THE VALUATION LAW REVIEW

volume 9 / issue 1
January 2003

Corporate / Securities Decisions and Regulatory Developments

The Valuation Law Review summarizes corporate and securities decisions and recent regulatory developments of interest to business valuators and is a joint publication of The Canadian Institute of Chartered Business Valuators and Stikeman Elliott. The Valuation Law Review is not intended to provide legal advice and readers should not act on information in the publication without seeking particular advice on matters that are of concern to them. Readers are cautioned against relying upon the decision abstracts contained herein, which are edited and in outline form only, and are directed to the full report of the reasons of the Court or Securities Regulator, as applicable.

The primary contributors to this publication practice corporate and securities law with the firm of Stikeman Elliott:

Editor:
Donald G. Belovich

Associate Editors:
Andrew S. Cunningham
Chris Flood
Andrew Grossman

Editorial Advisory Board:
William J. Braithwaite
Dee Rajpal
Simon A. Romano
Mihkel E. Voore
Edward J. Waitzer

For subscription information please contact:
The Canadian Institute of Chartered Business Valuators
277 Wellington Street West, 5th Floor
Toronto, Ontario M5V 3H2
Telephone: (416) 204-3396

Subscription Rate: $75 plus GST per year published semi-annually

All rights reserved. No part of this publication may be reproduced, stored in a retrieval system, or transmitted, in any form or by any means, electronic, mechanical, photocopying, recording, or otherwise, without the prior written permission of the CICBV.
© Copyright CICBV 2002

The Canadian Institute of Chartered Business Valuators and Stikeman Elliott

I. CANADIAN DECISIONS

page 4

Grynwald (Mandatary of) v. Grynwald
[2002] Q.J. No. 1069
Québec Superior Court
(May 10, 2002)
In an oppression claim brought on behalf of a majority shareholder suffering from reduced mental capacity, the court rejected the minority shareholders' attempts to gain voting control of a corporation through a preferred share subscription without the consent of the majority shareholder. The court annulled the share subscription, and issued a unanimous shareholders' agreement to govern the break-up of the Company.

page 6

Ultramar Ltd. v. Luby
[2002] N.J. No. 175
Newfoundland and Labrador Supreme Court - Trial Division
(June 25, 2002)
In an oppression application brought by a creditor of a company controlled by the respondent, the court found that the creditor qualified as a "complainant" within the meaning of the oppression provisions in the Newfoundland *Corporations Act.* Relief from oppression is available where directors, in a conflict of duty, negotiate contracts that are not in the best interests of a corporation, and from which they stand to gain personally.

page 8

Re Francisco Gold Corp.
[2002] B.C.J. No. 1608
B.C. Supreme Court
(July 12, 2002)
Earlier in 2002, the B.C. Court of Appeal's *Sepp's* ruling - in which signatories to lock-up agreements were disqualified from voting as part of the minority or from being counted in "majority of minority" plan of arrangement votes - caused considerable concern in the business and legal communities. Francisco Gold, released several months after *Sepp's*, analyzes support agreements more consistently with industry practice and the Ontario Securities Commission's Companion Policy to Rule 61-501. Although it is a lower court ruling, Francisco Gold suggests that the reasoning in *Sepp's* may not have become entrenched in British Columbia.

Corporate / Securities Decisions and Regulatory Developments (cont'd.)

page 9
Casurina Limited Partnership v. Rio Algom Ltd.
[2002] O.J. No. 3229
Ontario Superior Court of Justice
(August 22, 2002)
An Ontario court recently considered the valuation of convertible debentures where the corresponding common shares are de-listed during a period in which the trust indenture effectively guaranteed debentureholders a 25% premium over par in the event of redemption. While the judge found the whole issue moot, as a "no action" clause in the trust indenture effectively barred the debentureholders from proceeding under the oppression provision of the *Business Corporations Act* (Ontario), he nevertheless considered the valuation issue on a hypothetical basis. Had he been called upon to fashion a fair remedy under the oppression provision, the judge would apparently have ordered the respondents to buy out the debentureholders at 25% over par value, as this reflected their reasonable expectations about what they would receive on a redemption during the period in question. He rejected an alternative approach of valuing the debentures on the basis of the actual value of the company's common stock at the time in question.

page 12
Discovery Enterprises Inc. v. Ebco Industries Ltd.
[2002], B.C.J. No. 1957
British Columbia Supreme Court
(August 28, 2002)
In a successful oppression claim under the B.C. *Company Act*, the court ordered that the company buy out the applicant's shares at half their initial purchase price. In making the ruling, the court rejected the parties' submissions, despite their similarity, on the fair market value of the shares.

II. U.S. DECISIONS

page 17
Peltz v. Hatten et al.
279 B.R. 710
United States District Court for the District of Delaware
(June 5, 2002)
In a Chapter 11 bankruptcy proceeding, the Trustee failed to show that the debtor received less than equivalent value in acquiring a cellular telephone company. The court examined the totality of the circumstances surrounding the acquisition, such as the parties' good faith, the arm's length relationship between the parties, relevant comparable sales and the conditions in the market place. Since the purchase price had been the result of negotiations between sophisticated parties who were well informed and had made reasoned judgments about growth, risks and marketplace values, the court refused to revise the purchase price.

page 20
Summit Metals, Inc. v. Gray, et al.
2002 U.S. Dist. Lexis 15599
United States District Court for the District of Delaware
(August 20, 2002)
In determining whether a director of various affiliated companies acted fairly in a transaction involving self-dealing, a court should apply the two-part test of fairness, which looks at whether there was fair dealing among the parties and whether the transaction was concluded at a fair price.

page 21
Applebaum v. Avaya, Inc., et al.
2002 Del. Lexis 699
Supreme Court of Delaware
(November 20, 2002)
A reverse stock split (i.e., consolidation) followed by a forward stock split aimed at eliminating the expensive small shareholdings of a public company was found not to violate Section 155 of the Delaware General Corporation Law. The Supreme Court of Delaware confirmed the Court of Chancery of Delaware's decision that for the purposes of determining the "fair value" of the small shareholders' shareholdings pursuant to Section 155, fair market value of the common stock was a fair determinant of fair value. The court also found that shareholders of a company need not be treated equally, provided they are treated fairly.

Corporate / Securities Decisions and Regulatory Developments (cont'd.)

III. REGULATORY DEVELOPMENTS

page 25
Proposed Amendments to the TSX Company Manual
Recently proposed amendments to The Toronto Stock Exchange Company Manual would amend the definition of "market price" from the closing price of the listed security to the five day volume weighted average trading price and would give The Toronto Stock Exchange the discretion to shorten or lengthen the applicable calculation period, based on a number of relevant factors.

page 26
Proposed National Instrument 81-106 - *Investment Fund Continuous Disclosure*
The Canadian Securities Administrators recently proposed draft National Instrument 81-106 - Investment Fund Continuous Disclosure, which would impose certain continuous disclosure obligations on investment funds. Specifically, labour sponsored investment funds would be required to file a statement of investment portfolio containing, where the current value of securities is not readily available, an independent formal valuation of its securities prepared in accordance with the proposed national instrument.

page 26
Proposed National Instrument 71-102 - *Continuous Disclosure and Other Exemptions Relating to Foreign Issuers*
The Canadian Securities Administrators recently published for comment National Instrument 71-102 - Continuous Disclosure and Other Exemptions Relating to Foreign Issuers, which, among other things, exempts eligible foreign issuers from the valuation requirements of Canadian securities laws.

page 27
Amendment to Section 171 of the Alberta Securities Commission Rules
The Alberta Securities Commission Rules were amended effective June 12, 2002 to relieve offerors in certain circumstances from the satisfying the valuation requirements imposed in the context of a formal take over bid.

I. CANADIAN DECISIONS

Grynwald (Mandatary of) v. Grynwald

[2002] Q.J. No. 1069

Québec Superior Court

(May 10, 2002)

In an oppression claim brought on behalf of a majority shareholder suffering from reduced mental capacity, the court rejected the minority shareholders' attempts to gain voting control of a corporation through a preferred share subscription without the consent of the majority shareholder. The court annulled the share subscription, and issued a unanimous shareholders' agreement to govern the break-up of the Company.

This matter involved an application under the oppression provisions of Section 241 of the *Canada Business Corporation Act* (the **"CBCA"**) to reverse an attempt to deprive an incapacitated majority shareholder of the voting control he held in Technical Knitting Services Limited (**"Technical Knitting"**).

In 2000, Chil Grynwald (**"Grynwald"**), the majority shareholder of Technical Knitting, held 100 common shares and 1,000 preferred voting shares. Rachel and Dora Grynwald, his wife and daughter, respectively (the **"Respondents"**), each owned 100 common shares. Although the Respondents were given shares of Technical Knitting and appointed directors along with Grynwald, they were never involved in any decision-making. Grynwald alone managed the company and its assets.

Complicating the relationship was the fact that, despite being married to Rachel Grynwald, Grynwald had been living with another woman (**"Bloom"**) for 26 years prior to the start of the application, although he did provide financial support to his wife and daughter.

In 1999, Grynwald underwent back surgery and subsequently suffered complications which left him mentally impaired. In February 2000, Bloom applied for a court order allowing her to take control over Grynwald's affairs in anticipation of his incapacity (the **"Mandate"**). The Mandate was granted on May 25, 2000.

Two months previously, on March 15, 2000, a notice of meeting was sent to Grynwald by the Respondents, stating that its purpose was to change the head office of Technical Knitting and to "confirm arrangements and decisions regarding the administration and control of the Company." Subsequently, on March 17, 2000, Bloom replied that since she could not yet act on Gynwald's behalf, she trusted that the Respondents would not "take advantage of the situation" and would limit the purpose of the meeting to changing the head office. On March 20, 2000, the Respondents, with the incapacity proceedings pending, each subscribed and paid for 1000 voting preferred shares of Technical Knitting and accepted the share subscriptions as directors. The shares they received were sufficient to outvote Grynwald's 1,000 shares of the same class. It was not until September 15, 2000 that Bloom was informed that the Respondents had purported to acquire voting control of Technical Knitting.

Bloom brought an application pursuant to the oppression provisions of Section 241 of the CBCA in which she claimed that the Respondents' share subscriptions were oppressive and unfairly prejudicial to Grynwald since they disregarded his interests by stripping him of control of Technical Knitting without his knowledge or consent.

The Superior Court began by addressing the Respondents' claim that Bloom lacked standing to bring the oppression application. The court found that Bloom, as Grynwald's mandatary (a Québec civil law term meaning, essentially, "agent" of an incapacitated person), was bound to exercise Grynwald's rights pertaining to the administered property. As Grynwald could validly complain that he had been unjustifiably deprived of control of Technical Knitting, and since Bloom administered his shares during his incapacity, it was therefore her right and duty to attempt to regain control.

The court then went on to address whether the Respondents' share subscriptions, and Technical Knitting's resulting issue of voting shares, was oppressive and unfairly prejudicial to Grynwald's rights as a shareholder. This determination was based on the court's view of the parties' reasonable expectations in the circumstances of Grynwald's incapacity. The court considered that Grynwald would have been dealt with unfairly if he or his legal representative were unjustifiably deprived of his voting shares against his, or his legal representative's, will.

In these circumstances, the court found nothing in the provisions of the Mandate, at law or in the conduct of Grynwald and Bloom to conclude that either had consented to the Respondents' share subscription, or that the Respondents were justified in acting because of something Grynwald or Bloom had done.

The court also rejected the argument that Grynwald's control of the company depended on the Respondents' tacit acceptance, since they were directors and held a majority of the common shares. By voting his preferred shares, Grynwald could have replaced the Respondents as directors and officers at any time, leading the court to conclude that the Respondents had no legitimate expectation of controlling Technical Knitting, and that the onset of Mr. Grynwald's incapacity did not change this.

The court focused on the fact that while Grynwald placed his wife and daughter on the board and made them officers, this did not mean that he would have wanted them to exercise control in the event that he could no longer do so himself. In

fact, the provisions of the Mandate indicated otherwise. The Mandate itself stated that in the event of Bloom's death or incapacity, his accountants and Bloom's daughter would replace Bloom.

The court found that the extent of the Respondents' expectations, based on Grynwald's past conduct, was to be informed of the business of Technical Knitting, and possibly, to take part in the deliberations of its board, without actually controlling it. On this basis, the court concluded that there was no justification for Respondents' share subscription, which was unfairly prejudicial to Grynwald.

In its remedy order, the court annulled the share subscriptions and created a governance structure for the company designed to prevent future conflicts. This structure included amended by-laws creating a five-person board of directors, a compulsory special shareholders meeting to be held within two weeks of the judgment in order to elect a new board and a unanimous shareholders' agreement that set out procedures for dissolving Technical Knitting in a way that protected the interests of Grynwald and the Respondents.

Leave to appeal was denied by the Québec Court of Appeal on August 12, 2002.

Ultramar Ltd. v. Luby
[2002] N.J. No. 175
Newfoundland and Labrador Supreme Court - Trial Division
(June 25, 2002)

In an oppression application brought by a creditor of a company controlled by the respondent, the court found that the creditor qualified as a "complainant" within the meaning of the oppression provisions in the Newfoundland *Corporations Act*. Relief from oppression is available where directors, in a conflict of duty, negotiate contracts that are not in the best interests of a corporation, and from which they stand to gain personally.

Ultramar involved a determination of whether the plaintiff, Ultramar Ltd. (**"Ultramar"**) qualified as a "complainant" within the meaning of Section 371 of the Newfoundland *Corporations Act* (the **"Act"**). This was a key point as it would determine whether Ultramar would be entitled to claim relief under the Newfoundland oppression provisions as a judgement creditor of Tors Cove Excavating Ltd. (**"Tors Cove"**), a company controlled by its director, Michael Luby (**"Luby"**). This issue of standing was significant because oppression provisions under the corporate statutes are most often relied upon by minority shareholders where they have been treated unfairly by the majority. Creditors typically have other means at their disposal to recover debts.

If the answer to the standing issue was affirmative, the court was asked to determine whether Luby acted in a manner that was oppressive to Ultramar, entitling it to damages from Tors Cove.

In an earlier action, Ultramar had received a judgment against Tors Cove for the amount claimed in the oppression claim (resulting in Ultramar's judgement creditor status *vis-a-vis* Tors Cove). Luby had indicated to the court that, although Tors Cove was not in a position to pay the judgement at that time, the debt would be paid following the settlement of an unrelated claim against the government of Newfoundland and Labrador. When the time came to negotiate and finalize a settlement with the government however, Luby negotiated a direct payment to himself (he was a joint plaintiff with Tors Cove, among others) of an amount well in excess of the amount claimed by Ultramar. The settlement was arranged with the knowledge of all of the parties to the judgment registered against Tors Cove in favour of Ultramar, but Luby failed to make any payment to Ultramar in respect of the judgement debt. As a result of the payment to Luby, Tors Cove, among others, discontinued its action against the government.

The court dealt with two issues pertaining to liability: first whether Ultramar was a "complainant" under the Act's oppression provisions; and second, whether the actions of Luby, as a director of Tors Cove, were oppressive against Ultramar.

Creditors who do not hold securities are not one of the defined categories of "complainant" under the oppression provisions in most Canadian corporate statutes. So in order for a creditor to qualify to bring an action for oppression, he or she must convince a court that he or she fits within the "complainant" definition's basket clause. That is, the court must use its discretion to determine whether the party bringing the action is a "proper person" to bring such a claim.

The court found that there were at least two circumstances in which an applicant could be regarded as a "proper person" under the test in the Act: first, where the act or conduct complained of constitutes using the corporation as a vehicle for committing fraud upon the applicant; and second, where the act or conduct complained of constitutes a breach of the underlying expectation of the applicant, arising from the circumstances in which the applicant's relationship with the corporation arose.

Since there was no fraud alleged by Ultramar, the court looked to the second circumstance referred to above. It cautioned against routinely turning debt actions into oppression actions, preferring the view that complainant status should be

granted only where a creditor is in a position analogous to that of a minority shareholder with a legitimate interest in the manner in which the affairs of the company are managed. By virtue of the judgement debt owed to it by Tors Cove, Ultramar was found to have had such a legitimate interest.

The court in *Ultramar* ultimately determined that creditors can be viewed in appropriate circumstances as valid complainants under the relevant legislation in Newfoundland and Labrador, as well as the Canadian courts generally.

Having found that Ultramar qualified as a complainant under the Newfoundland oppression provisions so that it could sue Luby, the court turned to the question of liability. The court noted that while historically one component in proof of oppression included "bad faith", recent jurisprudence on the remedy has clearly departed from this requirement and focused on whether the acts complained of have had an "unfair result" on the complainant.

The court in *Ultramar* concluded that Luby had a duty to act in the best interests of Tors Cove as well as to work towards preserving his own claim against the government of Newfoundland. In resolving the negotiations with the government in the manner in which he did, Luby in particular was in a conflict position and failed to protect the interests of Tors Cove or those parties, like Ultramar, with a legitimate interest in the way in which Tors Cove was managed. As a result, the court ordered in favour of Ultramar for the full amount of its claim.

Re Francisco Gold Corp.
[2002] B.C.J. No. 1608
B.C. Supreme Court
(July 12, 2002)

Earlier in 2002, the B.C. Court of Appeal's *Sepp's* ruling - in which signatories to lock-up agreements were disqualified from voting as part of the minority or from being counted in "majority of minority" plan of arrangement votes - caused considerable concern in the business and legal communities. *Francisco Gold*, released several months after *Sepp's*, analyzes support

As discussed in the July 2002 VLR, the court in *Sepp's Gourmet Foods v. Janes* (2002), 98 B.C.L.R. (3d) 217 (C.A.) agreed that a minority shareholder should be excluded from being counted in a "majority of minority" vote on a proposed plan of arrangement where he has entered into a "lock-up" agreement in which he agreed to support the transaction. In doing so, the court maintained, the minority shareholder had acted "jointly or in concert with" the majority. This conclusion was inconsistent with industry practice and with the carefully considered Companion Policy to Ontario Securities Commission Rule 61-501. The Supreme Court of Canada declined to hear an appeal in *Sepp's*.

Francisco Gold also concerned a proposed plan of arrangement under Section 252 of the B.C. *Company Act.* Although the proposal received 95% support from the shareholders who voted, an unhappy 2% shareholder argued, apparently without referring to *Sepp's*, that the agreement was a related party transaction because certain director-shareholders of Francisco Gold had entered into a support agreement with Glamis, the prospective acquiror. If the transaction had been construed as a related party transaction, an independent valuation would have been required.

agreements more consistently with industry practice and the Ontario Securities Commission's Companion Policy to Rule 61-501. Although it is a lower court ruling, *Francisco Gold* suggests that the reasoning in *Sepp's* may not have become entrenched in British Columbia.

The judge was highly sceptical of the shareholder's argument. The support agreement, he noted, was "an integral part of the plan of arrangement itself, among otherwise unrelated parties." He went on to describe the respondent shareholder's argument as an "unlikely proposition", although it is important to note that he did not come down conclusively against it, instead noting that even if it were supposed to have some validity, the transaction was perfectly fair and should be allowed to go forward even so.

Even if the judge's comments are technically *obiter*, they may provide a precedent by which the impact of the *Sepp's* decision might eventually be minimized. However, this is rendered uncertain by the apparent failure of the judge to consider the *Sepp's* decision.

Casurina Limited Partnership v. Rio Algom Ltd.
[2002] O.J. No. 3229
Ontario Superior Court of Justice
(August 22, 2002)

Billiton plc's take-over of Rio Algom Ltd. in August 2000 gave rise to this litigation on behalf of holders of 1997 Rio Algom convertible debentures. On the terms of the trust indenture, the convertible debentures were not redeemable until February 1, 2002 unless Rio Algom shares had been trading at 125% of the $40 conversion price over a specified period just before the time notice of redemption was given. Essentially this meant that the debentureholders could expect a 25% premium over par (at least) if their debentures were redeemed before the call date. As of that date, however, the convertible debentures would be redeemable at par regardless of the trading price of the Rio Algom common shares.

An Ontario court recently considered the valuation of convertible debentures where the corresponding common shares are de-listed during a period in which the trust indenture effectively guaranteed debentureholders a 25% premium over par in the event of redemption. While the judge found the whole issue moot, as a "no action" clause in the trust indenture effectively barred the debentureholders from

Billiton's acquisition of all of Rio Algom's common shares, which was followed by their de-listing, accordingly raised some difficult issues. The relevant trust

proceeding under the oppression provision of the *Business Corporations Act* (Ontario), he nevertheless considered the valuation issue on a hypothetical basis. Had he been called upon to fashion a fair remedy under the oppression provision, the judge would apparently have ordered the respondents to buy out the debentureholders at 25% over par value, as this reflected their reasonable expectations about what they would receive on a redemption during the period in question. He rejected an alternative approach of valuing the debentures on the basis of the actual value of the company's common stock at the time in question.

indenture listed certain events of default. One of these was the breach of the covenant that common shares of Rio Algom be issued on The Toronto Stock Exchange (the "TSX") upon the exercise of conversion rights. The share sale and de-listing constituted a breach of the covenant, Mr. Justice Spence held, since Rio Algom was no longer in a position to issue common shares on the TSX, or even to list there (no longer having the broad public shareholding that the Exchange requires). An event of default had therefore occurred. The remedy set out in the trust indenture was redemption at par. After an initial proposal to redeem the convertible debentures at par plus accrued interest was rebuffed, Billiton apparently took a hard line, declining to offer anything over par (and perhaps not even that). This drove the debentureholders to seek a remedy under the oppression provisions of the *Business Corporations Act* (Ontario) (the **"OBCA"**). These provisions allow for a much broader range of court-ordered remedies, and the debentureholders were undoubtedly hoping to get more than par value by proceeding under them.

The oppression argument did not get very far. Spence J. found that the "no action" clause in the trust indenture prevented the debentureholders from seeking statutory relief in their own names, rather than proceeding through the Trustee. It is important to note that this does not mean that the existence of a bargained-for remedy in the contract precludes a party from resorting to a statutory remedy - it is simply that the Trustee must be the conduit of such an action.

Thus the debentureholders' application was denied. Despite this finding, however, Spence J. considered valuation issues at length "both for the parties in this case and for other prospective litigants in other cases." Although he characterized his remarks as *obiter dicta*, what Spence J. had to say might be indicative of how others in similar situations would fare.

The respondents (Billiton, Rio Algom et al.) argued that "fair value" should be the basis of any remedy under the OBCA oppression provisions. The court considered two ways of arriving at fair value. The first was to make an actuarial calculation of the value of the debentures. A Harvard professor testified as an expert on this form of valuation. Using his figures, Spence J. found that the value of the convertible debentures at the time of the share acquisition would have been just under their par value - $98.18. The value could not be above par, since the debentureholders were far out of the money at the relevant time (the commons had been trading at $18, Billiton offered $27, and the conversion price was $40).

An alternative approach to "fair value" would be to consider the prices paid in actual redemptions or repurchases in comparable transactions. Although Spence J. maintained that identifying truly "comparable" transactions would be very difficult, the respondents pointed out that, as a matter of general principle, there is "no custom in the Canadian market" according to which a bidder for common shares pays above par for the early redemption of convertible debentures: "Where the debenture is well out of the money...there is no immediately obvious rationale for a price at a premium to par", they argued. Spence J. seems to have generally accepted this argument. He therefore concluded, with respect to the two approaches to "fair value", that each would produce a figure slightly below the par value in these circumstances.

The debentureholders argued that the standard of relief should not be determined by an economic calculation of fair value, but should instead be grounded in a more expansive understanding of "fairness" that would take into account their expectation that a 25% premium to par would be available to them if their convertible debentures were redeemed or repurchased before February 1, 2002. Spence J. agreed with the respondents that to apply this standard would be to produce something of a windfall from an economic point of view. Indeed, he even accepted that, had a few common shares remained outstanding in the hands of minority shareholders, the oppression remedy would undoubtedly have required only that the respondents buy out the debentureholders at a price based on the price at which those shares had been trading prior to the impugned transaction - a figure that in this case would have been far less than 125% of par value.

In spite of these considerations, however, Spence J. stated that this would have been the correct result under the oppression remedy, had it applied. What matters most is the reasonable expectation of the debentureholders that their convertible debentures would not be redeemed early except at the premium price. Even though the vast majority of the debentures had been purchased after Billiton had acquired its controlling interest in Rio Algom, the purchasers were deemed by Spence J. to have relied on the expectations of those from whom they had purchased, even if, as a matter of psychological fact, no such expectations had actually existed.

It should be added that Spence J. did not seem entirely committed to this result - the whole discussion of valuation is couched in highly conditional language and is

prefaced with the remark that, even after the "comments" that he is about to make (and which we have just recounted), "the valuation issue remains unresolved". Moreover, he implied that he preferred the startlingly generous 25%-over-par option merely as the best of the three options he was asked to consider by counsel.

Discovery Enterprises Inc. v. Ebco Industries Ltd.
[2002], B.C.J. No. 1957
British Columbia Supreme Court
(August 28, 2002)

In a successful oppression claim under the B.C. *Company Act*, the court ordered that the company buy out the applicant's shares at half their initial purchase price. In making the ruling, the court rejected the parties' submissions, despite their similarity, on the fair market value of the shares.

In 1996, Discovery Enterprises Inc. (**"Discovery"**) filed an oppression petition against Ebco Industries Ltd. (**"Ebco"**), a private company run by two brothers (the **"Majority Shareholders"**), and commenced a derivative action against Helmut, one of the Majority Shareholders. Discovery was a venture capital fund established by the British Columbia government that, in consideration for the issuance of Class D shares, had invested $2.7 million in Ebco in 1987 to develop its aerospace division. The aerospace division made a profit in 1987, but by 1990 it had incurred an aggregate loss of approximately $3.5 million.

The Class D shares permitted Discovery to wind up the aerospace division (in which case, Ebco would be entitled to redeem the Class D shares) if the cumulative annual dividends payable on the shares remained unpaid for four years. In 1990, Discovery was in a position to exercise that right and threatened to do so, but decided otherwise. It had been erroneously advised that Ebco's Articles of Incorporation did not permit the payment of a dividend on the Class D shares when the aerospace division was in cumulative deficit.

By 1992, all members of the board of directors, including Discovery's nominee, had resigned in the face of increasing acrimony between the Majority Shareholders. In May of 1992, Discovery again threatened to wind-up the aerospace division but withdrew its notice upon entering an agreement with Ebco that provided, among other things, that the aerospace division would be transferred to a newly incorporated company of which Discovery would own 30% (the **"Agreement"**). However, the closing of the transactions contemplated by the Agreement was conditional on the parties receiving approval from the federal government, which

had also provided a loan to the aerospace division. That consent was ultimately refused on the basis that the aerospace division had defaulted on all of its loan payments.

Discovery then realized that it would likely incur a loss on the Ebco shares, even if it were able to find a buyer for the illiquid investment. The court found that instead of accepting the loss, Discovery became prepared to use any tactic necessary, including the oppression and derivative claims, to pressure Ebco into purchasing the Class D shares at a price acceptable to Discovery. The court found that in pursuing this strategy, Discovery had unfairly pressured Ebco during this period. This influenced the court in deciding not to exercise its discretion in Discovery's favour on the derivative claim.

In the meantime, the Majority Shareholders agreed to go to arbitration to settle their differences as Ebco's board was effectively deadlocked. The arbitrator split the business between the Majority Shareholders with one of them, Helmut, retaining control of Ebco itself and the aerospace division. The resulting costs of the arbitration laid the groundwork for the derivative action commenced by Discovery.

The Derivative Action

Discovery commenced the derivative action on the basis that Helmut had claimed the $4 million cost of the arbitration, including valuation and accountants' fees, as an expense of Ebco rather than a personal expense, and that by doing so, Helmut had breached his fiduciary duty as a director.

The court dismissed the derivative action on the basis that the arbitration was a reasonable corporate expense in light of the alternative (i.e. winding up Ebco) and the fact that it was the only way to break the board's deadlock. The court equated the appointment of a liquidator on the winding-up of a company to the Majority Shareholders' appointment of the arbitrator. Like a liquidator, the arbitrator was charged with deciding what to do with Ebco's assets while taking into account the interests of all shareholders. Moreover, because the Majority Shareholders wanted Ebco's assets distributed to satisfy their respective interests in the company, valuation and accounting evidence was required to substitute for market valuations. As a result, the costs of the arbitrator, the valuators and the accountants were proper expenses of the company.

In reaching its conclusion, the court was influenced by its view that Discovery had not actively pursued its rights as a minority shareholder during or immediately after the arbitration process. While aware of the arbitration agreement between the Majority Shareholders, Discovery had not objected to the process or pursued any legal remedies to reverse the arbitrator's decision until years later. The court was also critical of the resignation of Discovery's board nominee in 1992, noting that Discovery had squandered the cost-effective alternative to breaking the deadlock between the Majority Shareholders.

The Oppression Petition

The oppression petition brought by Discovery sought, among other things, an order to have the aerospace division run as a separate company. Despite Ebco's acknowledgement that some of its actions were unfairly prejudicial to Discovery, the court reviewed several transactions entered into by Ebco to establish that the petition would have been successful despite Ebco's admission.

Of the transactions reviewed, the court focused on certain interdivisional loans made by the aerospace division to Ebco and the effect of those loans on Discovery. The court found that the aerospace division could not afford to advance the approximately $1 million it had transferred to Ebco and should have instead used the money for the repayment of the division's federal government loan. As mentioned above, as a result of Ebco's failure to repay the federal government loan, the federal government refused to approve the Agreement, which was commercially advantageous to Discovery. In addition, the advances ignored the parties' reasonable expectations, as evidenced by the Agreement, that the affairs of the aerospace division would be treated as a separate entity.

In light of Ebco's admission, the court determined that Discovery had been unduly prejudiced and that the most appropriate remedy was for Ebco to purchase the Class D shares.

Valuation Date

Ebco and Discovery disagreed over the appropriate valuation date for the Class D shares. As a general rule, courts use the date a petition is filed as the valuation date, but Discovery argued that the proper date was the first day of trial. The court could have elected not to apply the general rule, but it was not prepared to do so in this case since Discovery was a sophisticated party that had other options

it could have turned to in order to influence the timing of a sale of the Class D shares, including the forced liquidation of the aerospace arm. Once it filed its petition, Discovery forfeited its right to benefit from any fortunes the aerospace division may have accumulated after that date.

Purchase Price of the Discovery Shares

The court then determined the value of the Class D shares to be paid to Discovery. Discovery sought $4.85 million, representing $2.7 million in paid-up capital, plus simple interest at 5% from the time of investment to the start of trial or, in the alternative, an order requiring a valuation of the aerospace division. Discovery conceded to the court that the $4.85 million figure bore no relation to the fair value of the shares in August of 1999.

The court rejected the valuation option as overly costly and impractical, given that 6 years had passed since the valuation date. Instead, it chose to focus on the parties' submissions on fair value for the Class D shares, implicitly rejecting Discovery's claim for $4.85 million.

Ebco submitted that the fair value of the shares in 1996 was $300,000, representing the sum that would have been derived on liquidation of the division. Discovery's own assessment of the shares in 1996 had been $311,000 but it had discounted the value to $300,000 as a result of the Agreement not taking effect.

Despite the fact that the parties agreed on the fair value for the Class D shares, the court was not convinced that a purchase price at the fair value was appropriate because of the unconventional nature of the investment. First, the investment provided for participation in the profits and assets of a single division rather than Ebco as a whole. Second, neither party fully understood their rights and obligations under the share provisions of the Articles of Incorporation because, in the court's view, they were poorly drafted. Therefore, the court found that the appropriate purchase price was what the parties would have negotiated had the meaning of the share provisions been clear and had Discovery disposed of its shares pursuant to the provisions. The court found that, had the share provisions been clear, neither Discovery nor Ebco would have had an interest in winding up the company, with both realizing that the aerospace division was worth more as a going concern.

The issue then became the amount of the buyout price the parties would have agreed upon. The court decided that such a determination was impossible given

the passing of 6 years from the valuation date. It nonetheless found that the parties would have agreed to $1.35 million as a purchase price for Discovery's shares, representing half the original purchase price of $2.7 million. The premium over the agreed-upon fair market value was justified in the court's view, by the fact that Ebco would have wanted to avoid a liquidation of the division and would have paid over fair market value to buy Discovery out to do so.

II. U.S. DECISIONS

Peltz v. Hatten et al.

279 B.R. 710

United States District Court for the District of Delaware

(June 5, 2002)

In a Chapter 11 bankruptcy proceeding, the Trustee failed to show that the debtor received less than equivalent value in acquiring a cellular telephone company. The court examined the totality of the circumstances surrounding the acquisition, such as the parties' good faith, the arm's length relationship between the parties, relevant comparable sales and the conditions in the market place. Since the purchase price had been the result of negotiations between sophisticated parties who were well informed and had made reasoned judgments about growth, risks and marketplace values, the court refused to revise the purchase price.

USN Communications, Inc. (**"USN"**) was a reseller of local, long distance and other telecommunications services. USN sought to improve its position in the market by acquiring a wireless service provider. In 1997, USN contacted Hatten, an executive of Hatten Communications Holding Company, Inc. (**"HCHC"**), and offered to purchase the shares of Connecticut Telephone and Connecticut Mobilecom (collectively "**CT Tel"**), which were held by HCHC. CT Tel was a telecommunications reseller which provided cellular telephone, local and long-distance telephone as well as Internet services in a different geographical market than USN. After brief negotiations, USN and CT Tel executives agreed on a purchase price of U.S.$68 million. At USN's request, the acquisition was conditional upon a successful initial public offering in which USN had planned to raise U.S.$128 million.

Before signing the purchase agreement, USN conducted extensive due diligence of CT Tel's business, analysed comparable transactions involving cellular service providers and formed a committee to examine the proposed transaction. USN hired an investment banker who performed a valuation of CT Tel and concluded that that the value of CT Tel exceeded the proposed purchase price. USN's senior management also valued CT Tel at U.S.$114 million, using a discounted cash flow (**"DCF"**) analysis. A DCF analysis values a corporation by projecting its future cash flows, determining the present value of these cash flows by assigning a discount rate, performing a present value calculation, and then summing them. USN's investment bankers saw the acquisition as a positive and strategic move for USN as CT Tel would fill a gap in USN's offered services and geographical areas. The CT Tel acquisition and USN's successful initial public offering were completed in early 1998.

In early 1999, USN filed for bankruptcy. Peltz, USN's liquidation trustee, commenced an action against Hatten and all HCHC shareholders to recover money paid by USN to the HCHC shareholders for the HCHC shares. Peltz claimed that the transaction constituted a voidable fraudulent transfer under Chapter 11 of the United States Bankruptcy Code (**"USBC"**).

Chapter 11 of the USBC allows a liquidation trustee to apply to the courts to void certain transfers of money or property made by the bankrupt. The trustee must prove that the transfer was made within the year preceding the filing for bankruptcy, that the debtor received less than a reasonable equivalent value in exchange for his payment and that the debtor was insolvent on the date of the transfer or became insolvent because of the transfer.

After confirming that the transfer took place less than one year before USN filed for bankruptcy, the court examined whether USN received reasonable equivalent value in exchange for the U.S.$68 million it paid for CT Tel's shares.

The trustee argued that USN received less than reasonably equivalent value in exchange for the U.S.$68 million it paid for CT Tel. The trustee presented evidence from three expert witnesses who used DCF studies to value CT Tel's business at U.S.$43.5 million. The experts stated that the rapid growth the market had been experiencing had started to decline in 1996, especially for cellular resellers. Moreover, CT Tel was a mature company that needed to expand into new service and geographical areas in order to continue to grow. One expert noted that CT Tel's subscriber growth declined in the year before the transaction. Based on such factors, the experts used a 16% discount rate to estimate CT Tel's future cash flows for the purpose of their DCF study.

The HCHC shareholders claimed that USN received reasonably equivalent value for the price it paid for CT Tel's shares. It was submitted that since the CT Tel acquisition was part of USN's initial public offering, USN received more than equivalent value from the initial public offering combined with the acquisition. The shareholders and their expert witness raised several arguments to support the reasonableness of the purchase price. First, the market for cellular resellers was rapidly growing at the time of the transaction. Second, CT Tel was an attractive target because of its high gross margins, low customer turn-over rate and its unique ability to provide all of its services on one unified billing platform. Third, the court should not revise the purchase price because it was the result of arm's length negotiations between informed and sophisticated parties.

The shareholders argued that DCF studies, such as those performed by the trustee, should not be used to value CT Tel for three reasons. First, the DCF studies did not take into account the host of factors surrounding the transaction, such as market conditions. Second, a DCF study that is done retrospectively

does not reflect fair market value at the time of the transaction. Third, DCF analyses are often inaccurate because they depend on each valuator's perspective and assumptions.

The HCHC shareholders' expert witness valued CT Tel on the basis of per-subscriber price paid in three comparable transactions that were close in time to CT Tel's acquisition. In those three transactions, buyers paid a price ranging from U.S.$719 to U.S.$900 per customer or subscriber for companies that did not offer the same extensive range of services as CT Tel. Based on such comparison, the expert concluded that USN received reasonably equivalent value when it purchased the CT Tel shares for a price of U.S.$932 per subscriber.

The court rejected the use of DCF studies to determine CT Tel's value. In the court's opinion, DCF studies often produce uneven results. It was indicated that the input data for DCF studies is subjective since the valuator is required to estimate future cash flows, and to make judgments about the company's liquidity and about the cost of capital. The court found that the discount rate used in the trustee's DCF was excessive and that such a high discount rate was not supported by other factors or by the industry standard.

The court stated that a reasonably equivalent value cannot be determined by a fixed mathematical formula. Rather, courts must examine the totality of circumstances surrounding the transaction, deferring to marketplace values to determine whether a valuation is reasonable. Other important factors include the parties' good faith, the difference between the price paid and the fair market value, and whether the transaction was at arm's length.

Based on the evidence, the court concluded that the acquisition of CT Tel was an important strategic move for USN as it allowed the company to enter new service and geographical markets. Moreover, the court noted that USN conducted extensive due diligence and market research, and had consulted with investment bankers, venture capitalists as well as accounting and consulting firms with expertise in cellular companies. USN had extensive knowledge of the relevant facts and of the market, which allowed it to make an informed decision about CT Tel's value. In addition, the evidence regarding comparable sales in the relevant time period indicated that the price paid for CT Tel was in line with prevailing values that the market placed on such companies.

The court concluded that since the purchase price was agreed upon by sophisticated parties who made reasoned judgments about the value of assets that were supported by prevailing marketplace values and by the parties' reasonable perceptions about growth, risks and the market at the time, it was not the place of fraudulent transfer law to re-evaluate or question those transactions with the benefit of hindsight.

Summit Metals, Inc. v. Gray, et al.
2002 U.S. Dist. Lexis 15599
United States District Court for the District of Delaware
(August 20, 2002)

In determining whether a director of various affiliated companies acted fairly in a transaction involving self-dealing, a court should apply the two-part test of fairness, which looks at whether there was fair dealing among the parties and whether the transaction was concluded at a fair price.

The plaintiff Summit Metals, Inc. **("Summit")**, a Chapter 11 debtor, sought to have the court rescind a transfer by The Chariot Group, Inc. (**"Chariot"**), Summit's predecessor, of 92% of the shares of Chariot's subsidiary, Energy Savings Products, Inc. (**"ESP"**) to a defendant, HomeStar Acquisitions Corporation (**"HomeStar"**). Summit argued that the transfer should be rescinded on the basis of self-dealing since Gray, a defendant, signed the agreement transferring the shares of ESP as chairman of both the seller, Chariot, and the purchaser, HomeStar. HomeStar paid for the shares with a U.S.$15 million promissory note from Hallowell Industries, another corporation of which Gray was chairman. Three affiliated companies gave written undertakings to repay the promissory note should HomeStar default. Each of the three undertakings were also signed by Gray as sole director of each company. The transaction was not submitted to the shareholders of Chariot for approval. It had been approved by Gray in his capacity as the sole director of Chariot.

Summit also argued that the transfer price of U.S.$15 million was not fair and that the shares were worth more than such amount. This argument was based on allegations that the Canadian Imperial Bank of Commerce had valued ESP in excess of U.S.$20 million, that a written offer to purchase ESP for U.S.$17 million had been made by a third party and had been rejected, and that an independent accounting firm (retained on behalf of ESP) projected that ESP would, by 1998, have sales in excess of U.S.$31 million, gross profits in excess of U.S.$9.2 million, and net income in excess of U.S.$1.5 million.

Summit brought a motion for partial summary judgement on its claim for rescission of the transfer, among other issues. The court denied the motion on

the basis that there were issues of material fact in dispute that had to be determined at trial relating to the fairness of the ESP transaction and the fairness of the price that the ESP shares were transferred at.

In discussing the issues, the court stated that when directors of a corporation engage in a transaction involving self-dealing, the directors must demonstrate their utmost good faith and the most scrupulous inherent fairness of the bargain. The court referred to Weinberger v. UOP, Inc. (**"Weinberger"**), which indicated that fairness is composed of two parts: fair dealing and fair price. Fair dealing considers when the transaction was timed, how it was initiated, structured, negotiated, disclosed to the directors, and how the requisite approvals were obtained. Fair price relates to economic and financial considerations regarding assets, market value, earnings, future prospects and any other elements that affect a company's stock. The court indicated that when deciding the disputed issues relating to the fairness of the ESP transaction and the fairness of the price that the ESP shares were transferred at, the fairness factors set out in Weinberger should be considered.

Applebaum v. Avaya, Inc., et al.
2002 Del. Lexis 699
Supreme Court of Delaware
(November 20, 2002)

A reverse stock split (i.e., consolidation) followed by a forward stock split aimed at eliminating the expensive small shareholdings of a public company was found not to violate Section 155 of the Delaware General Corporation Law. The Supreme Court of Delaware confirmed the Court of Chancery of Delaware's decision that for the purposes of determining the "fair value" of the small shareholders' shareholdings pursuant to Section 155, fair market value of the common stock was a fair determinant of fair value. The court also found that shareholders of a company need not be treated equally, provided they are treated fairly.

The court was asked to determine whether or not the Court of Chancery of Delaware erred in finding that the fair market value of a publicly traded stock is "fair value" pursuant to Section 155 of the Delaware General Corporation Law (the **"DGCL"**). The plaintiff Applebaum, a minority shareholder of Avaya, Inc. (**"Avaya"**), had brought a motion in the lower court for summary judgment to prevent Avaya from executing a reverse stock split followed by a forward stock split intended to buy out the minority shareholders of Avaya.

Avaya is a public corporation that provides communications systems and software to businesses, government agencies and other organizations. Avaya's common stock is one of the most widely held stocks traded on the New York Stock Exchange (the **"NYSE"**). Each year, Avaya spends a significant amount of money to maintain small accounts for its minority shareholders. Approximately 3.3 million holders of Avaya common stock hold on average fewer than 90 shares. Of these stockholders, 947,000 own fewer than 50 shares. Avaya pays

approximately U.S.$3.9 million annually to maintain the accounts of those stockholders holding fewer than 50 shares.

In an attempt to reduce its significant annual expenditures, Avaya's board of directors proposed three alternative transactions. Each proposed transaction consisted of a reverse stock split, immediately followed by a forward stock split. Each proposed transaction would occur in the same manner, the difference between each alternative being the minimum number of shares that would be cashed out. The stockholders of Avaya holding fewer than the minimum number of shares at the time the stock split was to occur would be paid cash by Avaya for their stockholdings, rather than fractional shares. Avaya stockholders holding more than the minimum number of shares would not be affected by the reverse/forward stock split.

The board of directors recommended the three alternative transactions to the shareholders of Avaya, promising to determine at a future time, which of the three proposed alternatives would best suit Avaya. The board of directors reasoned that the proposed transactions would provide two significant advantages to the shareholders of Avaya that would be cashed out. First, Avaya would pay all transaction costs associated with the reverse/forward stock split. Second, since small shareholders would have advance notice of the reverse/forward stock split, there would be an opportunity for such shareholders to increase their shareholdings above the minimum amount, if they wished to continue to maintain an interest in Avaya and not be cashed out. On February 26, 2002, each of the three proposed transactions received shareholder approval.

Applebaum made a number of arguments in an attempt to oppose the reverse/forward stock split. First, it was argued that Section 155 of the DGCL did not permit Avaya to carry out the reverse/forward stock split in the manner proposed. Although the initial reverse stock split would create fractional interests for all Avaya stockholders, the fractional interests of Avaya stockholders whose interest fell below the minimum threshold would be treated differently from those stockholders whose interests were above the minimum threshold. The reason, it was argued, was because Avaya would pay cash to those small stockholders whose fractional interest fell below the minimum threshold, while it would provide whole shares to all other stockholders via the forward stock split. Applebaum argued that such differential treatment was not permitted.

The court confirmed the Court of Chancery of Delaware's rejection of the foregoing argument stating that Section 155 of the DGCL did not contain any express language prohibiting Avaya from treating large and small stockholders differently. The court also confirmed that stockholders need not always be treated equally for all purposes. The court stated that it made no sense to construe the statute to require uniformity in dealing with the disposition of fractional interests created in transactions, as long as shareholders were treated fairly. The court concluded that Section 155 of the DGCL was available to Avaya for its proposed transaction.

Applebaum's second main argument was that even if Section 155 of the DGCL applied to the proposed transaction, neither of the two methods proposed to eliminate shareholdings below the minimum number complied with the statute. The two methods of payout involved either (i) Avaya's transfer agent aggregating and selling the fractional shares of the small shareholders in the open market, or (ii) Avaya paying cash for the fractional shares based on the fair value of the common stock being cashed out. In regards to the second alternative, the method for determining the fair value of the stocks being paid out would involve Avaya paying an amount equal to fair market value. Fair market value would be determined by taking the average closing price per share of Avaya's common stock on the NYSE for a period of ten consecutive trading days ending on the date the reverse and forward stock split would occur.

As the second method of payout was the method that Avaya intended to use in the proposed transaction, the court first considered such method. The court had to determine whether fair market value was equal to "fair value" under Section 155 of the DGCL in this case. Applebaum argued that "fair value" under the statute should not be determined by relying exclusively on the market value of the common shares. Instead, it was argued that "fair value" under Section 155 of the DGCL should be interpreted in a manner similar to the interpretation of "fair value" in Section 262 of the DGCL, the appraisal section. In Section 262, market value is just one factor considered in determining "fair value." Under such section, the trading price of a share includes an inherent minority discount that must be backed-out to derive fair value.

In considering the meaning of "fair value" under Section 155 of the DGCL, the court confirmed the decision that fair market value did in fact constitute "fair value" under the statute. The following reasons were cited in support of the court's conclusion. First, the court described a number of market characteristics

of Avaya common stock. Specifically, Avaya common stock was widely held, there was no controlling stockholder and it was traded on the NYSE. The market for Avaya common stock was also highly liquid. It had a three week average daily trading volume of 1.21 million shares. The court found that given such market characteristics, the proposed transaction would not result in any significant change to Avaya common stock as the common stock would continue to be listed and traded on the NYSE and it would remain a widely held and highly liquid security. The court confirmed that the Court of Chancery of Delaware had correctly concluded that a well-informed, liquid trading market will provide a measure of fair value superior to any estimate of fair value that a court could impose. Second, small shareholders of Avaya common stock who did not want to be cashed out by the reverse/forward stock split would have an opportunity to maintain their Avaya common stock holding. Since such shareholders would receive advance notice of the dates the reverse/forward stock splits were to occur, these shareholders would have the opportunity to purchase the amount of shares necessary to meet the minimum amount of shares and not be subject to the cash payout. In addition, those shareholders who would be cashed out would have the ability to repurchase Avaya common stock on the NYSE in order to reacquire the same ownership position held prior to the occurrence of the reverse/forward stock split. Third, the cash payment that would be made to the small shareholders of Avaya for its shares would not be reduced by transaction costs, which ordinarily amount to a significant portion of the total proceeds of a sale.

As the first method of payout was intended as a fall-back in the event that the second method failed, the court confirmed the decision that should the first method of payout be used, such method would be permitted by Section 155 of the DGCL.

III. REGULATORY DEVELOPMENTS

Proposed Amendments to the TSX Company Manual

The Toronto Stock Exchange (**"TSX"**) has recently proposed various amendments to certain provisions of the TSX Company Manual as a result of a review of the TSX's current written and unwritten standards and practices, a comparative analysis of standards and practices of other exchanges, and consultations with key stakeholders across Canada. The proposed amendments are subject to the approval of the Ontario Securities Commission. The period for public comments on the proposed amendments expired on October 2, 2002. As of the date of publication, the TSX has not published any comments received.

Recently proposed amendments to The Toronto Stock Exchange Company Manual would amend the definition of "market price" from the closing price of the listed security to the five day volume weighted average trading price and would give The Toronto Stock Exchange the discretion to shorten or lengthen the applicable calculation period, based on a number of relevant factors.

Among the proposals is the amendment to the existing definition of "market price", which is used in the private placement provisions of the TSX Company Manual. The TSX Company Manual currently determines "market price" of listed securities based on the closing price on the trading day prior to the TSX's receipt of notice of the proposed transaction. The TSX proposes amending "market price" to mean the volume weighted average trading price of the listed securities for the five trading days immediately preceding the relevant date. In the event that the five day volume weighted average trading price does not, in the opinion of the TSX, accurately reflect the securities' current market price, the volume weighted average trading price may be adjusted for such shorter or longer period as the TSX determines in their discretion, based on a number of relevant factors. These factors include (a) liquidity; (b) trading activity immediately before, during or immediately after the relevant period; and (c) any material events, changes or announcements occurring immediately before, during or immediately after the relevant period. If the listed securities are suspended from trading or have not traded on the TSX or another stock exchange for an extended period of time, "market price" will be the fair market value of the listed securities, as determined by the listed issuer's board of directors.

According to the TSX, the proposed amendment to the definition will allow issuers greater flexibility in structuring their transactions, while at the same time reducing the possibility that the market price can be artificially manipulated.

Proposed National Instrument 81-106 - *Investment Fund Continuous Disclosure*

The Canadian Securities Administrators recently proposed draft National Instrument 81-106 - Investment Fund Continuous Disclosure, which would impose certain continuous disclosure obligations on investment funds. Specifically, labour sponsored investment funds would be required to file a statement of investment portfolio containing, where the current value of securities is not readily available, an independent formal valuation of its securities prepared in accordance with the proposed national instrument.

The Canadian Securities Administrators recently published for comment proposed National Instrument 81-106 - *Investment Fund Continuous Disclosure* (**"NI 81-106"**). NI 81-106 would apply to all types of investment funds, including mutual funds, labour sponsored investment funds, exchange traded funds, split share corporations, closed end funds and scholarship plans. If approved, NI 81-106 would require investment funds to file annual and interim financial statements which would include statements of investment portfolio. NI 81-106 permits a labour sponsored investment funds to obtain and file a formal independent valuation prepared in accordance with NI 81-106 in lieu of disclosing in its statement of investment portfolio the fair value of securities which it holds and for which a market value is not readily available. The period for public comments on NI 81-106 expired on December 19, 2002. As of the date of publication, the Canadian Securities Administrators has not published any of the comments received.

Proposed National Instrument 71-102 - *Continuous Disclosure and Other Exemptions Relating to Foreign Issuers*

The Canadian Securities Administrators recently published for comment National Instrument 71-102 - Continuous Disclosure and Other Exemptions Relating to Foreign Issuers, which, among other things, exempts eligible foreign issuers from the valuation requirements of Canadian securities laws.

On June 21, 2002 the Canadian Securities Administrators published for comment proposed National Instrument 71-102 - *Continuous Disclosure and Other Exemptions Relating to Foreign Issuers* (**"NI 71-102"**) and the related companion policy.

NI 71-102 provides that an eligible "SEC Foreign Issuer" or "Designated Foreign Issuer" may satisfy the continuous disclosure, insider reporting requirements, early warning and certain other requirements of Canadian securities laws by complying with the applicable requirements of their home jurisdiction and concurrently filing and sending in Canada the documents that were filed and sent under the requirements of the issuer's home jurisdiction. Such issuers would also be exempt from, among other things, the valuation and minority approval requirements of Canadian securities laws (including the applicable requirements contained in Ontario Securities Commission Rule 61-501 - *Insider Bids, Issuer bids, Going Private Transactions and Related Party Transactions*), provided that, in the case of an SEC Foreign Issuer, less than 20% of the issuer's equity securities are owned of record, directly or indirectly, by residents of Canada. NI 71-102 does not relieve foreign issuers that electronically file under NI 13-101 - *SEDAR* or their insiders from the insider reporting requirements under SEDI.

NI 71-102 would also permit foreign issuers to file financial statements prepared in accordance with U.S. GAAP, International Accounting Standards or the accounting principals accepted in their home jurisdiction, without reconciliation to Canadian GAAP.

The period for comment on NI 71-102 expired on September 19, 2002. As of the date of publication, the Canadian Securities Administrators has not published any of the comments received.

Amendment to Section 171 of the Alberta Securities Commission Rules

Section 171 of the Alberta Securities Commission Rules (the **"ASC Rules"**) was amended effective June 12, 2002 to make them consistent with British Columbia and Ontario law. The amendments relieve an offeror from the valuation requirements in Section 171(2) of the ASC Rules when consummating a going private transaction if certain specified conditions are satisfied. Under the ASC rules, a valuation is not required where:

The Alberta Securities Commission Rules were amended effective June 12, 2002 to relieve offerors in certain circumstances from the satisfying the valuation requirements imposed in the context of a formal take over bid.

(a) the going private transaction is completed no later than 120 days after the expiry of the formal bid;

(b) the intent to effect the going private transaction was disclosed in the take-over bid circular or the issuer bid circular; and

(c) the consideration for security paid in the going private transaction:
  (i) is at least equal in value to the consideration per security that was paid in the formal bid; and
  (ii) is in the same form as the consideration per security that was paid in the formal bid, and if the consideration paid consisted of securities, consists of the same securities.