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COURT FILE NO.	2401-09247
COURT	COURT OF KING'S BENCH OF ALBERTA
JUDICIAL CENTRE	CALGARY
PROCEEDINGS	**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 LONG RUN EXPLORATION LTD. AND CALGARY SINOENERGY INVESTMENT CORP.**
DOCUMENT	**BRIEF OF LAW**
ADDRESS FOR SERVICE AND CONTACT INFORMATION OF PARTY FILING THIS DOCUMENTS	Field Law LLP 400, 444 – 7 Ave SW Calgary, AB T2P 0X8 Attention: Trevor Batty Phone: (403) 260-8500 Fax: (403) 264-7084 File No. 81749-2

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BRIEF OF LAW OF HENENGHAIXIN CORP.

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INTRODUCTION

1. The following are written submissions of Henenghaixin Corp. (**"H Corp"**) regarding the pending application by FTI Consulting Canada Inc. ("**FTI or the Monitor**"), the court-appointed Monitor (with enhanced powers) of Long Run Exploration Ltd ("**Long Run**") and Sinoenergy Investment Corp ("**Calgary Sinoenergy**") (Long Run and Calgary Sinoenergy collectively, (**"CCAA Debtors**").

2. The Monitor is applying for a Transaction Approval and Reverse Vesting Order ("**RVO**") approving an Amended and Restated Stalking Horse Subscription Agreement (the "**A&R Subscription Agreement**") between the CCAA Debtors and 2657493 Alberta Ltd. (the "**Purchaser**")[1].

3. H Corp opposes the relief sought by the Monitor, not because this is an inappropriate circumstance for using and RVO to complete the restructuring but rather that the form of A&R Subscription Agreement and the RVO proposed by the Monitor is inappropriate. H Corp's position is that this Court should not approve the proposed transaction in its current form as doing so will unjustly and unfairly prejudice H Corp in a manner that is contrary to established insolvency jurisprudence surrounding the issuance of reverse vesting orders and vesting orders generally.

4. Specifically, H Corp states that the A&R Subscription Agreement and the RVO are objectionable for the following reasons:

   (a) They transfer and effectively extinguish H Corp's contingent proprietary trust claims against the CCAA Debtors without an adjudication of H Corp's claims in violation of H Corp's rights to natural justice and due process;

   (b) At the same time as they extinguish H Corp's claims, they expressly preserve the CCAA Debtors related claims against H Corp's affiliated companies;

   (c) The RVO provides an overly broad release that arguably extinguishes H Corp's claims against former directors, officers and contractors of the CCAA Debtors who had no involvement with the CCAA proceedings of the CCAA Debtors and for which there is no justification for such a release; and

[1] Monitor's Fifth Report, dated October 30, 2024 (the "**Fifth Report**"), Appendix "B" (the "**A&R Subscription Agreement**")

(d) The A&R Subscription Agreement and RVO violate s. 19(c) and (d) of the CCAA by compromising and extinguishing H Corp's claims against the CCAA Debtors arising out of fraud, embezzlement, misappropriation or defalcation while acting in a fiduciary capacity and/or resulting from obtaining property by false pretences or fraudulent misrepresentation.

FACTS

5. H Corp relies upon the facts set out in the Affidavit of Gaoyong Zhang, affirmed September 13, 2024 (the "**Zhang Affidavit**"). Mr. Zhang is the President of H Corp.

6. H Corp also relies upon the facts set out in the Monitor's Reports filed in the within CCAA proceedings as well as the Affidavit of Ziqing (Eddie) Zou, affirmed on July 2, 2024 (the "**Zou Affidavit**").

Background

7. In 2019, two limited partnerships formed under the laws of the People's Republic of China, Jiang Yin Henenghaixin Investment Partnership and Wuhan Changxin Hesheng Industrial Investment Fund Partnership transferred funds equivalent to CAD $352.2 million (the "**Investment Funds**") to H Corp for the specific purpose of H Corp, through its wholly owned subsidiary West Lake Energy Corp. ("**West Lake**") purchasing certain oil and gas assets out of the receivership of Twin Butte Energy Ltd. (the "**Assets**").[2]

8. The purchase price for the Assets was $266MM, plus GST and subject to adjustments. An additional $80MM of the funds advance to H Corp was intended as working capital to operate and develop the Assets.[3]

9. Following investigations conducted in late 2018 and early 2019, representatives of Jiang Yin LP and Wuhan LP discovered that only $42 million of the Investment Funds were transferred to West Lake for working capital purposes and that $43,765,669 of the Investment Funds were diverted to the CCAA Debtors and used for other purposes (the "**Diverted Funds**"). [4]

[2] Zhang Affidavit at paras. 10-12 and 15-16.
[3] Zhang Affidavit at paras. 13 and 20.
[4] Zhang Affidavit at paras. 21-32.

The H Corp Action

10. On February 28, 2020, H Corp initiated legal action against the CCAA Debtors and various individuals by issuing a Statement of Claim in Court of King's Bench of Alberta Action No. 2001-03353 (the "**H Corp Action**")[5] wherein H Corp pleaded, *inter alia*, the following causes of action against the CCAA Debtors and the individual defendants, Tianzhou Deng ("**Deng**"), Xiaobo Den aka Lake Deng ("**Lake**"), who is Deng's daughter, and Michael Lam ("**Lam**", collectively with Deng and Lake, the "**Individual Defendants**"):

    (a) Misappropriation and diversion of funds from H Corp;

    (b) Breach of Director's fiduciary duties;

    (c) Knowing assistance and receipt;

    (d) Misrepresentation;

    (e) Unjust enrichment; and

    (f) Fraudulent conversion, conspiracy and fraudulent conveyances.

    (collectively, the "**H Corp Claims**")

11. In the H Corp Action, H Corp also claimed the following remedies, among others, as against one or more of the defendants (collectively, the "**H Corp Remedies**") in an effort to recover the Diverted Funds:

    (a) Judgment in the amount of $44 million, or such other amount as may be proven at trial;

    (b) Tracing, accounting, freezing and disgorgement of the Diverted Funds; and

    (c) A declaration that the Diverted Funds and any traceable assets resulting from the Diverted Funds are held in trust for the benefit of H Corp.

12. The CCAA Debtors filed a Statement of Defence in the H Corp Action denying the H Corp Claims and also filed a Third Party Claim[6] in the H Corp Action (the "**Third Party Claim**") against numerous Third Party Defendants, including H Corp's sole shareholder, York City Enterprises Limited ("**York City**"), York City's sole shareholder, Qingdao Zhongtian Yuhen Energy Co. Ltd. ("**Qingdao Yuhen**"),

[5] Zhang Affidavit, Exhibit 1
[6] Zhang Affidavit, Exhibit "20" (the "**Third Party Claim**")

and H Corp's wholly owned subsidiary, West Lake Energy Corp. ("**West Lake**", together with York City and Qingdao Yuhen, the "**H Corp Related Parties**"), the Individual Defendants and various other related entities and individuals.

13. The thrust of the CCAA Debtors' allegations in the Third Party Claim is that the Individual Defendants, while acting as directors and officers of the CCAA Debtors, improperly transferred funds to, among other Third Party Defendants, the H Corp Related Parties. Specifically, the CCAA Debtors allege that a total of $67MM was improperly transferred from the CCAA Debtors to either H Corp or the H Corp Related Parties and further claim both damages and set off against any amounts found to be owing to H Corp in the H Corp Action. [7]

14. In the time since H Corp filed its Statement of Claim it has proceeded with the H Corp Action in as expeditious a manner as possible, including obtaining an *ex parte* Attachment Order on April 23, 2020 (the "**Attachment Order**") against the CCAA Debtors and the Individual Defendants (later set-aside as against the CCAA Debtors on a re-hearing by Romaine J.[8] and as against the Individual Defendant reversed on appeal[9]). On April 23, 2020, H Corp registered the Attachment Order against each of the CCAA Debtors at the Alberta Personal Property Registry.[10]

15. Further interlocutory applications and discovery matters followed, including most recently H Corp's counsel questioning a representative of the CCAA Debtors on their Affidavits of Records and the CCAA Debtors granting of numerous undertakings associated therewith. The CCAA Debtors undertakings were provided on August 21, 2023 and remained outstanding at the time of the filing of the granting of the Initial Order in respect of the CCAA Debtors on July 4, 2024 (the "**Initial Order**").[11]

16. The initial Order had the effect of staying the H. Corp Action for an initial period of thirty (30) days and that stay has been extended several times since with the latest extension to December 31, 2024. On July 11, 2024, H Corp's counsel asked the Monitor whether it would consent to a lifting

[7] Third Party Claim at paras. 40-45
[8] Zhang Affidavit at Exhibit "24", Reasons for Decision of the Honourable Madam Justice B.E. Romaine of March 3, 2021.
[9] Zhang Affidavit at Exhibit "25", *Henenghaixin Corp v. Deng*, 2022 ABCA 271
[10] Zou Affidavit, Exhibit "N "at pages 21-22 and Exhibit "O" at pages 4-5.
[11] Zhang Affidavit at paras. 52-71.

of the stay of proceedings to allow the H Corp Action to proceed.[12] The Monitor denied H Corp's request and as a result no further steps have occurred in the H Corp Action.

The CCAA Proceedings, the SISP and the Stalking Horse Subscription Agreement

17. The CCAA proceedings of the CCAA Debtors were not initiated by the CCAA Debtors but were instead initiated by the China Construction Bank Toronto Branch, in its capacity as collateral agent for the China Construction Bank Qingdao Branch (the "**Secured Lender"**). Additionally, at the time the Initial Order was granted, the Monitor was given enhanced powers under the Initial Order to exercise control over the CCAA Debtors and their property. It is clear from these circumstances that this CCAA proceeding is creditor-driven as opposed to debtor-driven.

18. The Secured Lender's evidence is that Long Run's indebtedness to the Secured Lender as of June 28, 2024, was $243,606,593, plus interest and penalties from that date.[13]

19. On July 30, 2024, the Monitor brought an application for, among other relief, the Court's approval of a stalking horse sale and investment solicitation process for the property of the CCAA Debtors (the "**SISP**"), along with approval of the terms of a Stalking Horse Subscription Agreement between Long Run and Hiking Group Shandong Jinyue Int't Trading Corporation (the "**Stalking Horse Bidder**"), including the form of RVO attached thereto (the "**Stalking Horse Subscription Agreement**").[14]

20. The Monitor's July 30, 2024 Application also sought the Court's approval of interim financing in the sum of $7 million (the "**DIP Facility**") to address the cash flow shortages of the CCAA Debtors. The lender under the DIP Facility (the "**DIP Lender**") is Hiking Group Shandong Jinyue Int't Trading Corporation, which is the same entity that was the Stalking Horse Bidder.

21. The SISP, Stalking Horse Subscription Agreement and RVO are described and attached to the Monitor's Second Report.[15] The relevant portions are as follows:

[12] Third Report of the Monitor, dated September 5, 2024 (the "**Third Report**"), at para. 21.
[13] Affidavit of Ziqing (Eddie) Zou, affirmed on July 2, 2024 at para. 44.
[14] Application of the Monitor, filed July 24, 2024.
[15] Second Report of the Monitor, dated July 23, 2024 (the "**Second Report**").

(a) The SISP is to commence August 1, 2024 with the successful transaction to close by October 31, 2024;

(b) The Monitor is to choose the "Successful Bid" by comparing all "Superior Bids" obtained through the SISP to the Stalking Horse Bid;

(c) The Purchase Price in the Stalking Horse Subscription Agreement consists of:

(i) A cash component totaling $22.1 million, of which $22 million is earmarked for payment of "Priority Payables" and $100,000 for the "Estimated Trustee Fee Amount" to compensate FTI for its administration of a Creditor Trust; and

(ii) A credit bid component, whereby the Stalking Horse Bidder/DIP Lender sets off all of the indebtedness under the DIP Facility;

with the result being that the aggregate value of the Stalking Horse bid is $29.1MM.[16]

(d) The "Priority Payables" are defined as "any current of future amount owing as secured by any charges, liens or interest that rank in priority to the Lenders Secured Debt"[17] and includes the Court-ordered charges granted in the CCAA proceedings, carbon emissions payments, property taxes and GST accrued after the CCAA filing[18]. The H Corp Claims are not included under the definition of Priority Payables.

(e) The Stalking Horse Subscription Agreement is condition upon the RVO being approved by the Court[19]

(f) The RVO directs that certain assets (the "**Retained Assets**") and liabilities ("**Retained Liabilities**") remain with Long Run while other assets (the "**Transferred Assets**") and liabilities (the "**Transferred Liabilities**") are transferred to a "Creditor Trust" known as the "Long Run Exploration Residual Trust"[20];

(g) The purpose of the Creditor Trust is for FTI, as Trustee, to distribute the Settlement Funds (being the $100,000 Estimated Trustee Fee Amount that is earmarked for payment of the FTI's fees) and the Transferred Assets to the "Creditor Trust Beneficiaries" (being the creditors of Long Run)[21]; and

[16] Stalking Horse Subscription Agreement, Appendix "B" to the Second Report at Article 2.2
[17] Stalking Horse Subscription Agreement, Appendix "B" to the Second Report, at Article 1.1(qqq).
[18] Stalking Horse Subscription Agreement, Appendix "B" to the Second Report, at Schedule "C".
[19] Stalking Horse Subscription Agreement, Appendix "B" to the Second Report, at Article 4.3(b).
[20] RVO, paras. 9 and 17.
[21] Creditor Trust Settlement, Schedule "B" to RVO.

(h) Long Run and the Retained Assets are forever released and discharged from all claims, including the Transferred Liabilities and the Transferred Liabilities only have recourse to the Transferred Assets with the same rights and priorities as prior to the transfer to the Creditor Trust.

22. The Stalking Horse Subscription Agreement was subsequently amended and restated and assigned from the Stalking Horse Bidder to the Purchaser. The cash component in the current A&R Subscription Agreement was reduced from $22.1 million to $17.6 million but otherwise contains substantially the same form of transaction as the original Stalking Horse Subscription Agreement apart from certain changes for tax planning purposes.[22] It's detrimental impact on H Corp remains the same.

23. If the Court grants the RVO approving the A&R Subscription Agreement the end result is that the H Corp Claims are transferred to the Creditor Trust and if the H Corp Claims are proven H Corp will only have recourse to the Settlement Funds, which are comprised of the Estimated Trustee Fee Amount (which is only $100,000 and likely to be consumed by FTI's fees) and the Transferred Assets (which are comprised of the "Transferred Contracts" and any assets that the Purchaser determines it does not want prior to closing)[23]. Based upon this it appears that the recovery by H Corp and all other creditors with Transferred Liabilities will be negligible.

24. Based on the treatment of the H Corp Claims under the proposed Stalking Horse Subscription Agreement, H Corp's counsel appeared at the July 30, 2024 Application and opposed the Monitor's request that the Court pre-approve the Stalking Horse Subscription Agreement and the related RVO. H Corp's counsel submitted that the H Corp Action contains claims in fraud and constructive trust against the CCAA Debtors in the amount of $44 million that if proven could rank ahead of the claims of secured creditors, including the Secured Lender.[24]

25. The Honourable Justice Little heard the Application and granted the Second Amended and Restated Initial Order (the "**SARIO**") on July 30, 2024. Justice Little declined to make a ruling on whether the H Corp Action and H Corp Claims should be designated as Transferred Liabilities or Retained Liabilities and instead made it clear that he was reserving H Corp's rights to proceed with

[22]Fifth Report at para. 34.
[23] Stalking Horse Subscription Agreement, Appendix "B" to the Second Report, at Schedule "B".
[24] Third Report at para. 23.

its argument at a subsequent motion if the Stalking Horse Bidder is the Successful Bidder pursuant to the SISP.[25]

ISSUES

26. The only issue for this Court is to determine is whether it is appropriate to approve the A&R Subscription Agreement and RVO in their current forms given that:

(a) the effect of the resulting transaction is to compromise and extinguish the H Corp Claims, which include a contingent proprietary constructive trust claim against the assets of the Debtors that may rank in priority to the Secured Lender's security;

(b) there is a reasonable alternative to the proposed transaction that would allow the full and final adjudication of the H Corp Action and determine the extent of H Corp's proprietary interests the CCAA Debtors' assets;

(c) the proposed transaction extinguishes the H Corp Claim while expressly preserving the Third Party Claim;

(d) The RVO contains an overly broad release clause that arguably could be relied upon by the Individual Defendants in the H Corp Action; and

(e) The A&R Subscription Agreement's treatment of the H Corp Claim is contrary to s. 19(c) and (d) of the CCAA.

LAW AND ARGUMENT

Nature of an Unjust Enrichment Claim and Constructive Trust Remedy

27. As mentioned above, in the H Corp Action, H Corp is seeking a declaration that certain of the assets of the CCAA Debtors are impressed with a constructive trust for the benefit of H Corp.

28. The remedy of a constructive trust is imposed at the court's discretion where "good conscience" requires, including as a remedy for such wrongful acts as fraud, breach of duty of loyalty, and unjust enrichment and corresponding deprivation.[26]

[25] SARIO at para. 51
[26] *Moore v. Sweet* [2018] 3 S.C.R. 303 at para. 32

29. In the H Corp Action, H Corp has expressly pleaded that the CCAA Debtors and other Defendants' actions in handling the Diverted Funds constituted misappropriation, fraudulent conveyances, breach of duty and unjust enrichment. Establishing unjust enrichment requires meeting a well-known three-part test:

(a) The facts must show that the defendant has been enriched;

(b) There must be a corresponding deprivation to the Plaintiff(s);

(c) And an absence of any juristic reason for the enrichment.[27]

30. At the third step, to determine whether or not there is a juristic reason for the enrichment and corresponding deprivation, there is a two-pronged test:

(a) The plaintiff must show that the circumstances are not within any of the established categories for denial of recovery. These categories include existence of a contract, disposition of law, donative intent, or another common law or equitable obligation.

(b) The defendant has the opportunity to rebut the *prima facie* claim by demonstrating a reason to deny recovery.[28]

31. At the second stage of the analysis, the Court will consider the reasonable expectations of the parties and public policy arguments.[29] The above requirements are applicable to both commercial and domestic relationships.[30]

32. Remedies for unjust enrichment are restitutionary in nature. The object of the remedy is to require the defendant to repay or reverse the unjustified enrichment. Unjust enrichment may attract either a "personal restitutionary award" or a "restitutionary proprietary award". In other words, the plaintiff may be entitled to a monetary or a proprietary remedy.[31]

33. Courts have found that in some cases, when a monetary award is inappropriate or insufficient, a proprietary remedy may be required. Constructive trusts are broad and flexible equitable remedies. In *Kerr,* the Court noted that:

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[27] *Kerr v. Baranow*, 2011 SCC 10, para. 36.
[28] *Garland v Consumer GasCo.* 2004 SCC 25.
[29] *Ibid.*
[30] *Atlas Cabinets & Furniture v National Trust Co.,* [1990] 38 C.L.R. 106 (BCCA).
[31] *Lac Minerals Ltd. v International Corona Resources Ltd*., [1989] 2 S.C.R. 574.

> Where the claimant can demonstrate a link or causal connection between his or her contributions and the acquisition, preservation, maintenance or improvement of the disputed property, a share of the property proportionate to the unjust enrichment can be impressed with a constructive trust in his or her favour.[32]

34. A "sufficiently substantial and direct" link is required between the contribution and the trust property. Indirect contributions of money and direct contributions of labour may suffice, provided that a connection is established between the plaintiff's deprivation and the acquisition, preservation, maintenance, or improvement of the property.[33]

35. In addition to being a remedy for unjust enrichment, courts have also imposed constructive trusts in the absence of unjust enrichment on a broader basis in order to condemn wrongful acts and maintain the integrity of relationships of trust.[34]

H Corp has a prima facie case for unjust enrichment and a proprietary constructive trust claim against the assets of the CCAA Debtors

36. In the Zhang Affidavit, H Corp has provided sworn evidence of the circumstances surrounding the transfers of the Diverted Funds and the central roles that each of the CCAA Debtors played in the misappropriation of the Diverted Funds. This evidence includes Mr. Zhang's recounting of the deliberate production of false bank and financial statements, fraudulent transfers of funds that were verified by a forensic report prepared by PricewaterhouseCoopersLLC, and documentary evidence from Sinoenergy itself admitting the diversion of funds from H Corp to Sinoenergy and ultimately to Long Run.[35]

37. In her written decision in the H Corp Action dated March 3, 2021, Justice B. E. Romaine found that H Corp had produced sufficient evidence to prove a strong *prima facie* case as follows:

> **A strong *prima facie* case**
>
> In early 2018, the two Chinese investor parties became concerned that Mr. Deng would not be able to fund the acquisition of their equity interests and sent Mr. Zhang and two other representatives to Calgary in investigate West Lake's operation.
>
> At a meeting in Calgary in October 2018 with Ms. Deng and Mr. Lam, these representatives were shown West Lake Financial Statement for the period ended

[32] *Kerr* and *Pettkus*.
[33] *Kerr at p 51 citing Sorochan* and *Pettkus*.
[34] *Toronto-Dominion Bank v. Preston Springs Gardens Inc.*, 2004 CanLII 10168 (ON SC) at para 14
[35] Zhang Affidavit at paras. 22-48 and Exhibits "11" and "12"

December 31st, 2017 purporting to be audited that indicated that the share capital portion of shareholders' equity in West Lake was approximately $345,000,000, and that cash was about $31.4 million. Total current assets were approximately $61,000,000 and non-current assets were approximately $546,000,000. They were also shown bank statements indicating that West Lake had received about $80,000,000 from H Corp.

The Defendants submit that there is insufficient evidence to establish that the financial statements and bank records given to the representatives of Chinese investors in October, 2018 are false, but Mr. Lam confirmed the accuracy of the audited financial statements and bank records obtained later in January 2019, this indirectly confirming that the documents are false.

Mr. Lam submits that there is no expert evidence that establishes that the financial statements initially produced by Mr. Deng's team and Mr. Lam were false. However, given that the audited financial statements of West Lake were later produced and verified as accurate by the directors of West Lake and Mr. Lam, it is apparent on their fact that the previously produced statements are false and misleading. It is no answer to submit, as Mr. Lam does, that they were signed by two directors of West Lake. They may appear to be signed by these directors, but there is no evidence that these signatures are real.

On at least one occasion, money was subsequently transferred by Calgary Sinoenergy to Long run. The statements also revealed some subsequent transfers of funds from Calgary Sinoenergy to H Corp, but overall much more money flowed the other way.

Mr. Lam indicated in an affidavit sworn in September, 2020 that the purpose of the transfer was in part to pay back the deposit and to allow Calgary Sinoenergy and Long Run to become sufficiently profitable such that they could contribute, along with Mr. Deng and others, to the buyback guarantee set out in the investment agreement with the Chinese investors.

This does not, as submitted by the Defendants, provide a valid business purpose for the funds claimed by H Corp to have been misappropriated, but only evidence of a motive that benefits Mr. Deng with respect to his buyback obligation.

There is nothing in Mr. Lam's evidence that negates the strong *prima facie* case against Mr. Lam.

I found from evidence before me at the time of the ex-parte application that approximately $44,000,000 remained unaccounted for. H Corp submitted that these funds were diverted without knowledge, approval or authorization and for the purpose other tan the acquisition of Twin Butte assets and the necessary capitalization of West Lake.

The unrelated entities (i.e. including CCAA Debtors) all share common directors, Mr. Deng and Yong sheng Wu (phonetic) (i.e. Yingchun Wu). The documentation indicates that Calgary Sinoenergy received net $76,956,491 from H Corp, Long Run received net $150,000 from H Corp and $11.5 million of H Corp funds from Calgary Sinoenergy. Long Run paid $1,462,292 into H Corp for its benefit.

> It was on this basis that I found that H Corp had established a strong *prima facie* case.36

38. With respect to the evidence provided by Lam to justify the transfer of the Diverted Funds from H Corp to CCAA Debtors, namely a purported Shareholder Declaration of H Corp and a purported York City Loan Agreement between York City and Calgary Sinoenergy, Justice B. E. Romaine found that:

> The declaration is described as relating to an agreement dated April 10, 2017 with respect to a loan in the amount of $58.76 million to Calgary Sinoenergy (described as the "Abrogated Actions"), and states that it relieves all of the directors of H Corp of their duties and liabilities to the fullest extent permitted by the ABCA as it relates to the Abrogated Actions.
>
> The declaration restricts the powers of the directors of H Corp "to the fullest extent permitted by the act and by law as it relates to the Abrogated Actions", and gives such power to York City "as it relates to the Abrogated Actions". The declaration purports to approve the execution of the loan agreement by York City.
>
> The loan agreement, which is attached to the declaration, is between Calgary Sinoenergy and York City. The loan is unsecured and bears interest at prime plus 100 bps. It is stated to be repayable on the "Termination Date", which appears to be undefined.
>
> According to Mr. Lam, the Changchun Sionoenergy press release states that over $93 million was transferred from H Corp to Calgary Sinoenergy, despite H Corp not being the lender under the loan agreement, and $92.150 million of that was transferred to Long Run.
>
> The amount of the transfers to Calgary Sinoenergy from H Corp are well in excess of the $58,760,000 loan facility in the purported loan agreement. Although the purported loan agreement states the amount can be increased by York City, there is no evidence that York City ever did so.
>
> As noted, H Corp and the investors deny knowledge of the documents. There is a matter for trial.
>
> However, given that the transfer of funds from H Corp to Calgary Sinoenergy exceed the amount authorized by the loan agreement and given the issues relating to the declaration and loan agreement as described herein, the existence of these documents is not sufficient to negate the prima facie case that was established by H Corp at the *ex parte* application and that continues to be established in this application.[37]

39. No decision of the Court in the H Corp Action has ever challenged or overruled the evidence of a strong *prima facie* case that Justice Romaine declared in her decision of March 3, 2021.

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[36] Zhang Affidavit at Exhibit "24", Reasons for Decision of the Honourable Madam Justice B.E. Romaine of March 3, 2021, paras. 12(5), 12(6), 14, 16, 19-21, 23, 33-35.

[37] Zhang Affidavit at Exhibit "24", Reasons for Decision of the Honourable Madam Justice B.E. Romaine of March 3, 2021, paras. 39, 40, 42, 47, 55, 56

40. As a result, the Diverted Funds are a clear case where the CCAA Debtors were enriched at the expense of H Corp and there is no juristic reason for that enrichment. The individual defendants in the H Corp Action caused the unauthorized transfer of the Diverted Funds to the CCAA Debtors and none of the Defendants in the H Corp Action have produced any valid agreements or other documents justifying these impugned transfers.[38]

41. Further, one of the Individual Defendants in the H Corp Action (Deng) was a director of H Corp at the time of the impugned transfers of the Diverted Funds and breached his fiduciary duties to H Corp by participating in the transfers. The transfers of the Diverted Funds constituted a fraud on H Corp and a constructive trust is justified in these circumstances to condemn the wrongful acts committed by the Defendants in the H Corp Action.

42. H Corp has proceeded with the H Corp Action in an expeditious fashion both to prove the improper transfers of the Diverted Funds, the unjust enrichment that resulted from the transfer of the Diverted Funds and the traceability of the Diverted Funds. In this regard, H Corp brought an application pursuant to Alberta Rules of Court Rule 7.1 for the trial of an issue to prove the aforementioned falsification of documents by the CCAA Debtors. The Judge hearing the Rule 7.1 application ultimately determined that this issue ought to be resolved in a full trial alongside the other issues raised.[39]

43. H Corp has also attempted to trace the Diverted Funds into the current assets of Long Run through the discovery process in the H Corp Action. However, H Corp's efforts have been thwarted by the CCAA Debtors failure in the first instance to provide a fulsome Affidavit of Records in accordance with their obligations under the Rules of Court and further failure to comply with undertakings given during questioning on their Supplementary Affidavits of Records. The H Corp Action and H Corp's efforts to obtain further information regarding the use and ultimate disposition of the Diverted Funds were then stayed by the Initial Order granted in the CCAA Proceedings.

[38] Zhang Affidavit at para. 36.
[39] Zhang Affidavit at paras. 59-62

The Court should grant H Corp a constructive trust claim notwithstanding the security interest of the Secured Lender

44. In an insolvency proceeding, the Court must take into consideration the position of other creditors when determining whether to impose a constructive trust:

> A remedial constructive trust will be imposed only if it is required in order to do justice between the parties in circumstances where good commercial conscience determines that the enrichment has been unjust. … it will not be imposed without taking into account the interests of others who may be affected by the granting of the remedy. In this case that would include other creditors of the bankrupt, (both secured creditors and general creditors, since the trust may defeat both), and any relevant third parties.[40]

45. It may be inappropriate to impose a constructive trust where it would be prejudicial to bona fide third-party rights, however, it may be imposed where there is no unfair or unjust effect.[41]

46. If there is a clear and direct enough connection between the assets and the trust claimant, the trust claim can trump the otherwise legitimate interests of a secured creditor.[42] Moreover, Courts have found in insolvency proceedings that in certain cases it's permissible to impose a constructive trust and upset the priority scheme under the *Bankruptcy and Insolvency Act* in order to "do justice to commercial morality".[43]

47. The Monitor is taking the position that it would be inappropriate for the Court to impose a constructive trust over the assets of the CCAA Debtors in favour of H Corp on the basis that it would be prejudicial to the Secured Lender as the senior secured creditor of the CCAA Debtors, as well as to the other parties who have advanced priority claims over the assets of the CCAA Debtors[44]. The Monitor further argues that the Court's imposition of a constructive trust in favour of H Corp would undermine the CCAA by giving H Corp and de factor super-priority and upsetting the priority scheme otherwise prevailing under the CCAA[45].

48. H Corp disagrees with this position for two reasons. First, because granting H Corp a constructive trust over the Diverted Funds and their proceeds does not deprive the Secured Lender of any

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[40] *Ellingsen (Trustee of) v. Hallmark Ford Sales Ltd.* 2000 BCCA 458 at para. 71
[41] *Coast Capital Savings Credit Union v. The Symphony Development Corporation*, 2014 BCSC 400 (CanLII) at para. 46
[42] *306440 Ontario Ltd. v. 782127 Ontario Ltd. (Alrange Container Services)*, 2014 ONCA 548 (CanLII) paras. 32-38
[43] *Ascent Ltd. (*Re), 2006 CanLII 528 (ON SC), [2006] 18 C.B.R. (5th) 269 (ON SC) at para 17
[44] Monitor's Bench Brief (H Corp Claims) at para. 109
[45] Monitor's Bench Brief (H Corp Claims) at paras. 114-115.

collateral that it originally bargained for, and second, because Parliament has expressly recognized and chosen to preserve trust claims in insolvency proceedings.

49. On January 26, 2017, the Secured Lender filed a registration of its security interests over "all present and after-acquired personal property ("**AllPAAP**") of CCAA Debtors as well as a Land Charge registration (the "**Secured Lender's First Security Registration**"). Later, on July 30, 2020, the Secured Lender filed an additional AllPAAP security registration against the CCAA Debtors and a further Land Charge Registration (the "**Secured Lender's Second Security Registration**").[46]

50. In the intervening time between the Secured Lender's First Security Registration and the Secured Lender's Second Security Registration, H Corp filed its own registration of the Attachment Order at the PPR on April 23, 2020, just over three months prior the Second the Secured Lender Security Registration. The Secured Lender's evidence is the Long Run's credit facilities and current indebtedness to the Secured Lender are subject to and governed by various credit agreements (the "**Credit Agreements**") and security agreements that were entered into between Long Run and the Secured Lender on October 27, 2020[47] – six months after the granting and registration of the Attachment Order. Accordingly, at the time that the Credit Agreements were being negotiated and entered into, the Secured Lender was aware of the H Corp Action and the related Attachment Order.

51. The Monitor states that the full amount advanced by the Secured Lender to the CCAA Debtors (being $431MM) was advanced upon the signing of the original Credit Agreement and the registration of the Secured Lender's First Security Registration.[48] The Monitor further sets out that the CCB Secured Debt is currently approximately $355MM – which is less than the original amount advanced.

52. As set out in the Zhang Affidavit, the Diverted Funds were wrongfully transferred from H Corp during the time period from April to September of 2017.[49] Accordingly, when the Secured Lender advanced the funds to Long Run and registered the Secured Lender's First Security Registration, the Diverted Funds and/or their proceeds were not in the possession of the CCAA Debtors and did

[46] Zou Affidavit, Exhibit "N" at pages 11-14 and 23-24, Exhibit "O" at pages 2-3 and 6-7.
[47] Zou Affidavit at paras. 14-21
[48] Monitor's Supplement to the Fifth Report at para. 26
[49] Zhang Affidavit at para. 25

not form part of the collateral that the Secured Lenders were relying upon for the repayment of the CCB Secured Debt.

53. If the Court grants H Corp a constructive trust over the Diverted Funds and their proceeds (after a tracing exercise is performed), the Secured Lenders floating security interest does not attach to the Diverted Funds or their proceeds. There is no unfairness in this as it will not deprive the Secured Lender of anything that it bargained for at the time it advanced the loan amounts to Long Run. At that time, the Secured Lender was not and could not have been relying on the Diverted Funds as collateral secure the loan.

54. Contrary to the submissions of the Monitor, granting H Corp a constructive trust also does not offend insolvency law or the priority structure set out by Parliament in insolvency legislation. In fact, Parliament has decided to expressly recognize and protect trust property from the general body of creditors in an insolvency by enacting specific provisions that allow for trust claims and expressly exclude trust property from the insolvent estate.[50]

Reverse Vesting Orders Generally

55. Typically, in CCAA and other insolvency proceedings assets are transferred from an insolvent entity to a purchaser by way of an Asset Purchase Agreement approved by the Court in using a Sale Approval and Vesting Agreement ("**SAVO**"). The standard form of SAVO directs that the assets be transferred free and clear of all claims and encumbrances (other than permitted encumbrances) and directs that the proceeds of the transaction stand in the place and stead of the assets subject to the creditors' claims in the same priority.

56. RVO's, by contrast, leave the assets in the debtor company while the purchaser acquires the debtor company's shares. The liabilities are then transferred by the RVO to another company, a "residual co.", usually specifically incorporated for this purpose. The purpose of an RVO is that it allows the purchaser to have the benefit of certain of the debtor's assets (such as tax attributes, permits, licenses, and environmental authorizations) that would otherwise be difficult or impossible to transfer using the standard SAVO process. In theory, this results in a higher recovery for the estate as the purchaser is willing to pay more for the enhanced benefits received. Once

[50] See *Bankruptcy and Insolvency Act*, RSC 1985 c. B-3, s. 65(1)(a)

the transaction approved by the RVO is completed the debtor company emerges from the CCAA without the need for proposing or implementing a Plan of Arrangement.

57. Until recently, RVOs were an uncommon form of remedy in CCAA proceedings and although RVOs have increased in frequency the Courts are still clear that they are only to be used in "extraordinary circumstances".[51]

58. RVOs are not expressly set out as a remedy under the CCAA and are instead the creation of the courts and insolvency practitioners relying on a generous, liberal interpretation of the court's general powers under s. 11 of the CCAA.

59. In determining whether an RVO is an appropriate remedy, the Court must first consider whether the usual factors enumerated at s. 36(3) of the CCAA and required for any asset sale under the CCAA have been met, being the following:

(a) Was the process leading to the proposed sale reasonable?

(b) Does the Monitor approve the proposed sale?

(c) Has the Monitor opined that the proposed sale would be more beneficial to creditors than a sale under a bankruptcy?

(d) Were the creditors consulted?

(e) How will the creditors and other interested parties be affected?

(f) Is the consideration offered fair and reasonable? [52]

60. Having considered the s. 36(3) factors, the Court must the consider the following additional factors specific to an RVO transaction:

(a) Why is the RVO necessary?

(b) Does the RVO structure produce an economic result that is at least as favourable as any other viable alternative?

[51] *Invico Diversified Income Limited Partnership v NewGrange Energy Inc*, 2024 ABKB 214 ["***Invico***"] at para. 19. See also *Harte Gold Corp. (Re)*, 2022 ONSC 653 ["***Harte Gold***"] .

[52] *Invico* at para 14.

(c) Is any stakeholder worse off under the RVO structure than they would have been under another viable alternative? and

(d) Does the consideration being paid reflect the value of the intangible assets being preserved under the RVO?[53]

61. Where the debtor is operating in a highly regulated industry and holds valuable regulatory permits and licenses, the conditions are favourable for granting an RVO. The same is true of existing contracts to which the debtor is a party and existing tax attributes would be lost if the assets were sold to a purchaser under a standard SAVO.[54]

The Terms of the Proposed RVO Effectively Extinguish the H Corp Claim and Deprives H Corp of its Rights to Natural Justice

62. H Corp acknowledges that because Long Run is a producer in the highly regulated oil and gas industry in Alberta there are numerous and significant advantages to an RVO transaction that allows the purchaser to enjoy the benefit of certain licenses, permits and other attributes that would not be available under a standard transaction using an SAVO.

63. However, H Corp's position is that those advantages either:

(a) Do not outweigh the prejudice to H Corp if the current form of A&R Subscription Agreement and RVO is granted; and

(b) Could still be realized with an alternate form of A&R Subscription Agreement and RVO that preserves these advantages without prejudicing the H Corp Claim.

64. As set out above, H Corp has a strong *prima facie* claim against the CCAA Debtors for unjust enrichment and a strong argument that the appropriate remedy for the unjust enrichment and/or for the CCAA Debtors' wrongful conduct is a constructive trust in favour of H Corp over those assets of Long Run that can be traced from the Diverted Funds.

65. Unfortunately H Corp has been unable to further substantiate and ultimately prove its claims against the CCAA Debtors due to a combination of: (i) the CCAA Debtors refusal to comply with the Alberta *Rules of Court* during its participation in the H Corp Action; and (ii) the stay of the H

[53] *Invico* at para. 20.; *Harte Gold* at para 38.
[54] *Invico* at paras 21-22.

Corp Action by virtue of the Initial Order in the CCAA Proceedings and the Monitor's refusal to consent to the lifting of the stay.

66. Now, the Monitor seeks to compromise and extinguish the H Corp Action by unilaterally determining, potentially in concert with either one or both of the Secured Lender and the Purchaser, that H Corp's claim to a constructive trust over certain assets of Long Run is invalid, does not have priority to the Secured Lender's security interests, and designating it as a Transferred Liability under the RVO.

67. H Corp submits that the Monitor does not have the jurisdiction or authority to make this determination and, as the cases in the following section demonstrate, it is only a determination that can be made by the Court.

Court's Treatment of Contingent Proprietary Claims when Issuing Vesting Orders

68. This matter is in essence a priority dispute between H Corp and the Secured Lender. If the Purchase Price was fully payable in cash, then the A&R Subscription Agreement could proceed to closing and the subscription proceeds could be held in trust by the Monitor pending a determination of the priority dispute.

69. However, the A&R Subscription Agreement provides for a cash payment of $17.5MM that is calculated as the approximate value of those claims against the CCAA Debtors that some combination of the Monitor, the Secured Lender and the Stalking Horse Bidder/Purchaser have deemed to have priority to the Secured Lender's security interests (defined as the "**Estimated Priority Payable Amount**"). The only other cash portion of the purchase price is $100,000 payable as the "Estimated Trustee Fee Amount" for administering the Creditor Trust, which together with the Estimated Priority Payable Amount constitutes the "Cash Component".[55]

70. Beyond the Cash Component, the balance of the consideration paid is a credit bid of the DIP financing indebtedness owing to the Stalking Horse Bidder and secured with a court-ordered charge against the assets of the CCAA Debtors and the assumption of the Secured Lender debt and all of the other "Retained Liabilities".[56]

[55] Stalking Horse Subscription Agreement, Appendix "B" to the Second Report at Article 2.2
[56] Stalking Horse Subscription Agreement, Appendix "B" to the Second Report at Article at Schedule "B"

71. Because the purchase price under the A&R Subscription Agreement includes the retention of the Secured Lender's Debt while at the same time transferring the H Corp Claims to the Creditor Trust it is not possible for the transaction to close in its current form without resolving the priority dispute.

Invico case

72. A very similar situation was at play in the recent case of *Invico*, where the secured creditor in a CCAA proceeding, Invico Diversified Income Limited Partnership ("**IDILP**"), was applying for an RVO to approve its stalking horse bid for the shares of the CCAA debtor and a portion of the consideration offered included a credit bid. FTI was also the monitor in Invico.

73. IDILP's RVO application purported to transfer and vest out certain gross overriding royalties ("**GORs**") and the royalty claimants opposed the application on the basis that the GORs ran with the lands and should be designated a retained liability instead. As such, this was also a priority contest between a secured creditor and a creditor claiming a proprietary interest in the assets of the CCAA debtor.

74. In Invico, Justice Hollins of the Alberta Court of King's Bench reviewed the contractual language that gave rise to the GORs, along with the surrounding circumstances, and ultimately made the finding that none of the GORs ran with the lands and therefore granted the RVO that IDILP was proposing.

Bison Properties Case

75. The Bison Properties[57] case was a receivership where the receiver had conducted a sale process and was seeking court approval of a bid by the secured construction lenders that was in part cash and in part a credit bid for the set off of the secured indebtedness. The relief sought was a SAVO that would convey clear title to the assets to the secured lenders and vest off a proprietary trust claim that was being asserted by the "Purchasing Bond Holders".

76. The Court determined that the trust claims of the Purchasing Bond Holders could not be determined on a summary basis and granted the SAVO approving the sale on the condition that

[57] *Bison Properties Ltd. (Re)*, 2016 BCSC 793 (CanLII) ("***Bison Properties***")

a portion of the sale proceeds (equal to the full amount of the trust claims) be placed into trust and held by the receiver pending an expedited adjudication of the merits of the trust claims.[58]

American Iron Case

77. In *American Iron*[59], the secured creditor, American Iron & Metal Company ("**AIM**") was seeking an Order for the appointment of a receiver over the debtors, along with approval of a stalking horse sale process for the sale of the debtors' property. The stalking horse bid contemplated a small cash component with the much larger balance being a credit bid of the secured indebtedness of the debtors to AIM. The sale process also contemplated a SAVO that would have the effect of extinguishing a contingent constructive trust proprietary claim by NASG Canada Inc. ("**NASG**") over the property of the debtors.

78. NASG objected to the relief sought by AIM and although the Court ultimately approved the relief sought by AIM, it did so only on the condition that the net sale proceeds be held in trust by the receiver pending a determination of the validity of NASG's constructive trust claim.[60]

Outcome of the case authorities

79. The commonality between Invico, Bison Properties and American Iron, is that the Courts in each of these cases were unwilling to issue an Order, whether it be an RVO or a SAVO, that vested off a contingent proprietary claim without first either:

(a) Adjudicating the contingent proprietary claim on a summary basis to determine its validity (as was done in *Invico*); or

(b) Placing funds in trust in an amount equivalent to value of the contingent proprietary claim until the parties have an opportunity to have the priority dispute resolved in an expeditious manner (as in *Bison Properties* and *American Iron).*

80. H Corp submits that the Courts in these other instances recognized that insolvency sale processes, and SAVOs and RVOs approving those processes, should not be used by secured creditors as a means by which to defeat competing contingent proprietary claims without first preserving them and allowing for their proper adjudication. H Corp further submits that the Court should not vary

[58] *Bison Properties* at paras 132-135
[59] *American Iron v. 1340923 Ontario*, 2018 ONSC 2810 (CanLII) ("***American Iron***")
[60] *American Iron* at paras. 29 and 33.

this approach in this case as H Corp is entitled to the same access to justice as the claimants in these other cases.

Alternative Measures to Preserve H Corp's Rights

81. As stated above, prior to granting an RVO, the Court must ask: "Is any stakeholder worse off under the RVO structure than they would have been under another viable alternative?" H Corp is severely prejudiced by the RVO and submits that while there may not be a viable alternative to an RVO process generally, there are a number of viable alternative ***structures*** to the RVO proposed that would preserve H Corp's rights.

82. Unlike in *Invico*, H Corp's Claims are not capable of being decided in a Chambers application on a summary basis prior to the Court issuing the RVO. As a result, if the transaction contemplated in the Stalking Horse Subscription Agreement is to proceed, it must provide for the preservation of the H Corp Claims in one of the following two ways:

    (a) The Stalking Horse Bidder pays the additional sum of $44 million (being the maximum amount of H Corp's claim in the H Corp Action) to the Monitor to hold in trust pending an adjudication of H Corp's constructive trust claim, including a determination of the amount and whether it has priority to the claims of the secured creditor of the Debtors. This adjudication could be done on an expedited basis in a streamlined process to be agreed upon between the Monitor and H Corp and could also include the use of an independent Court-appointed Inspector to review the books and records of the CCAA Debtors to determine the use and current location of the Diverted Funds;

    (b) Alternatively, if Stalking Horse Bidder is unable or unwilling to post the $44 million in respect of the H Corp Action, the H Corp Action and H Corp's underlying claims against the Debtors must be included as Retained Liabilities of Long Run in the Subscription Agreement and RVO and following the closing of the Stalking Horse Transaction the H Corp Action will proceed in the ordinary course.

83. Each of these proposals was presented to the Monitor well in advance of this Application and were emphatically denied on the basis that the Purchaser is not willing to pay an additional cash

component of $44 million and it not willing to proceed with the transaction if the H Corp Claim is designated as a "Retained Liability". [61]

84. H Corp submits that the Purchaser's willingness to accept one of these two solutions should not be determinative of whether H Corp's contingent proprietary claim can be disregarded and unilaterally deemed invalid by the Monitor. If the Purchaser is not prepared to proceed with a transaction that observes H Corp's rights and allows a proper adjudication then the transaction with the Purchaser is simply not viable the same way that the Monitor deemed other potential transactions to be not viable.

85. The Monitor, who is a court officer and has a duty to all stakeholders of the estates of the CCAA Debtors, has not demonstrated any effort to accommodate a process by which the H Corp Claim can be fairly and finally adjudicated. Instead, in what is essentially a priority dispute between the contingent constructive trust claim of H Corp and the security interests of the Secured Lender, the Monitor has advocated for the Secured Lender's position at every turn.

86. As set out in the Zhang Affidavit, H Corp is prepared to proceed with the H Corp Action on an expedited basis and has proposed a draft Procedural Order to accomplish exactly that.[62] A creative solution that allows the Monitor's transaction with the Purchaser to proceed with a substantially similar form while still preserving H Corp's rights to proceed with the H Corp Action on this expedited time line would be to amend the terms of the A&R Subscription Agreement as follows:

(a) The A&R Subscription Agreement is amended such that the H Corp Action is moved to the "Retained Liability" schedule;

(b) The A&R Subscription Agreement proceeds to closing;

(c) H Corp proceeds with the H Corp Action on the expedited schedule proposed by H Corp's litigation counsel or some modification thereof;

(d) An independent Court-appointed Inspector reviews the books and records of the CCAA Debtors in order to prepare a report on the ultimate disposition of the Diverted Funds

[61] Affidavit of Elvina Hussein, sworn on November 7, 2024, Exhibits "A" and "B"
[62] Zhang Affidavit at paras. 78-80 and Exhibit "34"

and in the process will identify any traceable assets and obtain an appraisal of those traceable assets;

(e) If the Court finds liability on behalf of the CCAA Debtors and the Individual Defendants AND the Inspector identifies traceable assets from the Diverted Funds, there will be an Application served on notice to the Secured Lender to determine whether H Corp should be granted the remedy of a constructive trust over the traceable assets notwithstanding the Secured Lenders security interests;

(f) If the Court awards a constructive trust in favour of H Corp over the traceable asset(s), the Purchaser/Long Run is notified and can elect to either retain the traceable asset(s) over which the constructive trust is granted or surrender them to H Corp;

(g) If the traceable asset(s) are surrendered to H Corp, the Secured Lender will reduce the Secured Debt owing by Long Run by an amount equal to the appraised value of the traceable asset(s); and

(h) If the Purchaser/Long Run wishes to retain the traceable asset(s), the Secured Lender will pay an amount equal to the appraised value of the traceable asset(s) to H Corp and the value of the Secured Debt owing by Long Run remains unchanged.

87. H Corp submits that the above process is a means by which the proposed transaction could go ahead while both preserving the H Corp Action and providing the Purchaser with the same deal that it has bargained for. There is no risk for the Purchaser as in the end it can elect to either surrender the traceable asset(s) and reduce the consideration it paid by the equivalent amount or it can retain the traceable asset(s) for the same and leave the Secured Debt unaltered.

88. The above proposal does create some risk for the Secured Lender, however, if a Court were to find that certain of Long Run's assets are traceable to the Diverted Funds, the Secured Lender should not be entitled to the benefit of those assets as part of its collateral. A decision as to whether H Corp is entitled to a constructive trust over certain assets in priority to the security interests of the Secured Creditor is better determined once those assets have been identified rather than at the present application.

Unjust Preservation of the Third Party Claim

89. In addition to effectively extinguishing the H Corp Claims, the A&R Subscription Agreement also preserves the Third Party Claim against the H Corp Related Parties and the rest of the Third Party Defendants.

90. One of the "Retained Assets" under the A&R Subscription Agreement is "all Claims, rights, Losses or causes of action by or on behalf of the Company against any Person".[63] As a result of this broad language, the Third Party Claim and the causes of action underlying the Third Party Claim will survive the RVO and remain with the CCAA Debtors. In theory, following the closing of the A&R Subscription Agreement, the CCAA Debtors will be at liberty to pursue the H Corp Related Parties while the H Corp Claims will have been transferred to the Creditor Trust thereby severing any mutuality of the debts and prejudicing any rights of set off.

91. It is unclear whether this is an intended consequence or an oversight on the part of the Monitor, but it is clearly an inequitable result that is only made possible by the form of RVO recommended by the Monitor. The RVO and/or A&R Subscription Agreement should either be amended to prevent this unjust result or otherwise the RVO approving the A&R Subscription Agreement should not be granted by the Court.

The Release Provisions in the RVO are too broad

92. The RVO proposed by the Monitor contains an extremely broad release clause that is unjustifiable in the circumstances.

93. H Corp opposes the language of the release clause as it applies to an extremely broad range of individuals, including the CCAA Debtors and all of their "current and former directors, officers, employees, contractors, executive team, agents, representatives, and all of their respective advisors…….". It is arguable that this extremely broad language includes every individual that has ever been involved in any capacity with the CCAA Debtors, including the Individual Defendants in the H Corp Action. For obvious reasons this is a significant concern for H Corp who, regardless of the outcome of this Application, wish to proceed with the H Corp Action against the Individual Defendants.

[63] A&R Subscription Agreement at Schedule "B" pg. B-8

94. The Individual Defendants all formerly had various official roles with the CCAA Debtors, either as directors, officers, contractors and/or consultants.[64] On a plain reading of the release clause in the RVO, after the Effective Time the Individual Defendants would be released from all claims apart from those claims that qualify as fraud, gross negligence or willful misconduct, or any claim not permitted to be released pursuant to s. 5.1(2) of the CCAA.

95. Counsel for the Monitor attempts to justify the release provision on the basis that it satisfies the factors in the *Lydian* decision[65] as follows:

(a) Whether the parties to be released from claims were necessary and essential to the restructuring efforts of the debtor;

(b) Whether the claims to be released were rationally connected to the purpose of the plan of arrangement and necessary for it;

(c) Whether the plan of arrangement could succeed without the releases;

(d) Whether the parties being released contributed to the restructuring; and

(e) Whether the release benefits the debtors as well as the creditors generally.

96. There is no evidence that the Individual Defendants have had any involvement in the CCAA proceedings of the CCAA Debtors or made any contributions to this restructuring. As a result, the *Lydian* factors certainly don't apply to them.

97. H Corp concedes that it's possible, and even likely, that the H Corp Claims against the Individual Defendants qualify as fraud, gross negligence or willful misconduct, or a claim that falls under s. 5.1(2) of the CCAA. However, there is still no justification for releasing the Individual Defendants from claims that don't fall squarely within those limited categories. Further, H Corp should not have to overcome the hurdle of proving that the H Corp Claims against the Individual Defendants fall within one of these categories to be able to proceed with the H Corp Action against them.

98. Accordingly, H Corp submits that regardless of the Courts determinations on the other issues raised in this brief, the RVO should not be granted in its current form and the release clause should

[64] Third Party Claim, at paras. 6-9 and 11-12.
[65] *Re Lydian International Limited*, 2020 ONSC 4006, cited in Bench Brief of the Monitor at para. 56

be narrowed to those who participated and contributed to the restructuring of the CCAA Debtors and to expressly exclude the Individual Defendants.

The A&R Subscription Agreement and RVO violate s. 19(2)(c) and (d) of the CCAA

99. Parliament has seen fit to expressly exclude certain claims from being compromised under the CCAA. Section 19(2) of the CCAA states in part as follows:

> **Exception**
>
> (2) A compromise or arrangement in respect of a debtor company may not deal with any claim that relates to any of the following debts or liabilities unless the compromise or arrangement explicitly provides for the claim's compromise and the creditor in relation to that debt has voted for the acceptance of the compromise or arrangement:
>
> …….
>
> (c) any debt or liability arising out of fraud, embezzlement, misappropriation or defalcation while acting in a fiduciary capacity or, in Quebec, as a trustee or an administrator of the property of others;
>
> (d) any debt or liability resulting from obtaining property or services by false pretences or fraudulent misrepresentation, other than a debt or liability of the company that arises from an equity claim; [66]

100. The creditor who asserts that its claim falls under s. 19 (2) bears the burden to prove on a balance of probabilities that it falls under one of the enumerated categories of s. 19(2).[67]

101. H Corp has proven on a balance of probabilities, both in the prior proceedings in the H Corp Action and by virtue of the evidence contained in the Zhang Affidavit, that the CCAA Debtors obtained property of H Corp (the Diverted Funds) under false pretenses and/or by way of fraudulent misrepresentation.

102. To discharge its burden of proving that its claim relates to a debt "resulting from obtaining property or services by false pretenses or fraudulent misrepresentation", a creditor must establish, on a balance of probabilities, the following four elements: (i) the debtor made a

[66] *Companies' Creditors Arrangement Act*, RSC 1985, c C-36, as amended, at s. 19(2)
[67] *Montréal (City) v. Deloitte Restructuring Inc*., 2021 SCC 53, para 25.

representation to the creditor; (ii) the representation was false; (iii) the debtor knew that the representation was false; (iv) the false representation was made to obtain property or a service[68]

103. As set out above and as evidenced in the Zhang Affidavit, the CCAA Debtors, through the actions of the Individual Defendants, knowingly obtained the Diverted Funds from H Corp by falsifying bank records and financial statements. Accordingly, the H Corp Claims, that the Monitor is seeking to extinguish by transferring them to the Creditors' Trust, fall squarely within s. 19(2)(d) of the CCCAA.

104. Additionally, the wrongful fraudulent actions of the Individual Defendants in misappropriating the Diverted Funds were done while occupying positions as directors, officers and consultants/agents of H Corp and its affiliates, positions that gave rise to fiduciary duties owing to H Corp. As a result, the H Corp Claims against the Individual Defendants clearly fall under s. 19(2)(c) of the CCAA.

105. Notwithstanding that the H Corp Claims against the CCAA Debtors and the Individual Defendants clearly fall under s. 19(2), the Monitor is putting forward and asking the Court to violate s. 19(2) by approving the A&R Subscription Agreement and the RVO, which either impair the H Corp Claims (in the case of the Individual Defendants) or extinguish them entirely by moving them to the Creditor Trust (in the case of the CCAA Debtors).

106. The Monitor has expressly acknowledged in its Bench Brief that even though this is an RVO transaction and not a Plan of Arrangement under the CCAA, s. 5.1 of the CCAA applies to the transaction and must be included as a carve out in the release provision.[69] Likewise, s. 19(2) of the CCAA must also be complied with and any proposed RVO transaction that violates s. 19(2) should not be approved.

107. As mentioned, RVO's are not expressly permitted under the CCAA and are a creation of the courts and insolvency practitioners relying on the broad authority granted to the court under s. 11 of the CCAA. This Court should not use that authority in this instance to approve the current form of A&R Subscription Agreement and RVO where it would be contrary to s. 19(2), which is a provision that Parliament saw fit to expressly mandate when drafting the CCAA. For this reason, among the

[68] *Montréal (City) v. Deloitte Restructuring Inc*., 2021 SCC 53, para 25
[69] Monitor's Brief at para. 54

other reasons set out in this brief, this Court should refuse to grant the relief sought by the Monitor in its Application.

CONCLUSION

108. As mentioned at the outset of this brief, H Corp does not dispute that in light of the business of Long Run and the character of Long Run's assets the best way to maximize the value of the estate of Long Run is through the use of an RVO. What H Corp does dispute, however, is the form of the A&R Subscription Agreement and RVO that the Monitor is asking this Court to approve.

109. The Monitor, or some combination of the Monitor, the Purchaser and the Secured Lender, have made the unilateral determination that the H Corp Claims, including H Corp's claim to a constructive trust over assets of Long Run, are invalid. They have made this determination by electing to include the H Corp Action in the category of "Transferred Liabilities" under the A&R Subscription Agreement while allowing the Secured Debt, in its entirety, to be assumed by the purchaser as a "Remaining Liability" continuing to be secured by the "Remaining Assets".

110. As clearly established in the *Invico*, *Bison Properties* and *American Iron* cases, it is only the Court that is entitled to determine the validity of contingent proprietary claims. When those contingent proprietary claims cannot be determined on a summary basis, these decisions illustrate how Courts have taken the necessary steps to preserve those claims, as well as an avenue to satisfy those claims if successful, pending a full and proper adjudication of the matter.

111. In the present case, due to the nature of the consideration that the Purchaser is offering under the A&R Subscription Agreement, it is not feasible to set aside funds in trust pending an adjudication of the H Corp Action. However, H Corp has suggested a creative solution that preserves H Corp's rights while still providing the Purchaser with certainty and allowing the proposed RVO transaction to proceed with the necessary modifications. To do otherwise by approving the RVO transaction in its current form would be to deny H Corp's rights to due process and natural justice.

REMEDY SOUGHT

112. Accordingly, H Corp respectfully requests that the relief sought by the Monitor, being the approval of the A&R Subscription Agreement and the RVO, be denied in its entirety unless it incorporates the modifications suggested herein or such other modifications as are necessary to preserve the H Corp Claims and H Corp Remedies.

ALL OF WHICH IS RESPECTFULLY SUBMITTED this 7th DAY OF NOVEMBER 2024.

FIELD LLP

Per: _____

Trevor Batty
Counsel for Henenghaixin Corp.

TABLE OF AUTHORITIES

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1. *Moore v. Sweet*, [2018] 3 SCR 303
2. *Kerr v. Baranow*, 2011 SCC 10 (CanLII)
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5. *Lac Minerals Ltd. v International Corona Resources Ltd.*, [1989] 2 S.C.R. 574
6. *Toronto-Dominion Bank v. Preston Springs Gardens Inc.*, 2004 CanLII 10168 (ON SC)
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12. *Invico Diversified Income Limited Partnership v NewGrange Energy Inc*., 2024 ABKB 214 - See also *Harte Gold Corp. (Re)*, 2022 ONSC 653
13. *Bison Properties Ltd. (Re)*, 2016 BCSC 793 (CanLII)
14. *American Iron v. 1340923 Ontario*, 2018 ONSC 2810 (CanLII)
15. *Re Lydian International Limited*, 2020 ONSC 4006 , cited in Bench Brief of the Monitor at para. 56
16. *Companies' Creditors Arrangement Act*, RSC 1985 c C-36, as amended at s. 19(2)
17. *Montréal (City) v. Deloitte Restructuring Inc.*, 2021 SCC 53