

1989 CarswellBC 334, 73 C.B.R. (N.S.) 195, [1989] 3 W.W.R. 363, 34 B.C.L.R. (2d) 122

1989 CarswellBC 334

Northland Properties Ltd. v. Excelsior Life Insurance Co. of Canada

NORTHLAND PROPERTIES LIMITED et al. v. EXCELSIOR LIFE INSURANCE COMPANY OF CANADA,  
NATIONAL LIFE ASSURANCE COMPANY OF CANADA and GUARDIAN INSURANCE CO. OF CANADA

British Columbia Court of Appeal

McEachern C.J.B.C., Esson and Wallace JJ.A.

Judgment: January 5, 1989

Docket: Vancouver Nos. CA010238; CA010198; CA010271

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Counsel: *F.H. Herbert* and *N. Kambas*, for appellant Excelsior Life Insurance Company of Canada and appellant National Life Assurance Company of Canada.

*A.P. Czepil*, for appellant Guardian.

*H.C.R. Clark* and *R.D. Ellis*, for respondent companies.

*G.W. Ghikas* and *C.S. Bird*, for respondent Bank of Montreal.

Subject: Corporate and Commercial; Insolvency

Corporations --- Arrangements and compromises — Under Companies' Creditors Arrangement Act — Arrangements — Approval by Court — "Fair and reasonable".

Corporations — Arrangements and compromises — Reorganization plan under Companies' Creditors Arrangement Act providing for consolidation of petitioner companies and grouping all priority mortgagees into one voting class — Two priority mortgagees, not being fully secured creditors, voting against and appealing court order approving plan — Appeal dismissed — Consolidation being appropriate where economic prejudice less than prejudice arising from continued debtor separateness — Composition of priority creditors not being unfair since plan formulated for benefit of all creditors, who had indicated approval — Plan being fair and reasonable since priority mortgagees assured value of security without liquidation expenses and this result being unavailable in absence of plan.

After the petitioners' bank commenced receivership proceedings against the petitioners, the court approved a reorganization plan filed under the Companies' Creditors Arrangement Act. The plan incorporated a settlement agreement that had been reached between the bank and the petitioners. In addition, the plan proposed consolida-

tion of all the petitioners and provided that all priority mortgagees would be grouped into one class for voting purposes. Of the 15 priority mortgagees, 11 were fully secured while the remaining four, including the respondents, faced deficiencies. All classes of creditors had voted unanimously in favour of the plan, except the priority mortgagee class, which had none the less approved the plan by the requisite majority under the Act. Prior to the settlement with the bank, R. Ltd., a priority mortgagee facing a deficiency, had struck an agreement with the petitioners on the value of its security amounting to approximately \$900,000 over a disputed appraisal value. R. Ltd. agreed in the settlement to vote in favour of the plan. Had it voted against, the petitioners would not have obtained the requisite majority from the priority mortgagee class. The respondents appealed the order approving the plan on a number of grounds.

**Held:**

Appeal dismissed.

There was some merit in the respondents' argument that the Act does not authorize the creditors of one company to vote on the disposition of a creditor's security in another company. However, the plan contemplated the consolidation of the petitioners and the chambers judge correctly concluded that consolidation was appropriate if its economic prejudice was less than the prejudice arising from continued debtor separateness.

Furthermore, the composition of the class of priority creditors was not unfair. The plan was not only for the benefit of the undersecured priority mortgagees, but also for the benefit of the companies and other creditors who, by their votes, had indicated that they thought the plan was in their best interest. Nor was the plan tainted by the agreement between R. Ltd. and the respondents. The agreement was not made for the purpose of ensuring a favourable vote because at the time it was made the petitioners had not yet reached a settlement with the bank. Furthermore, the agreement with R. Ltd. was fully disclosed in the plan and it was the bank, not the respondents, which stood to lose by that agreement.

Finally, the plan was neither unfair nor unreasonable. Only the appellants had voted against it and the court should not be astute in finding technical arguments to overcome the majority's decision. Moreover, the plan assured all priority mortgagees the full value of their security without liquidation expenses, which was more than they could have expected in the absence of the plan. Although they lost the right to pursue the petitioners for any deficiency, this right was wholly illusory given the petitioners' overwhelming debt to the bank.

**Cases considered:**

*Alabama, New Orleans, Texas & Pac. Junction Ry. Co., Re*, [1891] 1 Ch. 231 (C.A.) — referred to

*Associated Investors of Can. Ltd., Re*, [1988] 2 W.W.R. 211, 56 Alta. L.R. (2d) 259, 67 C.B.R. (N.S.) 237, 38 B.L.R. 148, (sub nom. *Re First Investors Corp. Ltd.*) 46 D.L.R. (4th) 669 (Q.B.) — referred to

*Baker & Getty Fin. Services Inc., Re*, 78 B.R. 139 (U.S. Bankruptcy Ct., N.D. Ohio, 1987) — referred to

*Br. Amer. Nickel Corp. v. O'Brien Ltd.*, [1927] A.C. 369 (P.C.) — followed

*Companies' Creditors Arrangement Act, Re; A.G. Can. v. A.G. Que.*, [1934] S.C.R. 659, [1934] 4 D.L.R. 75 — referred to

*Dairy Corp. of Can. Ltd., Re*, [1934] O.R. 436, [1934] 3 D.L.R. 347 — referred to

*Meridian Dev. Inc. v. T.D. Bank; Meridian Dev. Inc. v. Nu-West Ltd.*, [1984] 5 W.W.R. 215, 32 Alta. L.R. (2d) 150, 52 C.B.R. (N.S.) 109, 53 A.R. 39 (Q.B.) — *referred to*

*Norcen Energy Resources Ltd. v. Oakwood Petroleums Ltd.* (1988), 63 Alta. L.R. (2d) 361, 92 A.R. 81 (Q.B.) — *followed*

*Snider Bros., Re*, 18 B.R. 320 (U.S. Bankruptcy Ct., D. Mass., 1982) — *followed*

*Sovereign Life Assur. Co. v. Dodd*, [1892] 2 Q.B.D. 573 (C.A.) — *referred to*

*Wellington Bldg. Corp., Re*, [1934] O.R. 653, 16 C.B.R. 48, [1934] 4 D.L.R. 626 — *referred to*

#### **Statutes considered:**

Companies' Creditors Arrangement Act, R.S.C. 1970, c. C-25 [now R.S.C. 1985, c. C-36]

s. 20

Company Act, R.S.B.C. 1979, c. 59

ss. 276-278

Appeal from order of Trainor J. approving reorganization plan filed under Companies' Creditors Arrangement Act.

#### **McEachern C.J.B.C. (Excerpt from the transcript):**

1 We are giving an oral judgment this morning because of the commercial urgency of these appeals and because counsel's helpful arguments have narrowed the issues substantially. We are indebted to counsel for their useful submissions.

2 The petitioners (respondents on these appeals) are a number of companies (which I shall call "the companies") who have outstanding issues of secured bonds and are all engaged in real estate investment and development in Western North America and who collectively own and operate a number of office buildings and the Sandman Inn chain of hotels and motels. The appellants, Excelsior Life and National Life and Guardian Trust, are creditors of the petitioners who hold mortgages over specific properties owned by certain of the companies. They, along with eleven other lenders, are called "priority mortgagees".

3 The companies ran into financial problems starting in 1981 and by spring of 1988, the companies owed approximately \$200 million against assets of \$100 million. The major creditor, the Bank of Montreal (which I shall sometimes call "the bank"), was owed approximately \$117 million by the companies and the bank authorized the commencement of a receivership action. The bank holds security in all of the assets of the companies by way of trust deeds and bonds ranking second in priority to the security held by the priority mortgagees. Before decision in the receivership proceedings, the companies petitioned under the Companies' Creditors Arrangement Act, R.S.C. 1970, c. C-25 [now R.S.C. 1985, c. C-36] (which I shall sometimes refer to as "C.C.A.A.") for an order directing meetings of the secured and unsecured creditors to consider a proposed compromise or arrangement plan.

4 Mr. Justice Trainor, on 7th April 1988, granted the petition authorizing the companies to file a reorganization plan with the court, and that in the meantime, the companies would continue to carry on business and remain in possession of their undertaking, property and assets. Further, all proceedings against the companies were stayed. The original reorganization plan was filed on 25th August 1988. It provided that each priority mortgagee holding security over the property of the individual petitioners would constitute a separate class.

5 The petitioners obtained an order to hold a creditors' meeting on 31st October 1988 and 1st November 1988. The order provided that in addition to meetings of individual classes of creditors, there should be a later general meeting of all creditors to consider the plan. In addition, the petitioners obtained an order to file and serve the amended plan seven days before the creditors' meeting along with their information circular. Other applications were brought which dealt with notices, proxies, proof of claim forms, exchange rates and directions for the calling of meetings.

6 The amended plan was based on the following classes of creditors (descriptions of which are contained in the reasons for judgment of Trainor J. at pp. 6-7) namely:

7 — shareholder creditors

8 — A bondholders

9 — PUT debt claimants and C bondholders

10 — priority mortgagees

11 — government creditors

12 — property tax creditors

13 — general creditors

14 The amended plan also proposed consolidation of all the petitioner companies. The amended plan provided that all priority mortgagees would be grouped into one class for voting purposes. There were fifteen priority mortgagees in total, eleven of which were fully secured while the remaining four (including the appellants) faced deficiencies. The amended plan also authorized the companies to negotiate with creditors in order, if possible, to reach as much agreement as possible so that the plan would have a better chance of gaining the requisite majorities.

15 The companies and the Bank of Montreal reached a settlement agreement on 20th October 1988, dealing with (a) the amounts owing to the bank by the companies; (b) claims by the companies and others against the bank in relation to a lender liability lawsuit; and (c) the terms of a compromise between the bank and the companies. The Bank of Montreal, according to the information circular, would only realize \$32,859,005 upon liquidation. The settlement agreement between the Bank of Montreal and the companies, which is incorporated as part of the plan, provides that as of 17th January 1989, the bank is to receive the sum of \$41,650,000 in either cash or in cash plus properties. A copy of this agreement was provided to creditors, along with such other documents including a notice of the meetings, the reorganization plan, and an extensive information circular.

16 The class meetings and the general meetings of creditors were held in Vancouver on 31st October and 1st November 1988. All classes of creditors voted unanimously in favour of the plan except the priority mortgagee

class. This class approved the plan by the requisite majority pursuant to the provisions of the C.C.A.A., that is, a simple majority of creditors in the class holding at least 75 per cent of the debt voting in favour of the plan. 73.3 per cent of the priority mortgagees holding 78.35 per cent of the debt voted in favour of the plan.

17 Relax Development Corporation Ltd., a priority mortgagee facing a deficiency, voted in favour of the plan. If Relax had not voted in favour of the plan, the companies would not have obtained the requisite majority from the priority mortgagee class. Prior to the settlement with the bank, Relax struck an agreement with the companies on the value of its security amounting to about \$900,000 over an appraisal value which was in dispute. Relax agreed in the settlement to vote in favour of the plan. More about that later.

18 The appellants on these appeals voted against the plan, and raised objections that the plan improperly put all priority mortgagees into one class, and also that the plan preferred some creditors over others. They allege that the net effect of the plan on the fully secured priority mortgagees is different than that on the mortgagees facing deficiencies, in that the plan reduces the amount of debt owed to the mortgagees facing deficiencies to the market value of the subject property of their respective security, and required assignment of the deficiency for \$1. They lose the right to obtain an order absolute of foreclosure pursuant to their security. On the other hand, the fully secured priority mortgagees recover the entire amount of their indebtedness.

19 The appellants Excelsior and National are secured creditors of the petitioner, Northland Properties Ltd., one of the companies. They hold a first mortgage jointly over an office tower in Calgary adjacent to the Calgary Sandman Inn. Both buildings share common facilities. The principle amount of the debt owing to Excelsior and National as of 26th October 1988, is \$15,874,533 plus interest of \$311,901. The market value of the office tower as of 13th May 1988 was stated to be \$11,675,000. They, therefore, face a potential deficiency of \$4,512,434.

20 Guardian Trust is a secured creditor of the petitioner, Unity Investment Company Limited, and holds a first mortgage over a small office building in Nelson, British Columbia. The amount owing to Guardian is \$409,198.46 and the estimated deficiency is approximately \$150,000 exclusive of transaction costs.

21 Mr. Justice Trainor, on 12th December 1988, found that the companies had complied with the provisions of the C.C.A.A., and, therefore, the court could exercise its discretion and sanction the reorganization plan. Excelsior and National and Guardian appeal against that decision.

22 Mr. Justice Trainor had the carriage of this matter almost from the beginning and he heard several preliminary applications. In a careful and thorough judgment, he set out the facts distinctly, reviewed the authorities and approved the plan. I do not propose to review the authorities again because they are extensively quoted in nearly every judgment on this subject. It will be sufficient to say that they include *Re Companies' Creditors Arrangement Act*; *A.G. of Can. v. A.G. Que.*, [1934] S.C.R. 659, [1934] 4 D.L.R. 75; *Meridian Dev. Inc. v. T.D. Bank*; *Meridian Dev. Inc. v. Nu-West Ltd.*, [1984] 5 W.W.R. 215, 32 Alta. L.R. (2d) 150, 52 C.B.R. (N.S.) 109, 53 A.R. 39 (Q.B.); *Re Associated Investors of Can. Ltd.*, [1988] 2 W.W.R. 211, 56 Alta. L.R. (2d) 259, 67 C.B.R. (N.S.) 237, 38 B.L.R. 148, (sub nom. *Re First Investors Corp. Ltd.*) 46 D.L.R. (4th) 669 (Q.B.); *Re Alabama, New Orleans, Texas & Pac. Junction Ry. Co.*, [1891] 1 Ch. 231 (C.A.); *Re Dairy Corp. of Can. Ltd.*, [1934] O.R. 436, [1934] 3 D.L.R. 347; *Re Wellington Bldg. Corp.*, [1934] O.R. 653, 16 C.B.R. 48, [1934] 4 D.L.R. 626; *Br. Amer. Nickel Corp. v. O'Brien Ltd.*, [1927] A.C. 369 (P.C.); *Sovereign Life Assur. Co. v. Dodd*, [1892] 2 Q.B.D. 573 (C.A.), and others.

23 The authorities do not permit any doubt about the principles to be applied in a case such as this. They are set out over and over again in many decided cases and may be summarized as follows:

24 (1) There must be strict compliance with all statutory requirements (it was not suggested in this case that the statutory requirements had not been satisfied);

25 (2) All material filed and procedures carried out must be examined to determine if anything has been done which is not authorized by the C.C.A.A.;

26 (3) The plan must be fair and reasonable.

27 Similarly, there can be no doubt about the purpose of the C.C.A.A. It is to enable compromises to be made for the common benefit of the creditors and of the company, particularly to keep a company in financial difficulties alive and out of the hands of liquidators. To make the Act workable, it is often necessary to permit a requisite majority of each class to bind the minority to the terms of the plan, but the plan must be fair and reasonable.

28 There were really four issues argued on this appeal but, as is so often the case, there is some overlapping. I shall attempt to deal with them individually.

29 First it was alleged, principally by Mr. Czepil, that the Act does not authorize a plan whereby the creditors of other companies can vote on the question of whether the creditors of another company may compromise his claim. He called this the cross-company issue.

30 This argument arises out of the particular facts that Mr. Czepil's client found itself in where it had a first mortgage, that is, Guardian had a first mortgage on a building owned by Unity which was the only asset of Unity, and he says the C.C.A.A. does not permit creditors of other companies to vote on the disposition of Guardian's security. I think there would be considerable merit in this submission except for the fact that the plan contemplates the consolidation of all the petitioner companies and the applications are made in this case not just under the C.C.A.A., but also under ss. 276-78 of the British Columbia Company Act, R.S.B.C. 1979, c. 59. In this respect, it is necessary to mention s. 20 of the C.C.A.A. which provides:

31 20. The provisions of this Act may be applied conjointly with the provisions of any Act of Canada or of any province, authorizing or making provision for the sanction of compromises or arrangements between a company and its shareholders or any class of them.

32 During the argument of these appeals, we were treated to a review of the history of this matter in the court below. In reasons for judgment dated 5th July 1988 [now reported *Re Northland Properties Ltd.* (1988), 29 B.C.L.R. (2d) 257, 69 C.B.R. (N.S.) 266], Mr. Justice Trainor recited that he had been asked by some of the parties to approve a consolidation plan, but he declined to do so as the plan was not then before him in final form. It is implicit that Trainor J. thought he had authority to approve a consolidation plan and he referred to American authorities particularly, *Re Northland Properties Ltd.* [B.C.] Trainor J. 219 *Re Baker & Getty Fin. Services Inc.*, 78 B.R. 139 (U.S. Bankruptcy Ct., N.D. Ohio, 1987), and in *Re Snider Bros.*, 18 B.R. 320 (U.S. Bankruptcy Ct., D. Mass., 1982), and he said that he accepted the analysis of *Snider*, which proposes the test between economic prejudice of continued debtor separateness versus the economic prejudice of consolidation, and holds that consolidation is preferable if its economic prejudice is less than separateness prejudice.

33 I think Mr. Justice Trainor was right for the reasons described in the American authorities and because to hold otherwise would be to deny much meaning to s. 20 of the C.C.A.A. and would mean that when a group of companies operated conjointly, as these companies did (all were liable on the Bank of Montreal bonds), it would

be necessary to propose separate plans for each company and those plans might become fragmented seriously.

34 I am satisfied there is jurisdiction to entertain a consolidation proposal.

35 Secondly, it was agreed that the composition of the class of priority creditors was unfair by reason of including all priority mortgagees without regard to the fact that some of them faced a deficiency and some did not. The appellants were each in the latter difficulty and they argue that they should have been placed in a different class because the other 11 priority mortgagees were going to get paid in full whether the plan was approved or not. This argument would have more merit if the plan were only for the benefit of the undersecured priority mortgagee. But the plan was also for the benefit of the company and the other creditors who, by their votes, indicated that they thought the plan was in their best interest. The learned chambers judge considered this question carefully. At p. 25 of his reasons he said this:

36 An examination of the relationship between the companies and the priority mortgagees satisfies me that they are properly in the same class. The points of similarity are:

37 1. The nature of the debt is the same, that is, money advanced as a loan.

38 2. It is a corporate loan by a sophisticated lender who is in the business and aware of the gains and risks possible.

39 3. The nature of the security is that it is a first mortgage.

40 4. The remedies are the same — foreclosure proceedings, receivership.

41 5. The result of no reorganization plan would be that the lender would achieve no more than the value of the property, less the costs of carrying until disposal, plus the legal costs as well would come out of that. A possible exception would be if an order absolute left the creditor in the position of holding property for a hoped-for appreciation in value.

42 6. Treatment of creditors is the same. The term varied to five years, the interest rates 12 per cent or less, and the amount varied to what they would get on a receivership with no loss for costs; that is, it would be somewhat equivalent to the same treatment afforded to the Bank of Montreal under the settlement agreement.

43 The points of dissimilarity are that they are separate priorities and that there are deficiencies in value of security for the loan, which vary accordingly for particular priority mortgagees. Specifically with respect to Guardian and Excelsior, they are both in a deficiency position.

44 Now, either of the reasons for points of dissimilarity, if effect was given to them, could result in fragmentation to the extent that a plan would be a realistic impossibility. The distinction which is sought is based on property values, not on contractual rights or legal interests.

45 I agree with that, but I wish to add that in any complicated plan under this Act, there will often be some secured creditors who appear to be oversecured, some who do not know if they are fully secured or not, and some who appear not to be fully secured. This is a variable cause arising not by any difference in legal interests, but rather as a consequence of bad lending, or market values, or both.

46 I adopt, with respect, the reasoning of Forsyth J. of the Court of Queen's Bench of Alberta, in a recent unreported decision in *Norcen Energy Resources Ltd. v. Oakwood Petroleum Ltd.*, No. 8801-14453, 17th November 1988 [now reported 63 Alta. L.R. (2d) 361, 92 A.R. 81], particularly at pp. 13 and 14 [pp. 369-70]. I am unable to accede to this ground of appeal.

47 Thirdly, I pause to mention that it was not suggested that the arrangement with the Bank of Montreal constituted a preference. It was argued, however, that the entire plan was tainted by the agreement made by the companies with Relax. Apparently, there was an appraisal showing a value of its security at \$3.7 million while other evidence suggests a value of between \$4.5 million to \$4.6 million. The amount owing to Relax on its mortgage was \$6 million.

48 Early in the history of this matter before the plan was finalized, and before the companies struck their crucial arrangement with the Bank of Montreal, the companies and Relax agreed to a future cash payment of \$500,000 and a valuation of \$4 million for the Relax property which could, in total, amount to a preference of up to \$900,000 to Relax and that company, in consideration of that compromise, agreed to vote for the plan.

49 It should be mentioned that the plan, from its inception, ensured to the priority mortgagees the full market value of their security to be determined either by agreement, appraisal, or, if necessary, arbitration. Thus, the appellants do not stand to lose anything by the agreement made with Relax. It is the bank which carried the burden of that expense.

50 There is no doubt that side deals are a dangerous game and any arrangement made with just one creditor endangers the appearance of the bona fides of a plan of this kind and any debtor who undertakes such a burden does so at considerable risk. In this case, however, it is apparent that this agreement was not made for the purpose of ensuring a favourable vote because at the time the deal was struck the companies had not reached an accommodation arrangement with the bank. I think the companies were negotiating, as businessmen do, on values for the purpose of putting a plan together.

51 Further the arrangement with Relax was fully disclosed in the plan. This does not ensure its full absolution if it was improper, but at least it removes any coloration of an underhanded or secret deal. In fact, there were also negotiations between the companies and the appellants but nothing came of those discussions.

52 After referring to the fact that the plan anticipated and permitted negotiations about values and other matters, the learned chambers judge said this at pp. 28 and 29 of his reasons:

53 The negotiations might, on the surface, appear to have been in the nature of an excessive payment to Relax for the consideration in their agreement, which agreement, incidentally, included an undertaking to vote in favour of the plan. But the answer given by the companies is that what in effect was happening at that meeting was a negotiation as to the agreed price and that this negotiation took place earlier rather than later and that the parties in fact came to an accord with respect to the agreed price and that the settlement between them was on that basis.

54 If that is so, it is something which took place in accordance with what is proposed by the reorganization plan. I have reviewed and reread a number of times the submissions by the companies and particularly by counsel on behalf of Guardian and Excelsior. I am satisfied that I should accept the explanation as to what took place, which has been advanced on behalf of the companies.

55 In the circumstances of this case, I would not disagree with the learned chambers judge in that connection.

56 Lastly, it remains to be considered whether the plan is fair and reasonable. I wish to refer to three matters.

57 First, the authorities warn us against second-guessing businessmen (see *Re Alabama*, supra, at p. 244). In this case, the companies and their advisors, the bank and its advisors, and all the creditors except the two appellants, voted for the plan. As the authorities say, we should not be astute in finding technical arguments to overcome the decision of such a majority.

58 Secondly, I wish to mention Mr. Czepil's argument that the plan was unfair, perhaps not conceptually, but operationally by authorizing negotiations. He says this put the parties in a difficult position when it came to vote because they risked retribution if they failed to reach agreement and then voted against the plan. He complains that some benefits offered in negotiations are no longer available to his clients.

59 With respect, negotiations between businessmen are much to be desired and I would not wish to say anything that would impede that salutary process. If negotiations lead to unfairness, then other considerations, of course, arise. But that, in my view, is not this case.

60 Thirdly, the plan assures all the priority mortgagees the full market value of their security without liquidation expenses. That is more than they could expect to receive if there had been no plan.

61 What they gave up is the right to take the property by order absolute or to seek a judicial sale and pursue the borrower for the deficiency. Guardian was actually offered its security but declined to accept it. The difficulty about this whole matter is the uncollectability of the deficiency having regard to the overwhelming debt owed to the bank which would practically eliminate any real chance of recovery of the deficiency.

62 In my view, the obvious benefits of settling rights and keeping the enterprise together as a going concern far outweigh the deprivation of the appellants' wholly illusory rights. In this connection, the learned chambers judge said at p. 29:

63 I turn to the question of the right to hold the property after an order absolute and whether or not this is a denial of something of that significance that it should affect these proceedings. There is in the material before me some evidence of values. There are the principles to which I have referred, as well as to the rights of majorities and the rights of minorities.

64 Certainly, those minority rights are there, but it would seem to me that in view of the overall plan, in view of the speculative nature of holding property in the light of appraisals which have been given as to value, that this right is something which should be subsumed to the benefit of the majority.

65 I agree with that.

66 I also agree with the learned chambers judge that the plan should have been approved and I would dismiss these appeals accordingly.

***Esson J.A.:***

67 I agree.

***Wallace J.A.:***

68 I agree.

***McEachern J.A.:***

69 The appeals are dismissed with costs.

*Appeal dismissed.*

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