SUPERIOR COURT OF JUSTICE

COUNSEL SLIP/ENDORSEMENT

COURT FILE NO.: BK-22-2875614-0031 **DATE:** 28 November 2022

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TITLE OF PROCEEDING: **CannTrust Holdings Inc. v. Ernst & Young Inc**

BEFORE JUSTICE: **Osborne**

For Plaintiff, Applicant, Moving Party, Crown:

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ENDORSEMENT OF JUSTICE OSBORNE:

1. CannTrust Holdings Inc. ["CannTrust"] seeks various heads of relief on this motion, including approval of a Proposal, Articles of Reorganization, an order that CannTrust is not required to call an annual general meeting of shareholders before dissolving, and related relief.
2. The motion is unopposed, and is supported by the Proposal Trustee. However, in the unusual circumstances of this case and given its lengthy procedural history, it is necessary to set out in some detail the background to, and the basis for, the motion and the relief sought. Defined terms in this endorsement have the meaning given to them in the motion materials and factum of CannTrust unless otherwise noted.

3. CannTrust relies on the affidavit of Greg Guyatt sworn November 17, 2022, and Exhibits "A" through "N" thereto, together with the Second Report of the Proposal Trustee dated November 18, 2022 and Appendices "A" through "J". While I have not summarized in this endorsement all of the facts set out in that affidavit, I have reviewed all of the material.
4. CannTrust and related entities operated collectively as a licensed cannabis producer, the shares of which traded on the Toronto and New York stock exchanges.
5. Following the suspension by Health Canada of its cannabis licences for the cultivation and storage of cannabis in a manner contrary to applicable laws, CannTrust ceased sales and production. Individual as well as securities class actions were commenced in Canada and the United States. The auditor withdrew its 2018 audit report and the company has not filed financial statements since May, 2019.
6. A Cease Trade Order was issued by the Ontario Securities Commission on April 13, 2020 for the failure to file periodic disclosure as required by Ontario securities legislation. The CannTrust common shares were subsequently delisted from both stock exchanges.
7. CannTrust was and is insolvent. It had previously been the subject of a restructuring process conducted under the CCAA, commencing on March 31, 2020. A Plan of Arrangement under the CCAA was implemented on January 5, 2022 which, among other things, settled the actions referred to above and provided for the establishment of a trust to which cash contributions were made for the benefit of Securities Claimants, the payment in full of General Unsecured Claims and the release of CannTrust from Released Claims [all as defined in the. The existing CannTrust Common Shares, however, remained outstanding.
8. While the CCAA Plan addressed substantially all of the liabilities of CannTrust, it did not provide for new financing necessary for the continued operation of the business of the group conducted primarily by CannTrust Inc., the operating entity ["Opco"].
9. Today, CannTrust remains insolvent and has concluded that it is appropriate to wind up its operations by way of:
    a. paying in full its few remaining unsecured creditors other than Phoena Holdings Inc. ["Phoena"] and its subsidiaries;
    b. distributing to its shareholders its 10% equity interest Phoena and transferring its Residual Assets [defined in the affidavit of Mr. Guyatt at paragraph 47 and consisting essentially of a potential HST refund claim, potential residual value from the directors and officers trust and other unsecured indebtedness] to Phoena in satisfaction of its liabilities to Phoena and its subsidiaries; and
    c. once those steps are completed, dissolving.
10. This requires, as noted in paragraph one above, approval of the Proposal, approval of Articles of Reorganization which would in turn set out the terms for the distribution of the Phoena shares to the shareholders of CannTrust in an efficient manner, and authorize the directors of CannTrust to consent to its dissolution.
11. The relief sought today effectively facilitates that multi-step process.
12. The unusual nature of the relief sought arises out of the dual realities of there being virtually no cash available to fund any of the steps that might typically be required to effect the objectives sought, and the absence of any viable or more favourable alternatives.
13. As explained in more detail below, all creditors will either be paid in full or have consented to the relief sought. While shareholder approval has not been obtained, CannTrust emphasizes that no shareholder is prejudiced in any event, it in the sense that it is or will be in a worse position than if the relief is not granted.
14. CannTrust has limited assets consisting of minimal Residual Assets and a 10% equity interest in Phoena.
15. Phoena, in turn, owns all of the issued and outstanding common shares of Phoena Inc. which is the successor to Opco. Phoena, which is effectively an intermediate holding company, had been inserted between CannTrust and Opco prior to implementation of the CCAA Plan but pursuant to Court approval.

16. CannTrust's liabilities, on the other hand, exceed materially the value of its assets and consist principally of secured obligations as a guarantor of secured credit facilities provided to Opco, Phoena, and amounts owing to service providers and the Proposal Trustee and its counsel.
17. By previous orders of this Court, the deadline for CannTrust to call an annual general meeting ["AGM"] was extended to November 30, 2022. Given the other relief it is seeking, CannTrust seeks an order that it not be required to call an AGM prior to its dissolution.
18. Following emergence from protection under the CCAA, CannTrust hoped and intended to complete the necessary steps to either hold an AGM and then apply to the Ontario Securities Commission to revoke the previously imposed Cease Trade Order; or distribute the Phoena shares to its shareholders pursuant to plan of arrangement following which Phoena would subsequently seek a listing on a stock exchange for its common shares.
19. Obtaining a revocation of the Cease Trade Order would require CannTrust to restate certain historical audited financial statements and prepare other annual audited and interim unaudited financial statements.
20. However, its independent auditor advised following emergence from CCAA protection that the required financial statements would not be completed for an AGM to be called by the extended deadline of July 13, 2022. That deadline was further extended to November 30, 2022 by the order of Penny, J. dated July 7, 2022.
21. Regrettably, CannTrust has concluded that notwithstanding the successive extensions, it is not feasible to complete the necessary financial statements, obtain an audit opinion and hold the annual general meeting by the date required.
22. As submitted by the company, the more fundamental problem is that it remains insolvent and lacks the cash resources to complete the audit another necessary work or complete the steps necessary to seek the revocation of the Cease Trade Order. As stated in the Second Report of the Proposal Trustee, CannTrust's cash on hand as of November 4, 2022 is only $3,195. Simply put, it lacks the funds necessary to implement any of the steps that would typically be undertaken, beginning with the completion of the work necessary to issue audited financial statements.
23. That situation will not change: CannTrust is a holding company without operating revenues and has been operating at a loss for a significant period of time.
24. At the commencement of the BIA proceedings, its liabilities exceeded $25 million. Given that its remaining assets are limited, and consist only of the shares in Phoena and the Residual Assets, CannTrust determined that the Proposal and ancillary relief would facilitate an efficient and orderly wind down.
25. Accordingly, the Proposal contemplates that CannTrust will deposit sufficient funds with the Proposal Trustee to fund all of the cash payments and distributions contemplated by the terms of the Proposal. Preferred Claims, if any, will be paid in full, as will Unsecured Claims [other than claims of Phoena and subsidiaries]. Those claims of Phoena and its subsidiaries will also be satisfied in full albeit by the transfer of the Residual Assets or proceeds therefrom, to Phoena.
26. As noted at the outset of this Endorsement, the Proposal does not affect the Secured Claims, and each of the secured creditors has consented to the Proposal and agreed to release its guarantees and security to facilitate the implementation of the Proposal [this includes Cortland and the Investor Lenders].
27. Upon implementation of these steps, CannTrust will no longer have any liabilities, nor any assets save for the shares in Phoena. Those will, as noted above then be distributed to its shareholders, subject, however, to the following:
    a. only those shareholders of CannTrust holding at least 10,000 Common Shares will qualify for a distribution of the shares of Phoena;
    b. any distribution of shares of Phoena to a shareholder of CannTrust who is a person that is not Canadian or a U.Ss person will be subject to the company obtaining an opinion from qualified and independent securities counsel that such a distribution is exempt from any requirement for a prospectus;

c. no distribution will be made to a shareholder that holds their Common Shares of CannTrust in any registered retirement savings plan or other registered savings vehicle for which the shares of Phoena do not qualify as a permitted investment or a "qualified investment" within the meaning of the *Income Tax Act (Canada)*, as applicable;
d. the distribution will be made on account of capital; and
e. any shares of Phoena not so distributed will be returned to Phoena for cancellation without payment.

28. Not unexpectedly, all of this requires an amendment of the articles of incorporation of CannTrust in accordance with the Articles of Reorganization.
29. The motion materials described, and counsel for the company directed the Court in submissions to, the steps in the process underlying the Proposal.
30. The original Proposal was filed with the Official Receiver on October 18, 2022 by which filing these proceedings were commenced. The next day, CannTrust issued a press release to give notice to creditors, shareholders and others that it had commenced proposal proceedings pursuant to the BIA, and generally describing the terms of the Proposal.
31. An amended and restated Proposal was filed on November 3, 2022 which sought to clarify certain issues and provide for increased flexibility with respect to the timing of the dissolution of the company [this, to minimize the risk of a loss of opportunity to pursue an HST refund upon dissolution].
32. The first amended and restated Proposal was accepted, unanimously, by the creditors at a meeting of November 4, 2022. That result was announced by press release on November 16, 2022, which press release also provided general notice to creditors, shareholders and others of the hearing today. I observe that this press release, found in the record at Exhibit "L" to the affidavit of Mr. Guyatt, expressly refers to the exceptions to the distribution of the Phoena shares described above. Moreover, that press release advised any interested party that if they wished further information, such was available on the website of the Proposal Trustee and they had the right to appear at the hearing today and/or contact the Proposal Trustee for further information.
33. CannTrust proposes to make certain further clarifying amendments to the Proposal, all as contemplated in section 7.2 thereof, which section provides for amendments after the meeting of creditors so long as the consent of the Proposal Trustee and approval of this Court is obtained.
34. Those further amendments correct an error in the number of outstanding Common Shares as defined in the Proposal and add further clarifying details relevant to the distribution of the shares of Phoena to shareholders of CannTrust. A summary of those further amendments was included in the press release of November 16, 2022 described above.
35. As against that background, CannTrust seeks today relief that effectively would approve the Proposal [including proposed amendments and contemplated transactions]; approve the Articles of Reorganization; and relieve the company from the requirement to hold an annual general meeting [required by the terms of the current order to be held within two days].
36. This Court has the discretion to approve or refuse to approve a proposal, pursuant to section 60(5) of the BIA. Refusal to approve a proposal is mandatory if the Court is of the opinion that the terms of the proposal are not reasonable or are not calculated to benefit the general body of creditors.
37. In *Re Kitchener Frame Ltd*., 2012 ONSC 234, Morawetz, J. (now Chief Justice Morawetz) described the factors that must be satisfied in determining whether to grant approval of a proposal:
    a. the terms of the proposal are reasonable;
    b. the terms are calculated to benefit the general body of creditors; and
    c. the proposal is made in good faith. (see para.19).
38. The first two of those three factors flow directly from the statutory provision. The requirement that the proposal be made in good faith flows, as noted by the Court in *Kitchener Frame*, from the exercise by this Court of equitable jurisdiction which in turn generally requires that the Court take into account the

interests of the debtor, the interests of the creditors and the interests of the public at large in the integrity of the bankruptcy system. (See *Re Kitchener*, para. 20).

39. I agree. While the interests of the affected stakeholders are obviously central, there is also a broader interest at stake that transcends the individual interests of those parties. The underlying circumstances are such that the rights are necessarily being affected, through and pursuant to the BIA regime. It follows, therefore, that it is only logical that in approving a proposal, the Court be satisfied that it is made in good faith.
40. As to whether a proposal is reasonable, does it have a reasonable possibility of being successfully completed? Does it meet the requirements of commercial morality and maintain the integrity of the bankruptcy system? (See *Re Abou-Rached*, 2002 BCSC 1022 at paras. 65-66).
41. I am satisfied that the Proposal here is reasonable. It has the unanimous support of the secured creditors. It provides for the payment in full of all unsecured creditors [other than Phoena and its subsidiaries]. All of the liabilities of CannTrust to Phoena are satisfied on terms to which those parties consent. It provides for a distribution of the shares of Phoena to CannTrust shareholders in circumstances where they would otherwise recover nothing, subject to certain caveats discussed below. Finally, it facilitates the wind-down and dissolution of CannTrust thereby minimizing ongoing costs when, practically, it lacks the cash resources even to comply with the reporting requirements of the OBCA and applicable securities laws.
42. The proposed amendments to the Proposal do not change this analysis because they do not affect the treatment of creditors, but rather clarify the terms governing the distribution of the shares of Phoena to CannTrust shareholders.
43. I am also of the view that the terms of the Proposal contemplating the release of claims against Directors is authorized by section 50(13) of the BIA. That provision permits a compromise of claims against directors related to the obligations of the corporations where the directors are by law liable in their capacity as directors for the payment of such. I observe that the Proposal Trustee, as is its statutory duty under section 50(10)(b) of the BIA, has reported that it is not aware of any transactions that may be preferential.
44. For the same reasons, I am satisfied that the Proposal and its terms are calculated to benefit the general body of creditors [and in fact do benefit them]. The Proposal addresses every creditor: it either pays them in full or has their consent.
45. Finally, I am satisfied that the Proposal is made in good faith. It enjoys the support of the Proposal Trustee and, as noted, the consent of every creditor who is not otherwise paid in full.
46. The good faith analysis is informed by a consideration of the alternatives, in the event that the Proposal is not approved. CannTrust would be in breach of its statutory obligations for failing to prepare and file audited financial statements or hold an annual general meeting and would be completely unable to address in any way its remaining liabilities, or dispose of its Residual Assets and dissolve in an orderly way. Chaos is not to the benefit of any stakeholder.
47. I am cognizant of the fact noted above that not every shareholder will benefit by way of a distribution of the shares of Phoena. Specifically, those shareholders who hold fewer than 10,000 Common Shares in CannTrust, or who hold their shares through a registered savings plan or other registered savings vehicle for which the shares of Phoena do not qualify as a permitted investment or a "qualified investment" within the meaning of the *Income Tax Act (Canada)*, will not receive a distribution. Nor will distributions be made in jurisdictions for which there is not a prospectus exemption. Is the Proposal still reasonable and made in good faith? In my view, it is.
48. The Common Shares of CannTrust have no economic value today. Therefore, not only do shareholders lack any legal right to oppose a proposal, the value of what they hold today is nil in any event. The restrictions on the distribution are required to make the distribution economically rational, and therefore reasonable.
49. To provide for a distribution to shareholders with holdings below the threshold of 10,000 shares would create a situation where distribution costs would materially exceed the value of the shares of Phoena

being distributed. The Common Shares of CannTrust were issued at a price of approximately $0.009 per share at the time Phoena completed the Investment Transaction in March, 2022, with the necessary implication that the value of the threshold of 10,000 shares was $90 (See Guyatt Affidavit, para. 56).

50. While the value of the CannTrust Common Shares today is nil, the $90 value of the threshold March of this year gives comfort with respect to the order of magnitude of the shareholdings held by those not entitled to a distribution pursuant to the terms of the Proposal. It informs and supports the position of the company that the distribution costs below such a threshold would make the entire distribution uneconomic. The result of that would not be to benefit those shareholders whose holdings are below the threshold, but rather to simply prevent all of those other shareholders above the threshold from recovering anything.
51. The proposed Articles of Reorganization would effect these restrictions since it is, as submitted by CannTrust, neither reasonable nor practical to seek shareholder approval for the existing articles. Courts have previously held in the context of an insolvency that it is not necessary to provide a vote to shareholders who have no economic interest in a debtor. (See *Unique Broadband Systems, (Re)*, 2013 ONSC 676 at para. 54). I observe that neither section 59(4) of the BIA nor section 186 of the OBCA requires a shareholder vote.
52. All of this is consistent with the approach of the Alberta Court of Queen's Bench in *Re Canadian Airlines Corp*., 2000 ABQB 442 at para. 143-145, cited with approval by this Court in *Re Stelco*, 2006 CanLII 1773 at para. 15:

> Where a company is insolvent, only the creditors maintain a meaningful stake in its assets. Through the mechanism of liquidation or insolvency legislation, the interests of shareholders are pushed to the bottom rung of the priority ladder. The expectations of creditors and shareholders must be viewed and measured against an altered financial and legal landscape. Shareholders cannot reasonably expect to maintain a financial interest in an insolvent company where creditors' claims are not being paid in full. It is through the lens of insolvency that the court must consider whether the acts of the company are in fact oppressive, unfairly prejudicial or unfairly disregarded. CCAA proceedings have recognized that shareholders may not have "a true interest to be protected" because there is no reasonable prospect of economic value to be realized by the shareholders given the existing financial misfortunes of the company: Royal Oak Mines Ltd., supra, para. 4., Re Cadillac Fairview Inc., [1995] O.J. No. 707, (March 7, 1995), Doc. B28/95 (Ont. Gen. Div. [Commercial List]), and T. Eaton Company, supra….

53. The same approach was taken in *Peloton Pharmaceuticals Inc*., 2017 QCCS 1165, where two groups of minority shareholders opposed the approval of a proposal pursuant to the BIA, as well as a reorganization pursuant to section 191 of the CBCA. The court in that case held that only the creditors maintained a meaningful stake in the assets as the lack of interest of the minority shareholders was clear: their shares had no value since the insolvency of the debtor was uncontested.
54. Again, CannTrust remains insolvent today with the result that its Common Shares have no economic value. I am satisfied that the only route to achieve any value to distribute, according to the terms of the Proposal, is through Court approval of both the Proposal and the Articles of Reorganization.
55. This is so for a number of reasons. Since the company is insolvent, it cannot make distributions to its shareholders as to do so would violate section 38(3) of the OBCA which prohibits the payment of dividends and other shareholder distributions when such would lead the corporation to be unable to pay its liabilities as they become due, or the realizable value of the corporation's assets would thereby be less than the aggregate of its liabilities and it stated capital of all classes.
56. The sequence of the steps of the Proposal, when implemented, will be such that the company will no longer be insolvent when the distribution is made.
57. In much the same way, CannTrust cannot distribute, pursuant to applicable securities laws, the shares of Phoena without qualifying the distribution with a prospectus or relying on an available exemption. When the distribution is made in connection with the Proposal in this insolvency proceeding, however,

such an exemption is available to shareholders in Canada pursuant to section 2.11 of National Instrument 45 – 106 - Prospectus Exemptions.

58. For shareholders in the United States, the *United States Securities Act of 1933* provides a not dissimilar exemption from registration. It applies to securities issued, other than for cash under or in connection with an arrangement or proposal where the terms and conditions are approved by a court expressly authorized to grant such approval, after a hearing on the substantial of and procedural fairness of such terms and conditions at which all persons to whom the securities are proposed to be issued have the right to appear and receive timely notice of the hearing. I am satisfied that today's hearing, in this Court, is such a hearing as contemplated.
59. Finally, and as noted above, the Proposal provides for and contemplates the dissolution of CannTrust. Section 237 of the OBCA requires shareholder approval for a voluntary dissolution, by special resolution or written consent. That is neither feasible nor practical here for the reasons noted above. The proposed amendment to the articles of incorporation, provided for in the terms of the Articles of Reorganization, allow any director to consent to the dissolution on behalf of the shareholders. I am satisfied that approval of the Articles of Reorganization is appropriate here.
60. That leaves the requirement to hold an annual general meeting, which the company is completely unable to do in the circumstances, either by the required deadline of November 30, or at all prior to its dissolution.
61. Justice Penny of this Court previously extended the deadline for the calling of the annual general meeting, based on the inherent jurisdiction of the Court and the statutory jurisdiction found in section 11 of the CCAA. The decision of Justice Penny is informative here, notwithstanding that it clearly applied to a request for an extension of the time within which a meeting was required to be called, rather than circumstances where the meeting requirement was sought to be dispensed with altogether prior to dissolution.
62. However, in my view, the same factors and analysis ought to apply, and this Court ought to consider whether it is just and equitable to grant the relief sought, since the ultimate objective is to balance the interests of the Company against any meaningful risk of harm to the shareholders arising from the granting of an extension or relief from the requirement to hold the meeting. (See *IMAX Corp., Re*, 2007 CarswellOnt 8860 (ONSC) at para. 23).
63. In his decision earlier in this proceeding, Justice Penny observed that CannTrust is governed by the OBCA which, unlike the CBCA, has not been amended to close the "perceived functional gap" by including a provision expressly allowing a corporation to obtain an extension to the deadline for calling an AGM. Justice Penny further noted that Ontario courts have exercised their inherent jurisdiction to fill functional gaps in corporate legislation in many cases, and have exercised their jurisdiction to extend the time for the calling of a meeting where it is just and equitable to do so. The courts can and do look to the principles developed by other courts under other statutory regimes. (See Endorsement of Penny, J., July 7, 2022).
64. At the end of the day, the practical yet inevitable fact is that CannTrust lacks the financial resources to call an annual general meeting and facilitate a vote of shareholders for dissolution. The Proposal, while requiring according to its terms relief from these requirements, includes those very requirements to affect the result that is otherwise unachievable: the realization of some value for CannTrust shareholders [subject to the exceptions noted above] in the form of a distribution of the shares in Phoena.
65. Moreover, and as noted above, the shareholders would not have the right to defeat a proposal supported by all creditors even if a meeting were held and the shareholders voted against it. I am therefore satisfied that there is no prejudice in granting the relief sought, that it is appropriate, just and equitable, and that the general statutory jurisdiction in section 11 of the CCAA permits the relief in these unusual circumstances.
66. The practical effect of denying the relief sought in respect of amending the articles to authorize a dissolution by one director is the same whether a meeting of shareholders were not required to be held

[as the company seeks here] or whether the meeting was held and the resolution defeated. In either event, the only practical result is a negative one: such a result would deprive the shareholders [again subject to the exceptions noted above] from realizing the value in the distribution of the 10% of the Phoena shares, yet no shareholder or other stakeholder would be better off.

67. The Proposal provides for the realization of some value in challenging circumstances. The alternative, if the Proposal is not approved, is that no value will be realized by any shareholders.
68. For all of the above reasons, I am satisfied that all of the relief sought is, in these unique circumstances, just and equitable and should be granted.
69. Order to go in the form signed by me today, which order is effective without the necessity of issuing and entering.