re*, 2010 SCC 60, [2010] 3 S.C.R. 379 (S.C.C.) [hereinafter Century Services], at paras. 65ff., the Supreme Court of Canada gave guidance on the approach to the scope of statutory remedies under the *CCAA*, and, if need be, under related sources of judicial authority. The court adopted the analysis proposed by Justice Georgina R. Jackson of the Court of Appeal for Saskatchewan and Professor Janis Sarra in an article entitled, "Selecting the Judicial Tool to get the Job Done: An Examination of Statutory Interpretation, Discretionary Power and Inherent Jurisdiction in Insolvency Matters" in Sarra, ed., *Annual Review of Insolvency Law, 2007* (Toronto: Thomson Carswell, 2007), at p. 41. Blair J.A. also approved of this approach in *Metcalfe & Mansfield*, at paras. 48-49.

43 Jackson and Sarra note that the *CCAA* is skeletal legislation and advocate a transparent and consistent methodology as judges define the scope of their jurisdiction under the statute. They propose that the courts should take a hierarchical view of the powers at their disposal, adopting a broad, liberal and purposive interpretation of the statute and applying the principles of statutory interpretation before turning to other tools such as the common law or the exercise of inherent jurisdiction.

44 At para. 66 of *Century Services*, the Supreme Court held that in most cases, the search for jurisdiction under the *CCAA* should be an exercise in statutory interpretation. The starting point is the "big picture" principles of statutory interpretation.

45 Driedger's modern principle is the crucial tool for construing skeletal legislation such as the *CCAA*. A court must go beyond an examination of the wording of the statute and consider the scheme of the Act, its object or the intention of the legislature and the context of the words in issue:

> Today there is only one principle or approach, namely, the words of an Act are to be read in their entire context and in their grammatical and ordinary sense harmoniously with the scheme of the Act, the object of the Act, and the intention of Parliament.

See: Jackson and Sarra, at p. 47; Elmer A. Driedger, *The Construction of Statutes*, 2d ed (Toronto: Butterworths, 1983) at p. 87, cited in *Bell ExpressVu Ltd. Partnership v. Rex*, 2002 SCC 42, [2002] 2 S.C.R. 559 (S.C.C.), at para. 26. See also *Rizzo & Rizzo Shoes Ltd., Re*, [1998] 1 S.C.R. 27 (S.C.C.), at paras. 23, 40.

46 With this in mind, I will apply the framework in *Century Services* to the search for jurisdiction. I turn first to a consideration of the purpose and scheme of the *CCAA*, before considering the language of the statute.

(5) Application of the framework

(i) The purpose of the CCAA

47 There is no dispute about the purpose of the *CCAA*. It describes itself as "An Act to facilitate compromises and arrangements between companies and their creditors". Its purpose is to avoid the devastating social and economic effects of commercial bankruptcies. It permits the debtor to continue to carry on business and allows the court to preserve the status quo while "attempts are made to find common ground amongst stakeholders for a reorganization that is fair to all": *Century Services*, at para. 77.

48 The *CCAA* has proven to be a flexible and successful tool to enable businesses to avoid bankruptcy. As Professor Sarra notes, "[i]t has been the statute of choice for debtor corporations in every major Canadian restructuring in the past quarter century, including national airlines, major steel and forestry companies, telecommunications companies, major retail chains, real estate and development groups, and the national blood delivery system": Janis P. Sarra, *Rescue! The Companies' Creditors Arrangement Act*, 2d ed. (Toronto: Carswell, 2013), at p. 1.

49 The *CCAA* achieves its goals through a summary procedure for the compromise or arrangement of creditors' claims against the company. It was described in *Stelco Inc., Re* (2005), 75 O.R. (3d) 5 (Ont. C.A.), at para. 36, as:

> a statutory framework to extend protection to a company while it holds its creditors at bay and attempts to negotiate a compromised plan of arrangement that will enable it to emerge and continue as a viable economic entity, thus benefiting society and the company in the long run, along with the company's creditors, shareholders, employees and other stakeholders.

50 The process has been effective because it is summary, it is practical, it is supervised by an independent expert monitor and it is managed in real time by an experienced commercial judge.

51 *Century Services* is a good example of how the purpose of the *CCAA* informs the exercise of the court's authority. At issue in that case were the reconciliation of another federal statute with the *CCAA* and the scope of a *CCAA* judge's discretion. At para. 70, the orders of the *CCAA* judge were considered squarely within the context of the purpose of the Act:

> The general language of the *CCAA* should not be read as being restricted by the availability of more specific orders. However, the requirements of appropriateness, good faith, and due diligence are baseline considerations that a court should always bear in mind when exercising *CCAA* authority. Appropriateness under the *CCAA* is assessed by inquiring whether the order sought advances the policy objectives underlying the *CCAA*. The question is whether the order will usefully further efforts to achieve the remedial purpose of the *CCAA* — avoiding the social and economic losses resulting from liquidation of an insolvent company. I would add that appropriateness extends not only to the purpose of the order, but also to the means it employs. Courts should be mindful that chances for successful reorganizations are enhanced where participants achieve common ground and all stakeholders are treated as advantageously and fairly as the circumstances permit.
>
> [emphasis added]

52 The Supreme Court concluded, at para. 75, that the order advanced the underlying purpose of the *CCAA*.

(ii) The scheme of the CCAA

53 The *CCAA* has been described as "skeletal" or "under-inclusive" legislation, (Jackson and Sarra at p. 48) which grants broad powers to the courts in general terms.

54 The Act has five parts. Part I, entitled "Compromises and Arrangements" permits the court to sanction a compromise or arrangement between a company and its secured or unsecured creditors, or both.

55 The powers of the court are found in Part II, entitled "Jurisdiction of Courts". The statute gives the court jurisdiction to receive applications, order stays, approve debtor-in-possession financing and appoint a monitor, among other things. Proceedings are commenced by an application to the Superior Court. The court generally grants an initial stay, appoints a monitor with authority to repudiate leases and other agreements and authorizes debtor in possession financing. A process is established for the identification and review of creditors' claims by the monitor and to deal with disputed claims, with the ultimate purpose of establishing classes of creditors who will vote, by class, on the compromise or arrangement.

56 One possible outcome is the preparation of a plan of arrangement. Creditors vote by class on the plan at a meeting called for that purpose. A majority by number of creditors in each class, together with two-thirds of the creditors in that class by dollar value, must approve the plan. If a class of creditors approves the plan, it is binding on all creditors within the class, subject to the court's approval of the plan. If all classes of creditors approve the plan, the court must then approve the plan as a final step.

57 Part III, entitled "General", deals with such issues as the determination of the amount of creditors' claims, classes of creditors, the duties of monitors, the disclaimer of agreements between the company and third parties and preferences and transfers at undervalue.

58 Section 19 identifies "claims" that may be dealt with in a compromise or arrangement. Those are claims provable in bankruptcy that relate to debts or liabilities, present or future, to which the *debtor company* is subject or may become subject before the compromise or arrangement is sanctioned. [4]

59 The significance of this definition is that the focus of the plan of arrangement is claims against the *debtor company* that are provable in bankruptcy. The *CCAA* judge identified this significance at para. 59 of his reasons, where he noted that s. 19(1) of the *CCAA* provides, effectively, "that a plan of compromise or arrangement may only deal with claims that relate to debts or liabilities to which a debtor company is subject at the time of commencement of proceedings under the *CCAA*". At para. 61, he noted that neither the Claims Process Order nor the *CCAA* contemplated that inter-creditor claims would be addressed by or be relevant to a plan of arrangement.

60 Section 20 sets out the method for determining the amount of the claim of any secured or unsecured creditors. In most cases, it will be the amount "determined by the court on summary application by the company or by the creditor".

61 Section 22 provides for the establishment of classes of creditors for the purpose of voting on a compromise or arrangement, based on, among other things, the nature of their claims, the nature of the security in respect of their claims and the remedies available to them in relation to their claims. Creditors may be included in the same class "if their interests or rights are sufficiently similar to give them a commonality of interest".

62 Part IV deals with Cross-Border Insolvencies. Its stated purposes are to give mechanisms to provide for the fair and efficient administration of such insolvencies, to promote cooperation with courts of other jurisdictions, to promote "the rescue of financially troubled businesses to protect investment and preserve employment" and to protect the interests of creditors, of other interested persons and of the debtor company. Part V deals with Administration.

63 The *CCAA* was amended in 2009. The amendments were the product of extensive discussion of the *BIA* and the *CCAA* in the Standing Senate Committee on Banking, Trade and Commerce. The Committee recommended amendments to the legislation, including an expanded power to review, invalidate or subordinate creditors' claims under the *CCAA*.

64 These recommendations were reflected in the 2009 amendments in two respects. First, s. 6(8) provides that a compromise or arrangement will not be approved unless it provides that all other claims are to be paid in full before an equity claim is paid.

65 This provision, coupled with the definition of "equity interest" [5] and "equity claim" [6] in s. 2(1), permits the court to determine whether a creditor's claim is in substance a share, warrant or option. This is the underpinning of the Debt/Equity Objection, an objection based on a disagreement as to the proper characterization of the disputed claims.

66 Section 22.1, also added in 2009, provides that all creditors with equity claims are to be in the same class unless the court otherwise orders, and may not, as members of that class, vote at any meeting unless the court otherwise orders.

67 Second, the 2009 amendments harmonized the rules of reviewable transactions under the *BIA* and the *CCAA*. Creditors in a *CCAA* proceeding are now entitled to invoke the provisions of the *BIA* to invalidate security granted by a debtor corporation to a creditor where a fraudulent preference or transfer at undervalue is established. Section 36.1 of the *CCAA* provides that ss. 38 and 95 to 101 of the *BIA* apply, with any required modifications, in respect of a compromise or arrangement, unless the compromise or arrangement provides otherwise.

68 USS says that the 2009 amendments reflected Parliament's decision concerning the extent of the court's jurisdiction over "reviewable transactions" in *CCAA* proceedings and the extent to which a creditor's claim can be subordinated to other claims as a result of its conduct. It says Parliament might have included jurisdiction to rearrange priorities between creditors, for example through equitable subordination, but it declined to do so.

69 The scheme of the *CCAA* focuses on the determination of the validity of claims of creditors against the company and the determination of classes of claims for the purpose of voting on a compromise or arrangement. Except as contemplated by ss. 2(1), 6(8), 22.1 and 36.1, the statute does not address either conflicts between creditors or the order of priorities of creditors. Priorities are, however, part of the background against which the plan of compromise or arrangement is negotiated.

70 There is nothing in the record before us to indicate that the issue of equitable subordination was given serious consideration at the time of the 2009 amendments or that those amendments were intended to import other remedies.

(iii) Interpreting the particular provisions before the court

71 I now turn to the words of the statute itself, considered in context and having regard to the scheme of the *CCAA*, the object of the act and the intentions of Parliament.

72 As Blair J.A. put it when deciding whether the *CCAA* granted the court the power to sanction the disputed order in *Metcalfe & Mansfield*, at para. 58, "[w]here in the words of the statute is the court clothed with authority to approve a plan incorporating a requirement for third-party releases?" The question before us is "where (if at all) in the words of the statute is the court (implicitly or explicitly) clothed with authority to make an order for equitable subordination of the USS claims?"

(a) Section 11: "The engine that drives the statutory scheme"

73 The parties focussed their arguments on whether the powers granted by s. 11 include the power to grant the remedy of equitable subordination. In order to inform the scope of s. 11, they urge us to consider the treatment of "equity" claims in s. 6(8) of the *CCAA* and the remedies available under s. 36.1.

74 In *Stelco*, at para. 36, Blair J.A. described s. 11 as "the engine that drives this broad and flexible statutory scheme". Section 11 states, in full:

> Despite anything in the *Bankruptcy and Insolvency Act* or the *Winding-up and Restructuring Act*, if an application is made under this Act in respect of a debtor company, the court, on the application of any person interested in the matter, may, subject to the restrictions set out in this Act, on notice to any other person or without notice as it may see fit, make any order that it considers appropriate in the circumstances.
>
> [Emphasis added.]

75 Prior to amendment in 2005 (S.C. 2005, c. 47, s. 128), the underlined portion above had read "subject to this Act". In *Century Services*, the Supreme Court, at paras. 67-68, interpreted this amendment as being an endorsement of the broad reading of *CCAA* jurisdiction that had been developed in the jurisprudence.

76 The jurisdiction under s. 11 has two express limitations. First, the court must find that the order is "appropriate in the circumstances". Second, even if the court considers the order appropriate in the circumstances, it must consider whether there are "restrictions set out in" the *CCAA* that preclude it.

77 As I have noted, the *CCAA* judge held that s. 11 did not confer jurisdiction to apply the doctrine of equitable subordination. The statute could have provided the authority to subordinate claims on this basis, as it did with equity claims, but it did not. He also held that the definition of "equity claim" and the option to bring proceedings under s. 36.1 were "restrictions" within the meaning of s. 11.

78 In my view, the interpretative process should start with the scope of s. 11 before the restrictions are considered in the analysis. The broad powers exercised by *CCAA* judges evolved in the jurisprudence before the concept of "restrictions" was legislated.

79 Moreover, it is inconsistent with the anatomy and history of the *CCAA* to maintain that if Parliament had intended that a *CCAA* judge would have the authority to make a certain type of order, it would have said so. The Supreme Court has made it clear that "[t]he general language of the *CCAA* should not be read as being restricted by the availability of more specific orders": *Century Services* , at para. 70.

80 What is apparent from the many creative orders that have been made, before and since the 2009 amendments, is that such orders are made squarely in furtherance of the legislature's objectives. In *Century Services*, at para. 59, the Supreme Court observed that "[j]udicial discretion must of course be exercised in furtherance of the *CCAA*'s purposes", to avoid the devastating social and economic effects of bankruptcy while an attempt is made to organize the affairs of the debtor under court supervision.

81 The words "may ... make any order it considers appropriate in the circumstances" in s. 11 must, in my view, be read as "may ... *in furtherance of the purposes of this act*, make any order it considers appropriate in the circumstances."

82 There is no support for the concept that the phrase "any order" in s. 11 provides an at-large equitable jurisdiction to reorder priorities or to grant remedies as between creditors. The orders reflected in the case law have addressed the business at hand: the compromise or arrangement.

83 I turn to the second limit on the court's jurisdiction under s. 11, the "restrictions set out in this Act". The first question is whether such restrictions must be express or can be implied.

84 It bears noting that there are numerous express restrictions on the court's jurisdiction contained within the *CCAA* itself. Some are contained in Part II (Jurisdiction of Courts) and some are actually preceded by the heading "Restriction". In *North American Tungsten Corp. v. Global Tungsten and Powders Corp.*, 2015 BCCA 426, 81 B.C.L.R. (5th) 102 (B.C. C.A.), at para. 34, the British Columbia Court of Appeal observed that "where other provisions of the statute are intended to restrict the powers under ss. 11 and 11.02 of the statute, they do so in unequivocal terms."

85 The *CCAA* judge found that there were "restrictions set out" in the *CCAA* that prevented the court from applying equitable subordination, namely the definition of "equity claim" in s. 2(1) and the provisions of s. 36.1. Essentially, he found that Parliament could have introduced equitable subordination into the *CCAA* when it amended the legislation in 2009, but declined to do so. "The court must respect that policy decision", he said at para. 53. The respondent supports this interpretation.

86 I agree with the appellant that "equity claim" is not a restriction at all, but a definition. Together with s. 6(8), it codifies what was essentially the law before the 2009 amendments. The purpose of this involvement in the priority of claims is to remove shareholders from the process of arriving at a compromise or arrangement, absent permission of the court. It has nothing to do with any wrongdoing by the person with the equity interest. The only "restriction", if any, would be the lack of flexibility to reverse this statutory subordination, as Pepall J. pointed out in *Nelson Financial Group Ltd., Re*, 2010 ONSC 6229, 75 B.L.R. (4th) 302 (Ont. S.C.J. [Commercial List]), at para. 34. However, this has to do only with subordination flowing from the characterization of a claim and not equitable subordination.

87 I also agree that the plain meaning of the words "subject to the restrictions *set out* in this Act" refers to express restrictions, of which there are a number.

(b) Subsection 6(8): Subordination of "equity claims"

88 In the court below, and in the appellant's submissions in this court, there was a blurring of the distinction between the separate concepts of "equity claim" and the doctrine of "equitable subordination". The *CCAA* judge's reasons referred at times to the "subordination claims" of the Union and the Milbournes as including the equitable subordination claims and the claims for oppression and breach of fiduciary duty.

89 As explained earlier, s. 6(8) of the *CCAA* effectively subordinates "equity claims", as defined, to the claims of all other creditors. No compromise or arrangement can be approved unless it provides for other claims to be paid, in full, before equity claims are paid.

90 With the exception of environmental claims, ss. 6(8) and 22.1 are the only provisions of the *CCAA* to deal expressly with priorities between creditors. [7] There is a clear rationale for these provisions. In E. Patrick Shea, *BIA, CCAA & WEPPA: A Guide to the New Bankruptcy & Insolvency Regime* (Markham: LexisNexis Group, 2009), at p. 89, the author explains that "[t]he intention of these amendments is to remove the shareholder/creditor from the reorganization process, unless the court orders that they have a seat at the table."

91 "Equitable subordination", on the other hand, refers to the doctrine at issue here: a form of equitable relief to subordinate the claim of a creditor who has engaged in inequitable conduct. Such a claim is not an "equity claim", as defined. If it were, it would be subordinated without the need for intervention by the court.

92 Pepall J. dealt with these different principles and distinguished them clearly in *I. Waxman & Sons Ltd.*, a Commercial List decision that predated the 2009 amendments. There, a trustee in bankruptcy brought a motion for advice and directions as to whether a judgment creditor's claim should be allowed. Other creditors argued that his claim was rooted in equity and was not a debt claim. In the alternative, they argued that even if it was a debt claim, it should be subordinated to their claims pursuant to the doctrine of equitable subordination.

93 Pepall J. addressed the argument that the judgment creditor's claim was an equity claim under the heading "Characterization" (paras. 18-26), because the issue was whether his claim was properly characterized as one of equity or debt, with the attendant priority consequences. Next she considered whether, even though she had found that the claim was a debt claim, it should be subordinated pursuant to the doctrine of equitable subordination (paras. 27-35). She noted, at para. 27, that "[a]s its name suggests, the basis for development of the doctrine is the equitable jurisdiction of the court". She held that even if it applied in Canada, which was not established, there was no evidence on which to apply it in that case.

94 By contrast, the *CCAA* judge in this case disposed of these issues under one heading, "The Authority of the Court to Adjudicate Claims for Debt Re-Characterization and for Equitable Subordination", at paras. 38-53. He found, at para. 51, that the absence of any provision in the *CCAA* that would permit the application of equitable subordination was indicative of an intention to exclude the operation of the doctrine.

95 The *CCAA* judge appears to have treated equitable subordination as akin to equity claims as defined in s. 2(1), the subordination of equity claims in s. 6(8) and the remedies under s. 36.1. He found that because equitable subordination is not mentioned in the context of these remedies, Parliament must have intended to exclude it.

96 The distinction between these terms undermines the argument that equitable subordination does not exist because it was not included as part of the definition of (or together with the subordination of) equity claims. Equity claims are subordinated in order to keep shareholders away from the table while the claims of other creditors are being sorted out. Even prior to being explicitly subordinated by statute in 2009, they generally ranked lower than general creditors: *Sino-Forest Corp., Re*, 2012 ONCA 816, 114 O.R. (3d) 304 (Ont. C.A.), at para. 30. The purpose of the 2009 amendments appears to have been to confirm and clarify the law: see The Report of the Standing Senate Committee on Banking, Trade and Commerce, *Debtors and Creditors Sharing the Burden: A Review of the Bankruptcy and Insolvency Act and the Companies' Creditors Arrangement Act* (Ottawa, November 2003), at p. 158-59.

(c) Section 36.1: Preferences and Assignments

97 Section 36.1, which was part of the 2009 amendments, incorporates by reference provisions of the *BIA* permitting the court to invalidate prior fraudulent preferences or fraudulent assignments.

> 36.1 (1) Sections 38 and 95 to 101 of the *Bankruptcy and Insolvency Act* apply, with any modifications that the circumstances require, in respect of a compromise or arrangement unless the compromise or arrangement provides otherwise.

98 The respondent argues that the inclusion of these express provisions implies that no other form of equitable remedy was contemplated. Its argument is that, had Parliament wished to invalidate or subordinate claims of creditors who had engaged in inequitable conduct in relation to other creditors, it could have expressly included that remedy.

99 I would not read anything into s. 36.1, one way or the other. Nor would I regard it as a "restriction" set out in the Act within the meaning of s. 11.

(6) Summary

100 The appellant requested "a declaration that the *CCAA* contains no restrictions within the meaning of s. 11 on the court's ability to apply the doctrine of equitable subordination." In my view, this is the wrong inquiry and this is why I reach the same result as the *CCAA* judge, but for different reasons.

101 I would not grant the relief sought because, applying the principles of statutory interpretation, nowhere in the words of the *CCAA* is there authority, express or implied, to apply the doctrine of equitable subordination. Nor does it fall within the scheme of the statute, which focuses on the implementation of a plan of arrangement or compromise. The *CCAA* does not legislate a scheme of priorities or distribution, because these are to be worked out in each plan of compromise or arrangement. The subordination of "equity claims" is directed towards a specific group, shareholders, or those with similar claims. It also has a specific function, consistent with the purpose of the *CCAA*: to facilitate the arrangement or compromise without shareholders' involvement.

102 The success of the *CCAA* in fulfilling its statutory purpose has been in large measure due to the ability of judges to fashion creative solutions, for which there is no express authority, through the exercise of their jurisdiction under s. 11. As Blair J.A. noted in *Metcalfe and Mansfield*, however, the court's powers are not limitless. They are shaped by the purpose and scheme of the *CCAA*. The appellant has not identified how equitable subordination would further the remedial purpose of the *CCAA*.

103 At this stage of the analysis, I am mindful of the Supreme Court's observation in *Century Services* that in most cases the court's jurisdiction in *CCAA* matters will be found through statutory interpretation. I am also mindful of its observation in *Indalex*, at para. 82, that courts should not use an equitable remedy to do what they wish Parliament had done through legislation. In my view, there is no "gap" in the legislative scheme to be filled by equitable subordination through the exercise of discretion, the common law, the court's inherent jurisdiction or by equitable principles.

104 There is no provision in the *CCAA* equivalent to s. 183 of the *BIA* or §105(a) of the U.S. *Bankruptcy Code*. Section 183 invests the bankruptcy court with "such jurisdiction at law and in equity" as will enable it to exercise its bankruptcy jurisdiction. This is significant, because if equitable subordination is to become a part of Canadian law, it would appear that the *BIA* gives the bankruptcy court explicit jurisdiction as a court of equity to ground such a remedy and a legislative purpose that is more relevant to the potential reordering of priorities.

CONCLUSION

105 For these reasons, I would dismiss the appeal. I would order that counsel may make written submissions as to costs, not to exceed five pages in length, excluding costs outlines. I would assume counsel can agree on a timetable for delivery of all costs submissions within 30 days of the release of these reasons.

P. Lauwers J.A.:

I agree

M.L. Benotto J.A.:

I agree

Appeal dismissed.

Footnotes

1 *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36.

2 6(8) No compromise or arrangement that provides for the payment of an equity claim is to be sanctioned by the court unless it provides that all claims that are not equity claims are to be paid in full before the equity claim is to be paid.

3 In a subsequent ruling, *U.S. Steel Canada Inc., Re*, 2016 ONSC 569 (Ont. S.C.J.), the *CCAA* judge dismissed the Debt/Equity objection, finding that approximately $2 billion of USSC's unsecured claims and $73 million in secured claims were properly characterized as debt rather than equity. He also dismissed the objection that approximately $118 million in secured claims should be invalidated due to lack of consideration or as a fraudulent preference.

4 *CCAA*, s. 2(1): "*claim* means any indebtedness, liability or obligation of any kind that would be a claim provable within the meaning of section 2 of the *Bankruptcy and Insolvency Act*." Section 121 of the *BIA* states that claims provable in bankruptcy are those to which the bankrupt is subject: "121(1) All debts and liabilities, present or future, to which the bankrupt is subject on the day on which the bankrupt becomes bankrupt or to which the bankrupt may become subject before the bankrupt's discharge by reason of any obligation incurred before the day on which the bankrupt becomes bankrupt shall be deemed to be claims provable in proceedings under this Act."

5 "*Equity interest* means (a) in the case of a company other than an income trust, a share in the company — or a warrant or option or another right to acquire a share in the company — other than one that is derived from a convertible debt, and (b) in the case of an income trust, a unit in the income trust — or a warrant or option or another right to acquire a unit in the income trust — other than one that is derived from a convertible debt."

6 "*Equity claim* means a claim that is in respect of an equity interest, including a claim for, among others, (a) a dividend or similar payment, (b) a return of capital, (c) a redemption or retraction obligation, (d) a monetary loss resulting from the ownership, purchase or sale of an equity interest or from the rescission, or, in Quebec, the annulment, of a purchase or sale of an equity interest, or (e) contribution or indemnity in respect of a claim referred to in any of paragraphs (a) to (d)."

7 Subsection 11.8(8) gives the federal and provincial Crowns priorities for environmental claims against the debtor.

End of Document

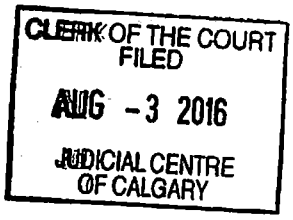
Tab 8

Form 27

[Rules 6.3 and 10.52(1)]

Clerk's Stamp

COURT FILE NUMBER	1501-07813
COURT	Court of Queen's Bench of Alberta
JUDICIAL CENTRE	Calgary



PLAINTIFFS (APPLICANTS)	FRONTFOUR CAPITAL CORP. and FRONTFOUR CAPITAL GROUP LLC
DEFENDANT (RESPONDENT)	LIGHTSTREAM RESOURCES LTD.
DOCUMENT	**APPLICATION BY THE PLAINTIFFS, FRONTFOUR CAPITAL CORP. AND FRONTFOUR CAPITAL GROUP LLC**

ADDRESS FOR SERVICE AND CONTACT INFORMATION OF PARTY FILING THIS DOCUMENT

CASSELS BROCK & BLACKWELL LLP
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NOTICE TO RESPONDENT(S):
(Indicate name(s) and status of Respondent(s))

Lightstream Resources Ltd., defendant (respondent)

This Application is made against you. You are a Respondent.

You have the right to state your side of this matter before the Master/Judge.

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

Date:	August 30, 2016
Time:	10:00am
Where:	Calgary Courts Centre, 601 - 5 Street S.W. Calgary, AB T2P 5P7
Before Whom:	Justice Campbell

Go to the end of this document to see what else you can do and when you must do it.

Remedy claimed or sought:

1. An Order granting the plaintiffs, FrontFour Capital Corp. and FrontFour Capital Group LLC leave to issue an Amended Statement of Defence in the form attached hereto as "Schedule A".

2. Such further and other relief as this Honourable Court deems just.

Grounds for making this Application:

3. The Plaintiff, FrontFour Capital Corp., is the Investment Fund Manager and Portfolio Manager of the FrontFour Opportunity Fund. FrontFour Capital Corp is based in Toronto, Ontario.

4. The Plaintiff, FrontFour Capital Group LLC, is the Investment Advisor to the FrontFour Master Fund Ltd. and separately managed accounts. FrontFour Capital Group LLC is headquartered in Greenwich, Connecticut, USA.

5. Collectively, FrontFour Capital Corp. and FrontFour Capital Group LLC are referred to herein as **FrontFour**.

6. The Defendant, Lightstream Resources Ltd. (**Lightstream** or the **Company**), is a light oil exploration and production corporation with its registered and records office in Calgary, Alberta. Until May 22, 2013, when the company was renamed, Lightstream operated as Petrobakken Energy Ltd. (**Petrobakken**).

7. This action was commenced by the plaintiffs by way of Statement of Claim filed July 13, 2015.

8. The plaintiffs commenced the action on the basis that Lightstream's conduct with respect to certain unsecured notes was oppressive pursuant to section 242 of the *Alberta Business Corporations Act*, RSA 2000, c B-9 and in breach of the indenture governing such notes.

9. FrontFour now seeks to amend the statement of claim to add the following individuals who, at all material times, were the directors of the Company: John D. Wright, Ian Brown, Martin Hislop, Kenneth R. McKinnon, Corey C. Ruttan, Craig Lothian and W. Brett Wilson.

10. FrontFour's representative, Stephen Loukas, has already been examined by Lightstream's counsel with respect to the misrepresentations at issue.

11. Neither the Company nor the Directors will suffer any non-compensable prejudice as a result of the amendments.

Material or evidence to be relied on:

12. Such further and other documentary evidence as counsel may advise and this Honourable Court may permit.

Applicable rules:

13. Rules 3.62, 3.63, 3.74, and 6.3 of the *Alberta Rules of Court*, Alta Reg 124/2010.

Applicable Acts and regulations:

14. Section 242 of the *Alberta Business Corporations Act*, RSA 2000, c B-9.

Any irregularity complained of or objection relied on:

15. None.

How the Application is proposed to be heard or considered:

16. The application is to be heard orally.

AFFIDAVIT EVIDENCE IS REQUIRED IF YOU WISH TO OBJECT.

WARNING

If you do not come to Court either in person or by your lawyer, the Court may give the applicant(s) what they want 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 time shown at the beginning of the form. If you intend to give evidence in response to the application, you must reply by filing an affidavit or other evidence with the Court and serving a copy of that affidavit or other evidence on the applicant(s) a reasonable time before the application is to be heard or considered.

Schedule "A"

COURT FILE NUMBER	1501-07813
COURT	Court of Queen's Bench of Alberta
JUDICIAL CENTRE	Calgary

Clerk's Stamp

PLAINTIFF	FRONTFOUR CAPITAL CORP. FRONT FOUR CAPITAL GROUP LLC
DEFENDANT	LIGHTSTREAM RESOURCES LTD., JOHN D. WRIGHT, IAN BROWN, MARTIN HISLOP, KENNETH R. MCKINNON, COREY C. RUTTAN, CRAIG LOTHIAN and W. BRETT WILSON
DOCUMENT	**AMENDED STATEMENT OF CLAIM**

ADDRESS FOR SERVICE AND CONTACT INFORMATION OF PARTY FILING THIS DOCUMENT	**CASSELS BROCK & BLACKWELL LLP** 2100 Scotia Plaza 40 King Street West Toronto, ON M5H 3C2 Tel: 416.869.5300 Fax: 416.360.8877 Timothy Pinos Tel: 416.869.5784 Fax: 416.350.6903 tpinos@casselsbrock.com Stephanie Voudouris Tel: 416.860.6617 Fax: 416.642.7145 svoudouris@casselsbrock.com

NOTICE TO DEFENDANT(S)

You are being sued. You are a Defendant.

Go to the end of this document to see what you can do and when you must do it.

Note: State below only facts and not evidence (Rule 13.6)

Statement of facts relied on:

(I) The Parties

1. The Plaintiff, FrontFour Capital Corp., is the Investment Fund Manager and Portfolio Manager of the FrontFour Opportunity Fund. FrontFour Capital Corp is based in Toronto, Ontario.

2. The Plaintiff, FrontFour Capital Group LLC, is the Investment Advisor to the FrontFour Master Fund Ltd. and separately managed accounts. FrontFour Capital Group LLC is headquartered in Greenwich, Connecticut, USA.

3. Collectively, FrontFour Capital Corp. and FrontFour Capital Group LLC are referred to herein as **FrontFour**.

4. FrontFour primarily invests in Canada and the United States.

5. The Defendant, Lightstream Resources Ltd. (**Lightstream** or the **Company**), is a light oil exploration and production corporation with its registered and records office in Calgary, Alberta. Until May 22, 2013, when the company was renamed, Lightstream operated as Petrobakken Energy Ltd. (**Petrobakken**).

6. At all material times, the directors of Lightstream were John D. Wright, Ian Brown, Martin Hislop, Kenneth R. McKinnon, Corey C. Ruttan, Craig Lothian and W. Brett Wilson (the "**Directors**"). The Directors were personally implicated in the oppressive conduct and are thus jointly and severally liable. Specifically, the Directors, jointly and severally, exercised their power in a fashion which caused Lightstream's business and affairs to be conducted in a way that unfairly disregarded FrontFour's interests and led to an unfairly prejudicial result.

(II) The Unsecured Notes and Indenture

7. On January 30, 2012, Lightstream (then operating as Petrobakken) closed a private placement of unsecured senior notes (the **Unsecured Notes**) having a principal amount of $900,000,000.00 (USD). The Unsecured Notes bear interest at a rate of 8.625% per annum and mature February 1, 2020.

8. In 2014, Lightstream repurchased $100,000,000.00 (USD) of the principal amount of the outstanding Unsecured Notes and retired them, leaving a total of $800,000,000.00 11(USD) of the principal amount of Unsecured Notes that remain outstanding to this date.

9. The Unsecured Notes are governed by an indenture (the **Indenture**) dated January 30, 2012 between Lightstream (Petrobakken as it then was) as issuer,

Petrobakken Capital Ltd. and PBN Partnership as guarantors (together with such other parties as may become guarantors under the Indenture from time to time, the **Guarantors**), U.S. Bank National Association as trustee, and Computershare Trust Company of Canada as Canadian trustee.

10. The Indenture provides for a number of rights to holders of the Unsecured Notes (the **Unsecured Noteholders**), enumerates binding covenants on Lightstream giving rise to default remedies should they be breached, and places certain strict restrictions on the Company regarding the incurrence of further debt.

11. The Indenture provides that the Company may incur or issue **Permitted Refinancing Indebtedness** which the Indenture defines, among other things, to include indebtedness used to refinance any other indebtedness of Lightstream or its subsidiaries.

12. The Indenture states that Lightstream may only incur Permitted Refinancing Indebtedness if particular conditions are met, including that the refinancing indebtedness in question has a final maturity date or redemption date no earlier than the final maturity date of the Unsecured Notes.

13. The Indenture further restricts Lightstream by providing that the Company and the Guarantors may not incur any indebtedness that is contractually subordinated to any other indebtedness, unless such indebtedness is also contractually subordinated to the Unsecured Notes and the applicable guarantees, on substantially identical terms. This ensures that the Unsecured Noteholders would always rank only behind, or be primed by, the existing first lien lender to the Company (the existing first lien lender being a syndicate of creditors including certain major Canadian banks, pursuant to a secured credit facility with the Company).

14. The Indenture restricts Lightstream from incurring or permitting to exist any lien other than **Permitted Liens** unless the Unsecured Notes are secured by a lien on such property or assets on an equal and ratable basis with the other indebtedness so secured. The Indenture defines Permitted Liens, among other things, as liens securing Permitted Refinancing Indebtedness.

15. The Indenture provides that Lightstream may not, without the prior consent of each affected Unsecured Noteholder, modify any of the provisions related to the Unsecured Noteholders unconditional right to receive principal, premium (if any), and interest on the Unsecured Notes, and such right may further not be affected or impaired without such consent.

(III) FrontFour Subscribes to the Notes

16. Beginning in or about February 3, 2015 and until March 12, 2015, FrontFour, in its capacity as investment advisor to funds that it manages, purchased a substantial principal amount of the Unsecured Notes.

17. As at May 12, 2015, FrontFour's resultant holdings of Unsecured Notes of the Company bore a face value of $31,750,000.00 (USD).

18. The Indenture terms bind Lightstream. Lightstream must perform its various obligations thereunder and abide by its restrictions. Further, the Indenture crystallizes the duties owed to FrontFour as an Unsecured Noteholder.

(IV) The Proposed Refinancing Transaction

19. On July 2, 2015, Lightstream issued a press release (the **July 2 Press Release**) in which the Company announced for the first time that it had entered into a privately negotiated agreement (the **Proposed Refinancing Transaction** or **Transaction**) with certain but not all of the Unsecured Noteholders.

20. The July 2 Press Release was posted to the System for Electronic Document Analysis and Retrieval (**SEDAR**). FrontFour located the July 2 Press Release through SEDAR shortly after its posting.

21. The July 2 Press Release came as a total surprise to FrontFour, which had previously not been notified of the Transaction by Lightstream, notwithstanding that FrontFour and Lightstream had been in communication to that time.

22. The Proposed Refinancing Transaction contemplates, among other things:

    (a) the exchange of a total of $465,000,000.00 (USD) Unsecured Notes for an aggregate amount of $395,000,000.00 (USD) newly issued 9.875% second-lien secured notes due June 15, 2019 (the **Secured Notes**) representing an exchange ratio of Unsecured Notes to Secured Notes of 1.00:0.85;

    (b) the issuance to the same select parties of an additional $200,000,000.00 (USD) in Secured Notes for cash; and

    (c) the contractual subordination of the Secured Notes to holders of the Company's existing first lien debt pursuant to an undisclosed intercreditor agreement.

23. The July 2 Press Release states that the Company expects to close the Transaction in mid-July 2015.

(V) Lightstream's Oppressive Conduct

24. The cumulative effect of the Proposed Refinancing Transaction is oppressive, unfairly prejudicial to, and unfairly disregarding of the interests of FrontFour.

25. Lightstream never provided notice of the Proposed Refinancing Transaction to FrontFour prior to the July 2 Press Release. Nor was any other Unsecured Noteholder not party to the Transaction previously notified.

26. Lightstream's President and CEO, the Respondent John D. Wright ("Wright"), repeatedly made representations to this effect right up until the time of the Secured Notes Transaction.

27. As recently as a few weeks prior to the Secured Notes Transaction FrontFour expressed that if Lightstream were to pursue a transaction, that the transaction offered to all of the bondholders. In response, Wright stated that Lightstream was not contemplating a potential transaction and that if they were to pursue a transaction along the lines of the Secured Notes Transaction, they would offer it to all bondholders.

28. The above-noted representations (collectively, the "Misrepresentations") all proved to be false. In fact, Lightstream was under significant pressure from Apollo and had already committed to the Proposed Refinancing Transaction which was within weeks of being completed. Accordingly, the Misrepresentations were made falsely, recklessly and/or negligently.

29. The Misrepresentations were made outside the scope of Wright's responsibilities as an officer and director of Lightstream. Nevertheless, the Misrepresentations were made with the full knowledge and agreement of the Directors, as they were directed at inducing FrontFour, and other senior unsecured bondholders, to maintain their positions in Lightstream.

30. The Directors were well aware that any precipitous move by FrontFour, or any other senior unsecured bondholders, would jeopardize the Secured Notes Transaction and, with it, the opportunity to entrench themselves as directors and their interests in management.

31. Notwithstanding the Misrepresentations, on July 2, 2015, Lightstream announced the Secured Notes Transaction.

32. Lightstream never provided FrontFour an opportunity to participate in the Proposed Refinancing Transaction on the same basis as the undisclosed parties who are to be issued Secured Notes in the Transaction, or at all.

33. The Proposed Refinancing Transaction currently contemplates inclusion of only certain existing Unsecured Noteholders to the exclusion of FrontFour and other interested Unsecured Noteholders in the same class.

34. The Proposed Refinancing Transaction would create a scenario in which Unsecured Noteholders not party to it will arbitrarily, oppressively, and prejudicially see the value of their debt significantly downgraded, and their exposure to loss in an event of default greatly increased.

35. The Company's announcement of the Proposed Refinancing Transaction shortly before the national Fourth of July holiday in the United States and the Calgary Stampede in Alberta demonstrates the Company's apparently calculated timing, the purpose of which 'was to attempt to execute the Proposed Refinancing

Transaction without considered attention or scrutiny from affected Unsecured Noteholders not party to the Transaction.

36. Contrary to the terms of the Indenture and in an oppressive and unfairly prejudicial manner to FrontFour:

(a) the Proposed Refinancing Transaction would result in the issuance of Secured Notes bearing a final maturity date earlier than the final maturity date of the Unsecured Notes;

(b) the Proposed Refinancing Transaction would result in indebtedness that is not contractually subordinated to the Unsecured Notes—indeed, the Secured Notes, by virtue of being secured, improperly rank in priority to the Unsecured Notes;

(c) the Proposed Refinancing Transaction will result in the incurrence of a lien in circumstances where: (i) the Transaction will not constitute a Permitted Refinancing Indebtedness under the Indenture; and (ii) in any event, the Unsecured Notes will not be secured by a lien on such property or assets on an equal and ratable basis with the other indebtedness so secured (i.e. the Secured Notes) or at all; and

(d) Lightstream did not obtain the prior consent of FrontFour as a holder of Unsecured Notes, notwithstanding that the Proposed Refinancing Transaction would have the de facto effect of significantly impairing the repayment rights of the Unsecured Noteholders under the Indenture while benefitting a select group of Unsecured Noteholders to the express detriment of FrontFour.

(e) Through the Misrepresentations, the Directors wrongfully and negligently induced FrontFour wrongfully and negligently induced FrontFour to hold its position in Lightstream, rather than sell its secured notes on the open market.

(VI) Market Reaction to the Transaction Announcement

37. The trading price for the Unsecured Notes immediately and dramatically fell following the July 2 Press Release of the Transaction, causing damage to be suffered by FrontFour.

38. Bloomberg Business described Lightstream's actions as "dividing its lenders into winners and losers". As an Unsecured Noteholder not included in the Transaction, FrontFour would be such a "loser".

39. Bloomberg Business further stated that "Those left out of the private deal got knocked down the capital structure, saw their holdings plunge in trading to about half their original value, and then got downgraded by Moody's Investors Service".

40. Moody's Investors Service stated that they viewed the Unsecured Noteholders not party to the private Transaction "as losing and having a much lower recovery level than they would have had before."

41. FrontFour states, and the fact is that, but for the Company's surprise announcement of the Transaction in the July 2 Press Release, the market price of the Unsecured Notes would not have been so severely diminished.

42. FrontFour states, and the fact is that, had the Company properly notified affected Unsecured Noteholders of the Transaction, and provided an equal opportunity to all such Unsecured Noteholders to participate therein, the market would have absorbed that information and, while the market price of the Unsecured Notes may well have dropped, FrontFour would have:

    (a) been on an equal footing with the undisclosed parties that ultimately became party to the Transaction in circumstances where their rights under the Indenture were identical;

    (b) carefully considered and likely entered into the Transaction; and

    (c) alternatively, even if FrontFour had not became party to the Transaction, the resulting damage would not have been nearly as grave.

(VII) Lightstream's Oppression Caused FrontFour Damages

43. FrontFour advances this claim pursuant to Part 19 of the *Business Corporations Act*, R.S.A. 2000, c. B-9, as amended from time to time (the **ABCA**).

44. FrontFour is a "complainant" within the meaning of s. 239(b)(ii) of the ABCA.

45. The actions of Lightstream and its Directors in respect of the conduct of its business and affairs are oppressive, unfairly prejudicial to, and unfairly disregarded the interests of FrontFour as security holder and creditor.

46. As a result of these oppressive acts, Lightstream and its Directors ~~has~~ have caused serious harm and prejudice to FrontFour as well as to the rights and interests of FrontFour as a security holder and creditor of the Company.

47. FrontFour reasonably believed and relied upon the expectation that Lightstream and its Directors would act in accordance with the terms of the Unsecured Notes and the Indenture and not in a manner oppressive to FrontFour and its interests.

48. FrontFour is entitled to immediate relief from Lightstream and its Directors under the ABCA to remedy and redress past, present and ongoing oppression.

49. In particular but without limitation, FrontFour is entitled to immediate injunctive relief to restrain the Proposed Refinancing Transaction from proceeding in its current form. FrontFour therefore claims interim and final Orders restraining

Lightstream from taking further actions to advance the Transaction in its current form or at all.

50. Alternatively, FrontFour seeks an Order directing Lightstream to permit FrontFour to participate in the' Proposed Refinancing Transaction on the same basis as the undisclosed parties who are to be issued Secured Notes in the Transaction.

51. FrontFour seeks an Order requiring the payment of damages by Lightstream and its Directors to FrontFour to compensate the Plaintiff for the loss in value of its security interest in the Company resulting from the announcement of the Proposed Refinancing Transaction and in the amount of at least $4,524,375.00 (USD), or as may be proven at trial.

52. Particulars in this regard include that Lightstream and its Directors fundamentally harms the rights of FrontFour by:

(a) deliberatively and knowingly creating this private Transaction;

(b) depriving FrontFour the opportunity to participate in the Transaction;

(c) not providing any notice of the Transaction;

(d) proposing to complete the Transaction which confers benefits that are unavailable to other Unsecured Noteholders of the same class (such as FrontFour) principally by creating a separate and unequal class of debt ranking ahead of the Unsecured Notes;

(e) subordinating FrontFour's debt contrary to the terms of the Indenture;

(f) granting a lien as security to the Secured Notes when a lien has not been granted as security to the Unsecured Notes on the same basis, contrary to the terms of the Indenture;

(g) arbitrarily increasing the likelihood that, in an event of default, Lightstream's indebtedness to FrontFour will not be satisfied while the select undisclosed parties to the Transaction will have their debt secured;

(h) causing the market value of the Unsecured Notes to drop precipitously in direct response to the Transaction and July 2 Press Release (in FrontFour's case, resulting in loss in excess of $4,524,375.00 (USD)); and

(i) such further particulars as may be proven at the trial of this Action.

53. FrontFour made a formal written demand to Lightstream on July 6, 2015, to rectify these oppressive acts. Lightstream has failed to comply with this demand.

54.

(VIII) Lightstream Breached its Duty of Honest Contractual Performance

55. It is a term of the Indenture, express or implied, that the Parties shall conduct themselves at all times in good faith, and engage in fair and honest dealing.

56. In breach of the Indenture, Lightstream has failed to conduct itself in good faith and has failed to engage fairly and honestly with FrontFour in relation to its performance under the Indenture.

Remedy sought:

57. FrontFour proposes that this action be tried at Calgary.

58. FrontFour seeks the following relief on an interim, interlocutory, and final basis:

(a) a declaration pursuant to sections 239 and 242 of the ABCA that the business affairs of Lightstream and the powers of the board have been carried on, conducted or exercised in a manner that is oppressive or unfairly prejudicial to or that unfairly disregards the interests of FrontFour;

(b) an injunction Order restraining the Company from proceeding with the Proposed Refinancing Transaction on its current terms or at all;

(c) alternatively, an Order directing that Lightstream provide FrontFour an opportunity to participate in the Proposed Refinancing Transaction on the same basis as the undisclosed parties who are to be issued Secured Notes in the Transaction, and varying the Transaction to effect same;

(d) damages in the amount of $4,524,375.00 (USD) or such amount to be proven at trial;

(e) costs on a solicitor-client basis, or alternatively costs; and

(f) such further and other relief as counsel for the Plaintiff may advise and this Honourable Court may deem just.

Tab 9

Form 27

[Rules 6.3 and 10.52(1)]

Clerk's Stamp

COURT FILE NUMBER	1501-08782
COURT	Court of Queen's Bench of Alberta
JUDICIAL CENTRE	Calgary

CLERK OF THE COURT
FILED
AUG - 3 2016
JUDICIAL CENTRE
OF CALGARY

PLAINTIFF (APPLICANT)	MUDRICK CAPITAL MANAGEMENT, LP
DEFENDANT (RESPONDENT)	LIGHTSTREAM RESOURCES LTD.
DOCUMENT	**APPLICATION BY THE PLAINTIFF, MUDRICK CAPITAL MANAGEMENT, LP**

ADDRESS FOR SERVICE AND CONTACT INFORMATION OF PARTY FILING THIS DOCUMENT

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NOTICE TO RESPONDENT(S):
(Indicate name(s) and status of Respondent(s))

Lightstream Resources Ltd., defendant (respondent)

This Application is made against you. You are a Respondent.

You have the right to state your side of this matter before the Master/Judge.

You have the right to state your side of this matter before the Master/Judge.

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

Date:	August 30, 2016
Time:	10:00am
Where:	Calgary Courts Centre, 601 - 5 Street S.W. Calgary, AB T2P 5P7
Before Whom:	Justice Campbell

Go to the end of this document to see what else you can do and when you must do it.

Remedy claimed or sought:

1. An Order granting the plaintiff, Mudrick Capital Management LP ("**Mudrick**") leave to issue an Amended Statement of Defence in the form attached hereto as "Schedule A".

2. Such further and other relief as this Honourable Court deems just.

Grounds for making this Application:

3. The Plaintiff, Mudrick, is an SEC-registered investment advisor which manages capital for a diverse group of institutions and individuals.

4. The Defendant, Lightstream Resources Ltd. (**Lightstream** or the **Company**), is a light oil exploration and production corporation with its registered and records office in Calgary, Alberta. Until May 22, 2013, when the company was renamed, Lightstream operated as Petrobakken Energy Ltd. (**Petrobakken**).

5. This action was commenced by the plaintiffs by way of Statement of Claim filed October 5, 2015.

6. The plaintiffs commenced the action on the basis that Lightstream's conduct with respect to certain unsecured notes was oppressive pursuant to section 242 of the *Alberta Business Corporations Act*, RSA 2000, c B-9 and in breach of the indenture governing such notes.

7. Mudrick now seeks to amend the statement of claim to add the following individuals who, at all material times, were the directors of the Company: John D. Wright, Ian Brown, Martin Hislop, Kenneth R. McKinnon, Corey C. Ruttan, Craig Lothian and W. Brett Wilson.

8. Mudrick's representative, David Kirsch, has already been examined by Lightstream's counsel with respect to the misrepresentations at issue.

9. Neither the Company nor the Directors will suffer any non-compensable prejudice as a result of the amendments.

Material or evidence to be relied on:

10. Such further and other documentary evidence as counsel may advise and this Honourable Court may permit.

Applicable rules:

11. Rules 3.62, 3.63, 3.74, and 6.3 of the *Alberta Rules of Court*, Alta Reg 124/2010.

Applicable Acts and regulations:

12. Section 242 of the *Alberta Business Corporations Act*, RSA 2000, c B-9.

Any irregularity complained of or objection relied on:

13. None.

How the Application is proposed to be heard or considered:

14. The application is to be heard orally.

AFFIDAVIT EVIDENCE IS REQUIRED IF YOU WISH TO OBJECT.

WARNING

If you do not come to Court either in person or by your lawyer, the Court may give the applicant(s) what they want 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 time shown at the beginning of the form. If you intend to give evidence in response to the application, you must reply by filing an affidavit or other evidence with the Court and serving a copy of that affidavit or other evidence on the applicant(s) a reasonable time before the application is to be heard or considered.

Schedule "A"

COURT FILE NUMBER	1501-08782
COURT	Court of Queen's Bench of Alberta
JUDICIAL CENTRE	Calgary
PLAINTIFF	MUDRICK CAPITAL MANAGEMENT, LP
DEFENDANT	LIGHTSTREAM RESOURCES LTD., JOHN D. WRIGHT, IAN BROWN, MARTIN HISLOP, KENNETH R. MCKINNON, COREY C. RUTTAN, CRAIG LOTHIAN and W. BRETT WILSON
DOCUMENT	**AMENDED STATEMENT OF CLAIM**

Clerk's Stamp

ADDRESS FOR SERVICE AND CONTACT INFORMATION OF PARTY FILING THIS DOCUMENT

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NOTICE TO DEFENDANT(S)

You are being sued. You are a Defendant.

Go to the end of this document to see what you can do and when you must do it.

Note: State below only facts and not evidence (Rule 13.6)

Statement of facts relied on:

15. The Plaintiff brings this claim on the basis that the Respondent, Lightstream Resources Ltd. ("**Lightstream**" or the "**Company**"), as well as Lightstream's directors, at the material times, John D. Wright, Ian Brown, Martin Hislop, Kenneth R. McKinnon, Corey C. Ruttan, Craig Lothian and W. Brett Wilson, ~~has~~ have conducted ~~itself~~ themselves in a manner that is oppressive, unfairly prejudicial to, and unfairly disregards the interests of, the Applicant, Mudrick Capital Management, L.P. ("**Mudrick**") in violation of section 242 of the *Business Corporations Act*, Alberta, RSA 2000, c B-9 (the "**ABCA**");

16. At all material times, John D. Wright, Ian Brown, Martin Hislop, Kenneth R. McKinnon, Corey C. Ruttan, Craig Lothian and W. Brett Wilson were personally implicated in the oppressive conduct and are thus jointly and severally liable. Specifically, the Directors, jointly and severally, exercised their power in a fashion which caused Lightstream's business and affairs to be conducted in a way that unfairly disregarded Mudrick's interests and led to an unfairly prejudicial result.

The Parties and Basis for the Claim

17. Lightstream is a light oil-focused exploration and production company operating in Western Canada. Lightstream is publicly traded on the Toronto Stock Exchange ("**TSX**") and its corporate headquarters is located in Calgary, Alberta. In 2013 it changed its corporate name from PetroBakken Energy Ltd. ("**PetroBakken**") to Lightstream.

18. At all material times, the directors of Lightstream were John D. Wright, Ian Brown, Martin Hislop, Kenneth R. McKinnon, Corey C. Ruttan, Craig Lothian and W. Brett Wilson (the "**Directors**").

19. Mudrick is an SEC-registered investment advisor which manages capital for a diverse group of institutions and individuals. It is a complainant under section 239 of the ABCA.

20. In 2012, Lightstream issued $900 million of 8.625% Senior Notes due 2020 (the "**Unsecured Notes**") issued pursuant to an indenture dated January 30, 2012 by and among PetroBakken (now Lightstream) as Issuer, PetroBakken Capital Ltd and PBN Partnership as Guarantors, US Bank National Association as Trustee, and Computershare Trust Company of Canada as Canadian Trustee (the "**Indenture**"). The holders of those Unsecured Notes ranked equally in their positions as creditors of Lightstream.

21. As described below, Mudrick acquired approximately USD$32 million of Unsecured Notes issued pursuant to the Indenture for its clients between January and ~~April~~ May 2015. Mudrick currently holds USD$97 million of Unsecured Notes.

22. In July 2015, Lightstream announced a transaction whereby it agreed to exchange $465 million of the Unsecured Notes for $395 million of secured second lien notes (the "**Secured Notes**"), and issued a further $200 million of Secured Notes ("**the Secured Notes Transaction**" and "**Transaction**"). The Secured Notes Transaction was entered into with some (the "**Secured Transaction Parties**"), but not all, of the holders of the Unsecured Notes. Lightstream did not offer the Transaction to Mudrick, and refused to extend such offer when requested to do so.

23. The Secured Notes Transaction had the effect of promoting the Secured Transaction Parties into secured creditors, thereby placing them in a superior security position to the remaining holders of Unsecured Notes who were excluded from the Secured Notes Transaction, including Mudrick and its clients. It also adversely affected the market price of the remaining Unsecured Notes.

24. The Secured Notes Transaction by Lightstream is oppressive of and unfairly prejudicial to its interests, and unfairly disregards those interests.

Mudrick's Decision to Purchase Unsecured Notes from Lightstream

25. Mudrick reviewed the Indenture and understood that it provided a number of protections for holders of Unsecured Notes. Mudrick also contacted Lightstream on a number of occasions and Lightstream represented that it had adequate liquidity, was

cash flow positive and had no requirement or intention to restructure its debt which included the Unsecured Notes.

26. Mudrick's decision to acquire Unsecured Notes was based on the following factors:

(a) Lightstream appeared to have sufficient liquidity and continuing oil production to withstand any short to medium-term declines in oil prices without the need for additional capital or debt restructuring;

(b) Lightstream had a limited amount of debt ahead of the Unsecured Notes; and

(c) Mudrick viewed the value of Lightstream as being in excess of the market valuation of USD$1.1 billion.

27. Mudrick acquired the Unsecured Notes for its clients in several instalments as follows:

(a) On January 22, 2015, Mudrick acquired Unsecured Notes in two instalments:

(i) USD$10,000,000 Unsecured Notes; and

(ii) USD$4,500,000 Unsecured Notes;

(b) On January 29, 2015, Mudrick acquired Unsecured Notes in another two instalments:

(i) USD$5,000,000 Unsecured Notes; and

(ii) USD$10,000,000 Unsecured Notes.

(c) On April 1, 2015, Mudrick acquired USD$500,000 Unsecured Notes;

(d) On April 7, 2015, Mudrick acquired USD$1,000,000 Unsecured Notes; and

(e) On May 28, 2015, Mudrick acquired USD$1,200,000 Unsecured Notes.

Lightstream Enters Into The Secured Notes Transaction to the Exclusion of Mudrick and Other Unsecured Note Holders

28. In May 2015, rumours began circulating in the industry that Lightstream was receiving many proposals to restructure its debt and enter into private transactions which could involve the exchange of Unsecured Notes for Secured Notes.

29. Both in private communications with Mudrick and in Lightstream's public communications, the Company continued to represent that it was sufficiently liquid, with positive cash flows, and did not need to restructure its debt and had no requirement for any such transaction.

30. Lightstream's President and CEO, the Respondent John D. Wright ("Wright"), repeatedly made representations to this effect right up until the time of the Secured Notes Transaction.

31. As recently as a few weeks prior to the Secured Notes Transaction - in response to Mudrick specifically expressing concern that Apollo was pressuring Lightstream to exchange Apollo's bonds into bonds that were structurally senior to the existing senior unsecured notes - Wright represented that:

(a) Lightstream had a constructive relationship with Apollo;

(b) No transaction was being contemplated;

(c) Lightstream continued to have ample liquidity; and

(d) If Lightstream were to pursue a transaction along the lines of the Secured Notes Transaction, they would offer it to all bondholders.

32. The above-noted representations (collectively, the "Misrepresentations") all proved to be false. In fact, Lightstream was under significant pressure from Apollo and had already committed to the Secured Notes Transaction which was within weeks of being completed. Accordingly, the Misrepresentations were made falsely, recklessly and/or negligently.

33. The Misrepresentations were made outside the scope of Wright's responsibilities as an officer and director of Lightstream. Nevertheless, the Misrepresentations were made with the full knowledge and agreement of the Directors, or at their direction, as they were directed at inducing Mudrick, and other senior unsecured bondholders, to maintain their positions in Lightstream.

34. The Directors were well aware that any precipitous move by Mudrick, or any other senior unsecured bondholders, would jeopardize the Secured Notes Transaction and, with it, the opportunity to entrench themselves as directors and their interests in management.

35. Notwithstanding the Misrepresentations, on July 2, 2015, Lightstream announced the Secured Notes Transaction.

36. Lightstream did not disclose and has not disclosed the identities of the Secured Transaction Parties. Various media outlets have since speculated that Apollo Global Management LLC and GSO, two of Lightstream's largest holders of Unsecured Notes, participated in the Secured Notes Transaction.

37. The Secured Notes Transaction was only offered to the Secured Transaction Parties, to the exclusion of other holders of the remaining $335 million of the Unsecured Notes, including Mudrick, despite Mudrick's repeated requests to participate in the Secured Transaction. Mudrick is not aware of any other holders of Unsecured Notes, aside from the Secured Transaction Parties, being made aware of the Secured Notes Transaction prior to the July 2, 2015 announcement.

38. Throughout the time when Mudrick first acquired Unsecured Notes in January of 2015, up to and including the present, there was ample opportunity for Lightstream to present the Secured Notes Transaction to Mudrick especially given that Mudrick repeatedly communicated its desire to be part of any debt restructuring that Lightstream might consider.

39. Furthermore, when the rumours of a restructuring emerged, Mudrick had considered the possibility of selling off its position in the Unsecured Notes so as not to be left holding Unsecured Notes in the event of an exchange or other transaction which might negatively impact them. Based on assurances received from Lightstream, both privately and publicly, Mudrick decided not to sell its Unsecured Notes.

40. In addition to its discussions with Lightstream, Mudrick also spoke to a representative of RBC Capital Markets, LLC ("**RBC**"), Lightstream's financial advisor in connection with the Secured Notes Transaction. Mudrick made its desire to participate in the Transaction clear. Mudrick was told that the Transaction would not be offered to the remaining holders of Unsecured Notes, but that Lightstream was considering an additional transaction on terms significantly less favourable than those that had been offered to, and accepted by, the Secured Transaction Parties. Mudrick was further told to provide the lowest price it would be willing to accept for an exchange and Lightstream would consider the offer.

41. Mudrick explained that it would not accept terms less favourable than those offered to the Secured Transaction Parties and again reiterated its desire to participate in the Transaction.

The Transaction Was Oppressive, Unfairly Prejudicial To and Unfairly Disregarded the Interests of the Applicant

42. The conduct of Lightstream and its Directors ~~conduct~~ was oppressive, unfairly prejudicial to, and unfairly disregarded the interests of the Applicant for the following reasons:

(a) The Secured Notes Transaction unfairly discriminated among holders of Unsecured Notes notwithstanding that all of the holders had purchased the exact same type of debt from Lightstream as governed by the Indenture;

(b) The Secured Notes Transaction was unnecessary. In Lightstream's private communications with Mudrick, as well as its public filings, and public communications, it indicated that it had sufficient liquidity and did not need to – or plan to – add additional liquidity or restructure its debt;

(i) Further, even if Lightstream believed that the Transaction would be beneficial, it was still obligated to treat all of its Unsecured Note holders equitably. Offering the Transaction only to some of the Unsecured Note holders was opportunistic, prejudicial, and unfairly discriminated within the class of holders of Unsecured Notes;

(ii) The Transaction significantly increased the amount of secured debt ahead of the remaining Unsecured Notes and caused the Unsecured Notes to decrease in value. If the transaction had been offered to all holders of Unsecured Notes, all of the holders – including the Secured Transaction Parties – would have participated and exchanged Unsecured Notes for Secured Notes because not doing so would have left any remaining holder of Unsecured Notes in a significantly worse position. The current trading price of the remaining Unsecured Notes confirms how the Secured Notes Transaction has left the excluded holders of the Unsecured Notes in a much worse position.

(c) The Secured Notes Transaction did not comply with the terms of the Indenture;

(d) Lightstream, through its Directors, repeatedly assured Mudrick that it was not contemplating a transaction similar to the Secured Notes Transaction,

and that if it did, it would make any such transaction available to all holders of the Unsecured Notes; and

(e) Lightstream repeatedly declined Mudrick's request to participate in the Secured Notes Transaction and indicated that it would not be making the Transaction available to the remaining holders of Unsecured Notes.

(f) Through the Misrepresentations, the Directors wrongfully and negligently induced Mudrick to hold its position in Lightstream, rather than sell its secured notes on the open market.

43. As a result of the Secured Notes Transaction, the Unsecured Notes have substantially decreased in value and are subordinated to the Secured Notes issued pursuant to the Transaction. Specifically:

(a) The market price for the Unsecured Notes peaked at $0.7900 on the dollar in the middle of May. As rumours began circulating that Lightstream was contemplating an exchange, the Unsecured Notes dropped to $0.6400 on the dollar. Immediately following the announcement of the Transaction, the notes further dropped to $0.5000 on the dollar and, at present, the Unsecured Notes are being offered at $0.4400 on the dollar, well below the value of the Unsecured Notes at the times Mudrick had made its acquisitions between January 21 2015 and May 28 2015; and

(b) Prior to the Transaction, the Company had CDN$638 million in debt senior to the Unsecured Notes. After the Transaction, the amount of debt ahead of the Unsecured Notes increased by CDN$480 million such that there is now CDN$1.121 billion in debt senior to the Unsecured Notes.

Remedy sought:

44. The Applicant seeks the following:

(a) an Order pursuant to section 242 of the ABCA, declaring that the Secured Notes Transaction was oppressive, unfairly prejudicial, and unfairly disregarded the interests of the Applicant;

(b) Appropriate remedial orders pursuant to section 242, specifically:

(i) that the Secured Notes Transaction be set aside;

(ii) alternatively, that Lightstream be required to offer the Transaction to Mudrick and its clients on the same terms and conditions as offered to the Secured Transaction Parties;

(iii) alternatively, that Lightstream be required to redeem the Unsecured Notes of Mudrick's clients for the "make-whole" price specified in the Indenture;

(iv) further, or in the alternative, that Lightstream compensate Mudrick and its clients for its losses as a consequence of the Secured Notes Transaction;

(v) the reasonable and proper costs of this application on full indemnity basis or double or triple costs basis, as appropriate; and

(vi) such other order as may be appropriate under section 242 and be just in the circumstances.

NOTICE TO THE DEFENDANT(S)

You only have a short time to do something to defend yourself against this Claim:

20 days if you are served in Alberta
1 month if you are served outside Alberta but in Canada
2 months if you are served outside Canada.

You can respond by filing a Statement of Defence or a Demand for Notice in the office of the clerk of the Court of Queen's Bench at Calgary, Alberta, AND serving your Statement of Defence or a Demand for Notice on the Plaintiff's(s') address for service.

WARNING

If you do not file and serve a Statement of Defence or a Demand for Notice within your time period, you risk losing the law suit automatically. If you do not file, or do not serve, or are late in doing either of these things, a Court may give a judgment to the Plaintiff(s) against you.