SUPERIOR COURT OF JUSTICE

COUNSEL/ENDORSEMENT SLIP

COURT FILE NO.: CV-24-724693-00CL **DATE: October 31, 2024**

NO. ON LIST: 1

TITLE OF PROCEEDING: VBI VACCINES INC. v ERNEST & YOUNG INC. et al.

BEFORE: JUSTICE PENNY

PARTICIPANT INFORMATION

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REASONS OF JUSTICE PENNY (Released November 1, 2024):

[1] On October 31, 2024, I granted the applicant's motion in these proceedings with reasons to follow. These are the reasons.

[2] This is an international insolvency proceeding with CCAA proceedings in Ontario and recognition proceedings in the U.S. and Israel. VBI is in the business of developing and producing new vaccines.

[3] The present motion is for approval of a sale (the credit bid of the first in priority secured lender and DIP lender, K2 Health Ventures) using a reverse vesting order structure and for various other collateral relief, including releases and the ability to sell other residual assets up to a maximum value of $5 million without further court approval.

[4] The acquisition agreement and transaction for which approval is sought represents the culmination of a lengthy solicitation process which includes a prefiling process as well as the court-approved and Monitor-supervised process in these proceedings.

[5] Solicitation material was sent to 235 potential bidders. There were three non-binding letters of intent by the bid deadline. The deadline was extended several times. One more non-binding letter of intent was received. The applicant's board, in consultation with the Monitor, determined that only the K2 credit bid should proceed to phase two. The board, again in consultation with the Monitor, ultimately determined that the K2 bid should be accepted.

[6] The transaction is structured to require a reverse vesting order. K2 will acquire new shares in the applicant. Existing shares will be extinguished. Certain liabilities and assets will be assigned to a new corporation, Residualco, which will ultimately be declared bankrupt.

[7] The jurisdiction to approve a transaction implemented through an RVO structure is found in s. 11 of the CCAA, which gives the court broad powers to make any order it thinks fit.

[8] The remedy of an RVO is extraordinary relief, not granted merely for the convenience of a purchaser or other party. An RVO changes centuries of corporate law by overcoming the need for a bilateral choice between a share purchase transaction and an asset transaction. Under an RVO structure, the purchaser is

able to obtain some of the benefits of a share deal without some of the negative consequences, and is able to obtain some of the benefits of an asset deal, without some of the negative consequences. What results is neither a pure asset transaction nor a pure share transaction but a combination of both. This is not a remedy available without the intervention of the court. It is not a remedy to which any party is entitled by law: *Harte Gold*, 2023 ONSC 653, *Atlas Global*, 2024 ONSC 5570. It requires the exercise of the discretion of the court under s. 11 of the CCAA.

[9] The RVO has been found to be a useful, value-enhancing procedure in circumstances where:

(a) the debtor operates in a highly regulated environment in which its existing permits, licences or other rights would be difficult or impossible to assign to a purchaser;

(b) the debtor is party to certain key agreements that would be difficult or impossible to assign to a purchaser; and

(c) maintaining the existing legal entity would preserve tax losses (capable of being brought forward and set off against future income) that would otherwise be lost in a traditional asset sale.

[10] However, because the RVO is extraordinary relief, it is subject to stringent factors set out in the case law. Essentially, in addition to the usual *Sound Air* factors which must be considered for court approval of a proposed transaction, approval of an RVO requires consideration of:

(a) why the RVO is necessary in this case;

(b) whether the reverse vesting transaction structure produces an economic result at least as favourable as any other viable alternative;

(c) whether any stakeholder is worse off under the reverse vesting transaction structure than they would have been under any other viable alternative; and

(d) whether the consideration being paid for the debtors' business reflects the importance and value of the licenses and permits (or other intangible assets) being preserved under the reverse vesting transaction structure: *Harte Gold*.

[11] These factors must, as is the case with the traditional *Sound Air* factors, be supported with evidence in the record filed on the approval motion.

[12] I am satisfied that the *Harte Gold* factors are satisfied in this case.

[13] The debtor operates in a highly regulated industry. The principal asset of the debtor is its intellectual property and its numerous Canadian, U.S. and Israeli government licences and other approvals. These are listed as a schedule to the acquisition agreement. I am satisfied on the evidence that these assets are neither readily assignable nor replaceable. No purchaser would take the risk that it could just pick up where the debtor left off without the firm knowledge that these licences and approvals remain valid and in place. This is the classic case where an RVO can be employed to enhance value for all stakeholders.

[14] The record also satisfies me that the transaction before the court is the only transaction available. The debtor has no funds, other than the funds made available by its secured lender. The secured lender made

the only acceptable bid – the value of its credit of about $52 million. The only other option to the proposed acquisition at this point is a bankruptcy. The evidence is clear, as stated by the Monitor,that all stakeholders would be worse off in a bankruptcy scenario. Therefore, the economic result of the RVO transaction is better than the economic result under a bankruptcy.

[15] No stakeholder will be worse off under the proposed RVO transaction than they would be under any other viable transaction. First, there is no other viable transaction – there is only a bankruptcy. The credit bid almost certainly represents more than the debtor is worth in realizable value. The purchaser, *qua* creditor, will likely suffer a shortfall. In no realistic scenario will there be surplus funds for unsecured creditors or for current equity holders.

[16] Finally, the value being paid clearly reflects the value of the intangible assets being preserved by the RVO structure. There has been a robust SISP process, both before and after the CCAA filing. K2 has emerged as the only party willing to acquire the debtor. The intangible assets are, in large measure, what the purchaser is acquiring in exchange for cancellation of its $52 million in debt.

[17] A consideration of the standard *Sound Air* factors also leads me to the same result. I find that the acquisition agreement meets the *Sound Air* test and should be approved.

[18] The Monitor supports both the SISP process and the approval of the transaction as the best transaction available. The Monitor also confirms its opinion that the proposed transaction is better for stakeholders than a bankruptcy.

[19] I agree with the applicant that a limited sealing order of the bid information resulting from the SISP process is justified. A sealing order is required to preserve the ability of the debtor to continue efforts to maximize value in the unlikely event that the proposed transaction does not close.

[20] The applicant seeks a release of those involved in keeping the debtor operating through the prefiling and post filing process that brought it to this point. This includes directors, officers and employees, the lender and professional advisors. A consideration of the *Lydian* factors satisfies me that the releases being sought should be approved. They are rationally related to the purpose of the restructuring; the proposed releasees contributed to that purpose; the releases are not overbroad and appropriately carve out any claims resulting from: (a) fraud, bad faith or illegal acts; and (b) that are not permitted to be released pursuant to section 5.1(2) of the CCAA. In addition, all stakeholders had notice of the releases being sought. There is no opposition to the proposed releases being granted. The Monitor approves of the scope and form of the releases being proposed.

[21] Finally, the debtor is seeking to amend the ARIO so that it may liquidate assets not exceeding $5,000,000 in the aggregate without further court approval. In *AbitibiBowater*, the CCAA debtors, with approval from the Monitor, were permitted to dispose of their assets, in whole or in part, provided that the price in each case did not exceed $50,000,000 in the aggregate. Justice Osborne in *Pride Group Holdings* permitted the CCAA debtors to sell assets without prior approval of the Court up to $12,000,000 in the aggregate. Here, there are excluded assets which are not part of the transaction. Thus there is the potential for additional assets being liquidated and further value maximization. Relatively modest returns are expected, however, and the cost of returning to court (indeed, to three courts because of the foreign recognition proceedings) would significantly impair the net realization on these residual assets. The Monitor will, of course, continue to supervise any additional transactions and will have to support them. I find, therefore, that it is in the best interest of the applicant and its stakeholders that the court approve the ARIO amending order to allow the applicant to dispose of assets not exceeding $5,000,000 in the aggregate without further approval of the court.

Penny J.

Penny J.