Court File No.: CV-17-11846-00CL

ONTARIO
SUPERIOR COURT OF JUSTICE
(COMMERCIAL LIST)

IN THE MATTER OF THE *COMPANIES' CREDITORS ARRANGEMENT ACT*, R.S.C. 1985, c.C-36, AS AMENDED

AND IN THE MATTER OF A PLAN OF COMPROMISE OR ARRANGEMENT OF SEARS CANADA INC., 9370-2751 QUÉBEC INC., 191020 CANADA INC., THE CUT INC., SEARS CONTACT SERVICES INC., INITIUM LOGISTICS SERVICES INC., INITIUM COMMERCE LABS INC., INITIUM TRADING AND SOURCING CORP., SEARS FLOOR COVERING CENTRES INC., 173470 CANADA INC., 2497089 ONTARIO INC., 698874I CANADA INC., 10011711 CANADA INC., 1592580 ONTARIO LIMITED, 955041 ALBERTA LTD., 4201531 CANADA INC., 168886 CANADA INC., AND 3339611 CANADA INC.

The Applicants

FACTUM OF EDWARD S. LAMPERT, ESL INVESTMENTS INC., ESL PARTNERS, L.P. AND RBS PARTNERS, L.P., SPE I PARTNERS, LP, ESL INSTITUTIONAL PARTNERS, L.P., SPE MASTER I, LP, CRK PARTNERS, LLC AND ESL INVESTORS, LLC
(MOTION RETURNABLE MARCH 2, 2018)

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TO: **THE SERVICE LIST**

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PART I - INTRODUCTION

1. The representative counsel for the retirees and former employees (the "**Representative Counsel**") of certain debtors in these proceedings (the "**Sears Canada Entities**") brings this motion for the appointment of a court officer to act as litigation trustee (the "**Litigation Trustee**") to investigate, consider and report upon a "*universe of potential claims*", including potential claims of creditors against third parties (the "**Mandate**").

2. The respondent equity holders, Mr. Edward Lampert, ESL Investments Inc., ESL Partners, L.P., RBS Partners, L.P., SPE I Partners, LP, ESL Institutional Partners, L.P., SPE Master I, LP, CRK Partners, LLC and ESL Investors, LLC (the "**Respondent Equity Holders**") do not object to the appointment of a litigation advisor or agent to assist in the investigation or litigation of such potential claims or to the formation of a committee of creditors (the "**Committee**") to investigate and attempt to litigate any potential claims which are not already statute barred. If the Committee wishes to seek funding for such an advisor or agent out of the estate of the Sears Canada Entities, the Court may so order if it deems such funding appropriate from time to time.

3. The Respondent Equity Holders submit this Factum, however, for the limited purpose of objecting to the characterization and appointment of such an advisor as a *court officer* and to clarify certain terms of the proposed order to ensure that certain due process rights are protected.

4. The appointment of such a court officer on the terms proposed in the Motion would

   (a) vest in a court officer the power to investigate, consider and report on claims between stakeholders and/or third-parties, which this Court has clearly stated is not the purpose of the CCAA, but which are functions more appropriate to a private litigation agent.

5. If an order is granted, the Respondent Equity Holders submit that it should provide for the organization of creditors to investigate and pursue potential litigation claims through the formation of a Committee and the retention of an advisor, litigation agent or further representative counsel (the "**Litigation Advisors**") without special status or special procedural or substantive rights.

6. Alternatively, should the Court deem it appropriate to appoint the Litigation Trustee to act as a court officer, the Litigation Trustee's powers should be limited to the investigation of claims belonging to the estate of the applicant debtors against third-parties. No creditors should be granted privileged consultation or information rights.

PART II - FACTS

7. The Representative Counsel has submitted into evidence various statements about the history of the Applicant Sears Canada Inc. ("**Sears Canada**") and its relationship with certain of its shareholders, some of which are misleading, some insufficiently contextualized, and some categorically false, as set forth below.

The Responding Equity Holders' Ownership Interests in Sears Canada

8. On November 13, 2012, several of the Responding Equity Holders obtained equity interests in Sears Canada pursuant to a spin-off transaction by Sears Holdings Corporation ("**Sears Holdings**") in which Sears Holdings distributed some of its shares in Sears Canada to Sears Holdings shareholders (the "**2012 Spin-Off Transaction**").

9. Immediately after the 2012 Spin-Off Transaction, the Respondent Equity Holders held a minority position of approximately 27.6 percent of the outstanding Sears Canada shares, while Sears Holdings retained majority ownership with approximately 51 percent of outstanding Sears Canada shares.

The 2012 and 2013 Sears Canada Dividends

10. The net earnings, cash reserves, and equity value for Sears Canada for 2011-2013 are set forth in the table below:

Financial Year	Net Earnings (loss)[1]	Dividend Declared	Equity Value at end of period	Cash and Cash Equivalents at end of period
2011	(50.3)	0	1,092.0	400.2
2012	101.2	101.9	1,076.4	238.5
2013	446.5	509.4	1,073.8	513.8

11. Sears Canada authorized the dividend paid by Sears Canada as of December 20, 2012 (the "**2012 Dividend**") and the dividend paid by Sears Canada as of December 9, 2013 (the "**2013 Dividend**").

12. The 2012 Dividend and the 2013 Dividend totaled CAD $611.3 million. As aggregate holders of approximately 27.6% of the outstanding equity in Sears Canada as a result of the 2012 Spin-Off Transaction was disclosed in public securities filings, the Respondent Equity Holders[2] received approximately CAD $169 million[3] in aggregate from the 2012 Dividend and 2013 Dividend combined.

13. Mr. Lampert did not serve on the board of Sears Canada when the board of directors of Sears Canada authorized the 2012 Dividend or 2013 Dividend.

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[1] All figures are CAD$ million.
[2] Two of the Respondent Equity Holders, RBS Partners, L.P. and ESL Investors, LLC, never received dividends from Sears Canada.
[3] The Affidavit of Jonathan Wypych ["**Wypych Affidavit**"], para 4, Responding Motion Record, Tab 1.

The Respondent Equity Holders Purchase Additional Shares in Sears Canada After the 2012 and 2013 Dividends

14. Pursuant to a rights offering completed on October 26, 2014 (the "**2014 Rights Offering**"), the Respondent Equity Holders paid an additional CAD $168 million[4] to Sears Holdings in exchange for additional equity interests in Sears Canada. As a result of the 2014 Rights Offering, the Respondent Equity Holders increased their aggregate equity holdings to 46.7% of the outstanding shares of Sears Canada.

15. The market value of the Respondent Equity Holders' equity holdings in Sears Canada shortly after the 2014 Rights Offering was approximately USD $270,000,000.

PART III - ISSUES AND THE LAW

16. The Representative Counsel's motion raises the following issue for determination:

Does the CCAA court have jurisdiction in these circumstances to appoint a court officer to investigate and potentially prosecute claims that a sub-set of creditors might have against non-applicants?

17. In tacit acknowledgement that the relief it requests is novel, the Representative Counsel relies on this court's broad discretionary power under Section 11 of the CCAA:[5]

> 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.

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[4] Wypych Affidvait, para 13, Responding Motion Record, Tab 1.
[5] *Companies' Creditors Arrangement Act*, RSC 1985, c. C-36, s. 11.

18. While CCAA courts have very broad discretion to grant orders under Section 11, such discretion may only be exercised in furtherance of the remedial objectives of the Act, "namely, to permit the debtor to carry on business and avoid the social and economic consequences of liquidation".[6] The Supreme Court of Canada in *Ted Leroy Trucking Ltd., Re* noted that the "appropriateness" at the core of Section 11 "extends not only to the purpose of the order, but also to the means it employs."[7] Section 11 provides no basis for appointment of court officers to investigate and organize litigation that is outside the CCAA Court's jurisdiction.

19. The effect of the proposed order is to appoint a court officer for the Committee's own purposes to carry out an investigation into, and report upon, causes of action that *may* lie in the hands of *creditors* against third parties. While the CCAA court will adjudicate inter-stakeholder litigation in very limited circumstances, it will only do so where a legitimate *restructuring reason* exists. Since Sears Canada is in liquidation, no such reason exists here.

20. The CCAA Court generally should not adjudicate or prosecute disputes between stakeholders. This was the opinion of the Ontario Court of Appeal in *Stelco Inc., Re*. At paragraph 32 of that decision, the Court of Appeal considered the intended scope of the CCAA:[8]

> First, as the supervising judge noted, the CCAA itself is more compendiously styled "An act to facilitate compromises and arrangements between companies and their creditors". There is no mention of dealing with issues that would change the nature of the relationships as between the creditors themselves. As Tysoe J. noted in *Pacific Coastal Airlines Ltd. v. Air Canada*, [2001] B.C.J. No. 2580 (B.C. S.C.) at para. 24 (after referring to the full style of the legislation):
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> > [The purpose of the CCAA proceeding] is not to deal with disputes between a creditor of a company and a third party, even if

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[6] *U.S. Steel Canada Inc., (Re)*, 2017 ONCA 99 at para 5, Brief of Authorities of the Respondents (**"Respondents' BOA"**) Tab 7.
[7] *Ted Leroy Trucking [Century Services] Ltd., (Re)*, 2010 SCC 60 at para 70 [*Century Services*]. See also *Century Services* at para 59, Respondents' BOA Tab 6.
[8] *Stelco Inc., (Re)*, [2005] O.J. No. 4883 at para 32, Respondents' BOA Tab 5.

> the company was also involved in the subject matter of the dispute. While issues between the debtor company and non-creditors are sometimes dealt with in CCAA proceedings, it is not a proper use of a CCAA proceeding to determine disputes between parties other than the debtor company. [Emphasis added]

21. This principle, articulated in *Stelco*, has informed recent jurisprudence emphasizing the rare and very limited scope of monitors' role as an adversary in disputes between stakeholders. In *Ernst & Young Inc. v. Essar Global Fund Ltd et al*, Justice Newbould granted standing to the monitor to bring an oppression action on behalf of creditors that were affected by a sale of an asset that was crucial to the successful restructuring of the debtor. The litigation was necessary to the overall success of the restructuring. In upholding Justice Newbould's decision, the Ontario Court of Appeal clarified that it "will be a rare occasion that a monitor will be authorized to be a complainant".[9] The Court of Appeal held that factors to be considered by a CCAA Court in permitting such litigation will include ***whether the proposed action or application by the monitor has a restructuring purpose***, and whether any other stakeholder is better placed to be a complainant.[10]

22. The precedent in Justice Newbould's decision in *Essar* was similarly circumscribed in Justice Myers' recent decision in *Urbancorp Cumberland 2 GP Inc., (Re)*. In refusing a monitor's motion that effectively sought approval to commence litigation, Justice Myers addressed the exceptional circumstances that existed in *Essar*, which involved litigation that was necessary to effect a proper and fair restructuring:[11]

> The Monitor is not a trustee in bankruptcy. The creditors know how to bankrupt a debtor if they believe doing so is appropriate. In the interim, I do not see how, in this liquidating *CCAA* process, the Monitor bringing proceedings in place of the creditors who stand to gain from it can be said to facilitate the restructuring. In *Essar* there was a particular roadblock to

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[9] *Ernst & Young Inc. v. Essar Global Fund Limited*, 2017 ONCA 1014 at para 123 [*Essar*], Respondents' BOA Tab 2.
[10] *Ibid*, Respondents' BOA Tab 2.
[11] *Urbancorp Cumberland 2 GP Inc., (Re)*, 2017 ONSC 7649 at para 21 [*Urbancorp*], Respondents' BOA Tab 8.

> a fair and proper restructuring affecting all interested parties. Here, by contrast, the Monitor pits the current creditors against a group of creditors who were paid over one year before the proceedings commenced. Why is this a fight for the Monitor rather than the creditors who stand to benefit from the claim?

23. Just as in the *Urbancorp* case, and as the Representative Counsel has stressed, the present proceeding is a *liquidating* CCAA. There is no plan or arrangement before the Court, and no going concern sale of the applicants that will preserve value for all stakeholders. In other words, the animating factors in the *Essar* restructuring that informed Justice Newbould's exceptional remedy (to take jurisdiction over claims on behalf of creditors against third parties) are missing from this case. While Justice Myers suggested that proceedings could be brought by the Monitor in certain limited circumstances, he was "not convinced in the utility of empowering the Monitor to drop its cloak of neutrality to bring what are really inter-creditor proceedings."[12]

24. The Litigation Trustee's mandate would include reporting to a select committee of creditors who would effectively provide instructions to the Litigation Trustee. This would be a departure from one of the defining duties of court officers in insolvency proceedings – to be independent. This request is further evidence that the Mandate is best suited to a privately appointed advisor.

25. Courts have long recognized the need to protect the integrity of insolvency proceedings, and the impartial role of court officers, through transparency. In *Winalta Inc., Re*, the Alberta Court of Queens' Bench commented on the inappropriateness of the monitor giving a secured creditor special access to

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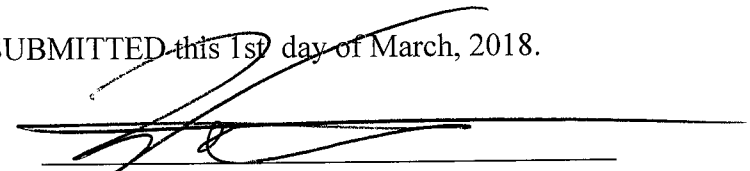
[12] *Urbancorp* at 22, Respondents' BOA Tab 8. The same principle was recently illustrated in a decision of Justice Conway of this Court. In *Wintercorn v. Global Learning et. al.*, her honour refused to appoint a receiver solely for the purpose of commencing a claim against certain professional defendants that were already the defendants in two proposed class proceedings. She found that it was not "just and convenient" to appoint a receiver for the purpose of commencing an action given the two existing parallel proceedings. She found that "[t]he Receiver is not being sought to advance defences on the part of [the prospective litigant debtor] but rather to advance the plaintiff's interest in the existing litigation." Endorsement of Justice Conway dated November 14, 2017 (CV-17-584138-00CL), Respondents' BOA Tab 1.

reports.[13] The Court found that the monitor had lost sight of the bright line between court officer and private consultant when it provided a report to a creditor, which created the appearance of bias.[14] The Court commented that a monitor, like bankruptcy trustees, cannot allow its appointment to favour one party or one side.[15]

PART IV - ORDER REQUESTED

26. The Respondents respectfully request that to the extent the Court is inclined to grant the motion, the order sought by Representative Counsel be revised as set forth in the alternative form of order provided by the Respondent Equity Holders.

ALL OF WHICH IS RESPECTFULLY SUBMITTED this 1st day of March, 2018.



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SCHEDULE "A"
LIST OF AUTHORITIES

1. Endorsement of Justice Conway dated November 14, 2017 (CV-17-584138-00CL).
2. *Ernst & Young Inc. v. Essar Global Fund Limited*, 2017 ONCA 1014.
3. Tom Cumming, Tony Mersich, & Pierre Grabinski, "Litigation Trusts in CCAA Proceedings" (2017) ANNREVINSOLV 16 (Janis Sarra, Ed.).
4. *Lutheran Church – Canada, (Re)*, 2016 ABQB 419.
5. *Stelco Inc., (Re)*, [2005] O.J. No. 4883.
6. *Ted Leroy Trucking [Century Services] Ltd., (Re)*, 2010 SCC 60.
7. *U.S. Steel Canada Inc., (Re)*, 2017 ONCA 99.
8. *Urbancorp Cumberland 2 GP Inc., (Re)*, 2017 ONSC 7649.
9. *Winalta Inc., (Re)*, 2011 ABQB 399.

SCHEDULE "B"
RELEVANT STATUTES

1. *Companies' Creditors Arrangement Act*, RSC 1985, c C-36, s 11.

11. General power of court

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.

Amendment History 1992, c. 27, s. 90; 1996, c. 6, s. 167(1)(d); 1997, c. 12, s. 124; 2005, c. 47, s. 128

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Applicants

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Proceeding commenced at Toronto

FACTUM OF EDWARD S. LAMPERT, ESL INVESTMENTS INC., ESL PARTNERS, L.P. AND RBS PARTNERS, L.P., ET AL. (MOTION RETURNABLE March 2, 2018)

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