CITATION: Growthworks WV Management Ltd. v. Growthworks Canadian Fund Ltd., 2018 ONSC 3108
COURT FILE NO.: CV-13-10279-00CL
DATE: 20180518

ONTARIO

SUPERIOR COURT OF JUSTICE

BETWEEN:	
GROWTHWORKS WV MANAGEMENT LTD. Plaintiff	*Melvyn L. Solmon* and *Nancy J. Tourgis*, for the Plaintiff
- and -	
GROWTHWORKS CANADIAN FUND LTD. Defendant	*Geoff R. Hall, Atrisha Lewis, Sapna Thakker* and *Sharanya Thavakumaran*, for the Defendant
	HEARD: July 18, 19, 20, 21, 24, 25, 26, 27 and 28, 2017

Wilton-Siegel J.

REASONS FOR JUDGMENT

[1] In this action, GrowthWorks WV Management Ltd. (the "Former Manager") claims fees it says are owing pursuant to a management agreement pertaining to the GrowthWorks Canadian Fund Ltd. (the "plaintiff" or the "Fund") and certain additional amounts for transition services after termination of the management agreement. The Fund asserts that it terminated the management agreement for cause and asserts certain damage claims against the Former Manager for breach of the management agreement.

The Fund, the Former Manager and their Contractual Relationship

The Parties

[2] The Fund is a corporation incorporated under the *Canada Business Corporations Act,* R.S.C. 1985, c. C-44 (the "CBCA"), which carried on the business of a mutual fund as a labour-sponsored venture capital corporation (an "LSVCC"). It was formed in 1988 with the investment objective of achieving long-term appreciation for its Class A shareholders, which principally

consist of retail investors. LSVCCs, including the Fund, must be "sponsored" by a labour organization. The Fund's sponsor is the Canadian Federation of Labour (the "Sponsor").

[3] The Fund is registered under the *Income Tax Act (Canada)*, the *Labour-Sponsored Venture Capital Corporations Act (Manitoba)* and the *Community Small Business Investment Funds Act (Ontario)*, and was approved under the *Labour-sponsored Venture Capital Corporations Act (Saskatchewan)*. The Fund is also an "investment fund" and a "mutual fund" for the purposes of the *Securities Act (Ontario)* and a "reporting issuer" under applicable securities laws in each of the provinces and territories of Canada.

[4] The Former Manager is also a corporation incorporated under the CBCA. The Former Manager is a wholly-owned subsidiary of GrowthWorks Ltd. ("GrowthWorks"), which also owns GrowthWorks Capital Ltd. ("GWC"). In these reasons, the term "Former Manager" includes GWC unless the context specifically requires otherwise.

[5] The Former Manager, GrowthWorks and GWC are direct or indirect subsidiaries of Matrix Asset Management Inc. ("Matrix"), which was a TSX-listed diversified asset management company until it filed a proposal in bankruptcy which was accepted by its creditors in 2015.

[6] During the period addressed in these Reasons, the Former Manager along with GWC also managed three investment funds apart from the Fund, namely the Working Opportunity Fund (EVCC) Ltd. (the "WOF"), based in British Columbia, the Commercialization Fund (the "Comm Fund") and the Atlantic Venture Fund (collectively the "Other GrowthWorks Funds").

[7] David Levi ("Levi") was the President and Chief Executive Officer of the Former Manager at all relevant times until the date of termination of the Management Agreement. He is the President and Chief Executive Officer of GrowthWorks and the Executive Vice President and a Director of GWC. Levi was also the president and chief executive officer of Matrix or its predecessor from 2010 until 2015.

<u>The Equity Capital of the Fund</u>

[8] The authorized capital of the Fund consists of (i) an unlimited number of Class A Shares ("Class A Shares"), issuable in series; (ii) an unlimited number of Class B Shares ("Class B Shares"); and (iii) an unlimited number of Class C shares ("Class C Shares"), issuable in series.

[9] On September 30, 2013, there were 30,630,098.8815 Class A Shares outstanding, all of which were held by individuals or registered plans established for the benefit of individuals.

The Class A Shares

[10] The Class A Shares may be issued to individuals, registered retirement savings plans and other persons permitted by legislation. Class A Shares are voting shares and were issued to the public on a "continuous offering basis" by way of a prospectus filed with Canadian securities regulatory authorities. As described below, the Fund ceased offering Class A Shares for sale to

the public on September 30, 2011 due to poor sales activity, primarily resulting from a change in the tax incentives available in the Province of Ontario for LSVCCs that is described below.

[11] The Class A Shares (i) are retractable (i.e. redeemable on demand by the holder), after eight years, subject to certain conditions and the restrictions in the CBCA generally applicable to the purchase and redemption of shares; (ii) subject to some restrictions, entitle the holder to receive dividends at the discretion of the Board; and (iii) entitle the holder to share rateably with other Class A shareholders in distributions on wind-up or dissolution of the Fund. In these Reasons, the retraction privilege is referred to as a right of redemption in line with the usage of the Fund.

[12] The Class A Shares are not listed or quoted on any stock exchange or over-the-counter market and no market exists through which Class A Shares may be sold. As a practical matter, Class A shareholders must therefore rely on redemptions to dispose of their Class A Shares. A Class A shareholder who elected to redeem Class A Shares prior to the eighth anniversary of the date the shareholder purchased the Class A Shares would generally have had to repay an amount in respect of the tax credit received by the shareholder on the purchase of their Class A Shares and would have been required to pay an early redemption fee to the Manager that varied according to the series of Class A Shares held.

The Class B Shares

[13] All of the outstanding Class B Shares are held by the Sponsor. The holder of the Class B Shares is not entitled to receive dividends. The holder of the Class B Shares is, however, entitled to elect a majority of the Fund's directors. Of the twelve members of the Board, eight were elected by the holder of the Class B Shares. On dissolution of the Fund, the holder of the Class B Shares would only be entitled to receive an amount equal to the purchase price paid for such shares, which is a nominal amount.

The Class C Shares

[14] The Fund also created a non-transferable series of Class C Shares designated as "IPA Shares." All of the outstanding Class C Shares, being 100 IPA Shares, have been issued to and are held by the Former Manager. The IPA Shares are the vehicle by which the Former Manager participated in realized gains and the cumulative performance of the Fund's venture capital investments. The share conditions of the IPA Shares are described in Schedule "A."

Management of the Fund

The Board of Directors

[15] The board of directors of the Fund (the "Board") was responsible for providing strategic direction to the Fund and oversight of the management of the Fund. It consisted of twelve members. As of September 30, 2013, the directors of the Fund included Levi, C. Ian Ross ("Ross"), the Chairman of the Board, and Nancy E. Hopkins ("Hopkins"), all of whom testified at this trial.

Committees of the Board

[16] The Board established a number of committees, of which the investment committee (the "IC") and the audit and valuation committee (the "AVC") existed from the time of the Former Manager's engagement and were involved in the events giving rise to this litigation.

[17] The mandate of the IC was to establish policies and procedures for the Fund's acquisition, management and disposition of investments and to monitor existing investments on an on-going basis. Subsequently, the IC assumed the role of monitoring the liquidity position and challenges of the Fund until the creation of the SC described below.

[18] In November 2007, the Board created an independent review committee (the "IRC") whose mandate was principally to review conflict of interest matters involving the Former Manager as well as to review and report on the adequacy and effectiveness of the Former Manager's written policies and procedures.

[19] In the second half of 2010, the Board also created a special committee (the "SC") chaired by Ross. The SC's mandate was to address two significant issues – initially the Proposed VenGrowth Transaction described below and subsequently the liquidity status and challenges of the Fund.

The Officers of the Fund

[20] Consistent with the scope of the Services (as defined below), Levi was appointed as the President and Chief Executive Officer of the Fund, and the Former Manager's legal counsel was appointed as the Fund's corporate secretary. In addition, an employee of the Former Manager, Clint Matthews, was appointed the Chief Financial Officer of the Fund in the spring of 2008. These individuals held these positions with the Fund until the termination of the Management Agreement in September 2013.

The Former Manager

[21] The Fund retained the Former Manager to manage the business of the Fund. The Fund had previously managed its affairs internally since its formation. The Former Manager was first engaged by the Fund in 2002, after being selected in a competitive bid process, and entered into a management agreement with the Fund at that time (the "initial management agreement"). As a consequence of engaging the Former Manager, the Fund ceased to have any employees. Between 2002 and 2006, the Fund acquired several other LSVCCs pursuant to merger transactions with their shareholders.

[22] The relationship between the Former Manager and the Fund was then restated pursuant to an amended and restated management agreement dated July 15, 2006 (the "Management Agreement"). The services to be performed by the Former Manager are set out in paragraphs 3.1 and 3.2 of the Management Agreement (herein, the "Services"). The scope of the Services is very broad and effectively includes all management services necessary to properly manage the day-to-day operations and business of the Fund, including managing the Fund's investment activities and administering its operations. It is agreed that the Services included providing

advice and recommendations to the Board regarding the strategic direction of the Fund, including its liquidity management.

[23] Section 3.4 of the Management Agreement contains a specific provision that required the Former Manager to comply with securities laws and regulations and the requirements of the Canadian securities administrators and policy statements of securities regulatory authorities insofar as they related to the Former Manager's duties and obligations under the Management Agreement.

[24] Section 3.5 of the Management Agreement constitutes a contractual obligation of care and skill of the Former Manager. It provides as follows:

> The [Former] Manager shall exercise the powers and authorities granted hereunder and discharge its duties hereunder honestly, in good faith and in the best interests of the Fund and, in connection therewith, shall exercise the degree of care, diligence and skill that a reasonably prudent person would exercise in the circumstances.

This contractual obligation is hereinafter referred to as the "Standard of Care."

[25] As described further below, the Former Manager was obligated to pay from its own resources, without reimbursement, all usual operating expenses of the Fund incurred in providing the Services. The Fund was responsible for paying the fees payable to the Former Manager described below, the fees of the Board and certain other expenses and tax obligations of the Fund, including as addressed below any expenses that were unusual and not expenses of the usual day to day operations of the Fund.

[26] As compensation for performance of the Services, the Manager was entitled to receive management and administration fees (collectively, the "Fees"). The Fees were calculated based upon the average net asset value ("NAV") from time to time of the assets of the Fund, being the total value of all securities in the Fund's portfolio less the Fund's liabilities. The Former Manager was required to calculate the NAV once a week. The value of the Fund's venture capital investments was based, among other things, on the amount invested in each company and the projection for the timing and value of divestiture proceeds for such investments.

[27] In addition, the Former Manager was also entitled to receive additional compensation as the manager of the Fund based upon the returns realized by the Fund upon the disposition of the Fund's venture capital investments. As mentioned, such compensation took the form of dividends on the IPA Shares (the "IPA Dividends").

[28] In accordance with its rights under the Management Agreement, the Former Manager delegated all of its obligations under the Management Agreement to GWC. GWC was a "registrant" for purposes of applicable provincial securities laws and conducted those activities of the Former Manager which required registration under those laws. As such, GWC was subject to the regulatory oversight and authority of the British Columbia Securities Commission (the "BCSC") and other provincial securities regulatory authorities. The BCSC had primary

jurisdiction over GWC due to the fact that the GWC's principal offices were, at all relevant times, located in Vancouver, British Columbia.

[29] In addition, pursuant to paragraph 3.6 of the Management Agreement, the Former Manager was permitted to engage third party service providers in connection with providing the Services. Pursuant to this provision, the Former Manager, directly or through GWC, engaged, among others, Just Systems Inc., now Unitholder Management Plus Inc. ("Just Systems"), FundSERV Inc. ("FundSERV"), and Concentra Trust ("Concentra"). The Former Manager asserts certain claims for reimbursement of the fees of these entities, which are addressed below.

The Business of the Fund

[30] The Fund is a retail venture capital fund. As such, the Fund raised capital, made venture capital investments, and sold its investments in the ordinary course of its business. The Fund invested in a diversified portfolio of small and medium-sized Canadian businesses. The Fund typically made venture capital investments in early to mid-stage private companies. On the date of termination of the Management Agreement, the Fund had approximately 20 active investee corporations and 60 inactive investee corporations.

[31] The timing of the Fund's sale or divestment of its venture capital investments was driven by a number of factors, including the Fund's liquidity needs, the stage of development and prospects of its investments, and the state of the IPO and M&A markets, which are the markets in which the Fund typically sold or divested its venture capital investments. Venture capital investments typically require time for favourable divestiture or exit opportunities to arise even after an investment has developed to the stage where it can be sold or divested. Forced sales of venture capital investments prior to the occurrence of viable exit or divestiture opportunities generally result in divestiture values that are lower than prevailing carrying values, which would result in portfolio losses.

[32] In order to achieve the Fund's objective of disposing of an investment at a time that would maximize returns for the Fund, the Fund generally made an initial investment in a company, which was followed by rounds of subsequent or "follow-on" investments. Follow-on investing is a key element of the investment life cycle of a venture capital fund. Venture capital funds do not typically provide initial funding that will fully support a portfolio company's development to a stage at which it can generate income sufficient to sustain its operations. Rather, follow-on investments are made as each portfolio company achieves financial or operational milestones. Of note, however, the failure to participate in follow-on rounds of financing could often lead to adverse consequences for a fund, including: (1) significant dilution of the fund's shareholdings in a portfolio company; (2) penalties such as loss of anti-dilution rights and board representation; and (3) forced conversion of preferred shares into common shares.

[33] It is also important that, unlike private venture capital funds, the Fund as an LSVCC could not raise additional capital to fund its liquidity needs by capital calls on its investors. The Fund had to rely instead on the sales of additional Class A Shares. Further, unlike a private venture capital fund, it was subject to redemption requests of holders of Class A Shares, which presented an additional liquidity consideration.

Tax Matters Pertaining to the Fund

[34] To encourage Canadian retail investors to invest in LSVCCs, the federal government and some provincial governments offered investment tax credits in respect of the shares of LSVCCs. Beginning in the 1980s, the federal government offered LSVCC investors a 15% tax credit on a maximum investment amount of $5,000 per year, providing up to $750 in federal tax relief. Most provincial governments also offered an additional 15% tax credit on eligible LSVCC investments, creating a total federal and provincial tax credit of 30%.

[35] As described above, Class A Shares that were redeemed earlier than eight years from their date of acquisition attracted penalties by way of repayment of the favourable tax treatment received at the time of acquisition. Conversely, after the eight-year hold period, the Class A Shares were retractable without any penalty. Because most Class A Shares were typically purchased during RRSP season (being January and February in each year), redemption requests also tended to be made during the RRSP season in any given year.

[36] Accordingly, the Fund was required to retain sufficient cash reserves to be able to satisfy the redemption demands in respect of all Class A Shares to which the eight-year hold no longer applied. Such shares are referred to as "hot money" shares or "hot money" capital. As set out below, redemptions historically ran at the approximate rate of 35% of all "hot money" shares in the relevant period. However, because of the sales history in earlier periods, the total amount of "hot money" capital was scheduled to increase significantly, relative to prior years, beginning with the 2009 RRSP season (being January and February 2009) necessitating larger cash reserves in 2009 and following.

[37] In mid-2005, the Ontario Government announced that it would phase out the Ontario investment tax credit over a five-year period, subsequently extended by one year, with the amount of the tax credit declining over the period. As discussed below, this had a significant adverse effect on the ability of the Fund to raise capital by the sale of Class A Shares in Ontario, which was the principal market for the Fund.

Overview of the Activities of the Fund from the Engagement of the Former Manager

[38] The following summarizes the factual background leading to the termination of the Management Agreement and this litigation.

[39] The Former Manager took over day-to-day management of the Fund on December 1, 2002. On November 27, 2003, the initial management agreement was entered into by the Fund and the Former Manager.

[40] Sales of Class A shares generated by the Fund were respectively $35,669,000, $11,754,000, $9,130,000 and $12,988,000 in the fiscal years ending August 31, 2002, 2003, 2004 and 2005, respectively. As mentioned, given the eight-year hold associated with the taxation credit, the Fund anticipated a heavy redemption experience commencing with the twelve-month period ending with the 2009 RRSP season.

Events Between 2005 and 2009

[41] As at August 31, 2005, the Fund had cash and liquid assets totaling $124,974,000 and a total NAV of $269,144,000. At this time, the Fund was in the course of negotiating acquisition transactions with the Canadian Science & Technology Growth Fund ("CSTGF") and the Capital Alliance Ventures Inc. ("CAVI"), both of which were suffering from a lack of liquidity. These transactions were approved by the Board on October 20, 2005, were approved by the shareholders of the Fund on November 17, 2005, and closed on November 29, 2005.

[42] On August 29, 2005, the Government of Ontario announced that it intended to eliminate the tax credit for LSVCCs by the end of the 2005 taxation year. As mentioned above, subsequently, on September 30, 2005, the Government of Ontario announced that it had decided to phase out the investment tax credit for LSVCCs by the end of the 2010 taxation year, reducing the taxation credit gradually over the five-year period. Legislation giving effect to this subsequent announcement was passed on December 15, 2005.

[43] Accordingly, the ability of LSVCC's, including the Fund, to count on receiving substantial additional funds annually from new Ontario retail investors was significantly reduced after 2005 and was necessarily going to be severely restricted after the 2010 fiscal year. Ontario was the predominant market for the sale of the Fund's Class A shares. In the short-term, however, in the case of a number of LSVCCs, the change in the tax credit created or exacerbated liquidity problems that presented favourable merger opportunities for other LSVCCs which had sufficient liquid assets, including the Fund.

[44] In the spring of 2006, the Former Manager pursued two further acquisition transactions on behalf of the Fund. On March 22, 2006, the Board approved the purchase of the First Ontario Fund ("FOF"), which was completed on July 14, 2006.

[45] As at August 31, 2006, the Fund had cash and liquid assets totaling $176,218,000.

[46] On December 13, 2007, the Government of Ontario announced certain amendments to the phase-out of the provincial tax credit for investors in LSVCC shares, including a one-year extension to March 1, 2011. However, the announcement confirmed the Government's intention to proceed with the phase out.

[47] As of August 31, 2007, the Fund's NAV was approximately $366 million and it had liquid assets totaling approximately $118 million. This large liquidity position reflected two successful divestitures of venture capital investments of $95.6 million over the period between 2004 and 2007 and $73 million in 2007, respectively. As of August 31, 2008, the comparable figures were $321 million and $126 million. In short, the Fund had no liquidity issues up to and including this latter date and, in particular, had sufficient funds to meet its projected redemptions.

[48] As described further below, however, the economic crisis that developed in the fall of 2008 significantly affected the venture capital financing market and the M&A and IPO markets for divestitures of venture capital investments. Notwithstanding this development, during the remainder of 2008, the Fund was able to negotiate the acquisition of another LSVCC that had

encountered liquidity problems – the ENSIS Growth Fund Inc. This transaction (the "ENSIS Transaction") closed on October 22, 2008.

[49] In the spring of 2009, the Fund entered into a further merger transaction with the Canadian Medical Discoveries Fund ("CMDF"), which had suspended redemptions due to liquidity problems (the "CMDF Transaction"). The CMDF Transaction was approved by the Board on April 23, 2009 and closed on May 25, 2009.

Events in 2010

[50] By late 2009, the Fund was experiencing a significant reduction in its liquidity as a result of several factors, principally the following: (1) the adverse markets for the divestiture of its venture capital investments following the 2008 economic crisis, which continued to depress markets in 2009 and into 2010; (2) the decline in sales of its Class A Shares as a result of the announced tax changes; and (3) an increase in redemptions of such shares as well as an increase in the amount of "hot money" shares, which reflected the level of sales eight years earlier.

The WOF Credit Facility

[51] In early 2010, in anticipation of possible increased redemptions or reduced fundraising during the 2010 RRSP season, the Former Manager arranged for a credit facility of $15 million to be made available to the Fund by the WOF. The WOF credit facility was approved by the Board at its meeting on March 1, 2010. The minutes of the Board meeting describe this WOF credit facility as a short-term, secured bridge loan to the Fund to enable it to address "short-term liquidity needs" pending a longer-term financing solution. This WOF credit line was put in place on March 23, 2010, could be drawn down until June 30, 2010 and was to be repaid by November 30, 2010. However, the WOF credit facility was never drawn upon and, instead, was rescinded on payment of a fee of $100,000 on June 28, 2010 after the Roseway Transaction (described below) was implemented. Levi says that the Former Manager had also arranged for a potential credit facility in the amount of $4 million from Matrix during the same period that was not however put in place.

The Roseway Transaction

[52] In April 2010, the Former Manager recommended a transaction with Roseway Capital LP ("Roseway") pursuant to which the Fund borrowed $20 million repayable after three years (the "Roseway Transaction"). The Roseway Transaction was approved at a Board meeting on April 27, 2010 and closed on May 28, 2010, at which time all of the monies available under the loan arrangements were drawn down by the Fund.

[53] The Roseway Transaction was set out in a participation agreement dated May 28, 2010 (the "Participation Agreement") under which Roseway advanced $20 million to the Fund in exchange for a "participation interest" in a defined basket of the Fund's venture capital investments (the "Defined Portfolio"). The participation interest generally entitled Roseway to receive participation payments equal to 20% of the proceeds realized by the Fund on the disposition of the investments in the Defined Portfolio. However, regardless of the performance of the Defined Portfolio, the Fund was also required to make minimum annual participation

payments to Roseway of $5.7 million in each of the first three years for a total of $17.1 million, which equated to a simple rate of interest of 28.5% per annum based on the original $20 million advance, and was required to repay the $20 million to Roseway on May 28, 2013. The Fund's payment obligations under the Participation Agreement are herein referred to as the "Roseway Obligations".

[54] The Roseway Obligations were secured by way of a security interest over all of the Fund's assets, subject to certain exceptions that are not material for present purposes, granted by the Fund in favour of Roseway pursuant to a security agreement dated May 28, 2010 (the "Roseway Security Agreement" and, together with the Participation Agreement, the "Roseway Documents").

[55] Concurrently with the execution of the Participation Agreement, the Former Manager also entered into a defined portfolio services agreement with Roseway pursuant to which the Former Manager agreed to provide certain monitoring and reporting services to Roseway in relation to the Defined Portfolio in exchange for an annual fee of $100,000.

Events in 2011

[56] By the beginning of 2011, the Fund required further liquidity to fund redemptions during the 2011 RRSP season and to remain compliant with certain financial covenants in the Roseway Transaction. The Former Manager explored financing possibilities with a number of Canadian and foreign banks, secondary investors and institutional funds with alternative high-yield alternative vehicles. None of these discussions resulted in viable offers of financing.

The WOF Loan

[57] In the absence of other alternatives, the Former Manager recommended to the Board that the Fund enter into a loan agreement for a loan of $9.5 million (the "WOF Loan") from the WOF. The WOF Loan bore interest at the rate of 12% per annum and originally matured on March 31, 2012. The WOF Loan was secured by a charge over the Fund's assets pursuant to a security agreement dated as March 31, 2011 between the Fund, WOF and 2275177 Ontario Inc., a company controlled by the Former Manager. The terms of the WOF Loan and related security were structured and negotiated on behalf of the Fund by the Former Manager.

[58] The WOF Loan was approved by the Board on February 21, 2011 and was finalized on March 31, 2011. However, the first draw under the WOF Loan did not occur until June 2011, due principally to lower than projected redemptions during the 2011 RRSP season. The WOF Loan was initially conceived of as a bridge loan until the credit facility for the Proposed VenGrowth Transaction described below was drawn down. However, the WOF Loan was eventually drawn down notwithstanding the fact that the Proposed VenGrowth Transaction did not proceed.

The Proposed Vengrowth Transaction

[59] Commencing in November 2010, the Former Manager pursued a further acquisition transaction with VenGrowth Funds with the approval of the Board (the "Proposed VenGrowth

Transaction"). While the initial impetus for this transaction may have been discussions with a prospective lender to the Fund, the Former Manager recommended this action, among other reasons, because it would increase the liquidity position of the Fund if it were completed on the terms proposed by the Former Manager. On May 30, 2011, the Board approved the Former Manager's proposal to acquire the VenGrowth Funds by way of a merger. Ultimately, however, in July 2011, the shareholders of the VenGrowth Funds rejected the Fund's offer in favour of a competing merger proposal.

[60] In connection with the Proposed VenGrowth Transaction, however, the Former Manager also pursued financing options to address potential liquidity requirements of the Fund if the merger were implemented. This resulted in a financing facility being put in place, although not drawn down, in March 2011 and a fee being paid to a third party agent who had arranged the facility.

The Suspension of Share Sales

[61] By the fall of 2011, sales of Class A Shares had decreased significantly. In a memorandum to the Board for its meeting on September 27, 2011, the Former Manager recommended to the Board that the Fund cease offering such shares to the public. The Board accepted this recommendation. The Fund ceased offering its Class A Shares on September 30, 2011.

The Suspension of Redemptions of Class A Shares

[62] In October 2011, the Board concluded that the Fund's liquidity was no longer sufficient to support continued redemptions of Class A Shares and to satisfy its liabilities, including minimum participation payments to Roseway under the Participation Agreement, principal and interest payments under the WOF Loan, and the fees payable to the Former Manager.

[63] At a special Board meeting held on October 27, 2011, the Former Manager recommended a redemption management plan (herein the "RMP") that would limit shareholder redemptions of Class A Shares on a managed basis, essentially as the Fund's cash flow resources permitted commencing with a cap of $20 million annually. For comparative purposes, redemptions in the period ending March 31, 2011 totalled $48.4 million and, in the Former Manager's memorandum provided for the June 8, 2011 Board meeting, were projected to be $40.6 million, $48.5 million and $38.4 million for the 12-month periods ending March 31, 2012, 2013 and 2014, respectively.

[64] With the concurrence of Ross, the Former Manager had previously approached the BCSC to seek permission to implement a cessation of redemptions on general terms to be determined by the Board. The BCSC indicated, however, that it was only prepared to grant such permission after a review which would take time. Counsel therefore decided to apply instead for an order authorizing a complete cessation of redemptions of Class A Shares for a limited period of time until the RMP could be implemented. Accordingly, the BCSC issued an interim order on November 10, 2011 permitting the complete cessation of redemptions of Class A Shares for a limited period of time and, on that date, the Fund suspended redemptions of Class A Shares.

[65] The BCSC order was effective until April 12, 2012. Subsequently, the BCSC also required shareholder approval, which was obtained. In the meantime, certain discussions which are discussed below took place between the BCSC and both the Former Manager and the Board. Pending the outcome of the BCSC's review of the Fund's application for approval of the RMP, the BCSC order was extended to July 31, 2012 and then to November 30, 2012. Ultimately, on November 30, 2012, the BCSC denied the Fund's request for approval of the RMP. However, by that date, the liquidity position of the Fund was such that it was unable to comply with the solvency test in section 36 of the CBCA in respect of redemptions of the Class A Shares. Accordingly, the Fund continued to suspend redemptions thereafter for this reason.

The Kirchner Letter

[66] On October 12, 2011, the Fund received an expression of interest from Kirchner Portfolio Management Corp. ("Kirchner Letter") respecting a possible purchase of Fund assets by that firm. The Kirchner Letter suggested that the applicable discount to net asset value in the transaction that it contemplated would be in the range of 60% to 90%, subject to due diligence. The proposal was addressed by the Board at its meeting held on November 16, 2011 at which time the Board decided not to pursue the offer. The reasons for this decision are not in evidence.

Events in 2012

[67] The Fund continued to face liquidity challenges in early 2012. By February 3, 2012, the WOF Loan had been fully drawn. There continued to be reduced divestiture activity in the M&A markets and a payment of $5.7 million was due to Roseway on May 28, 2012.

The Board Strategy for Addressing Liquidity Management

[68] To address its liquidity needs, on the recommendation of the Former Manager, the Board resolved on a policy of selling part of the Fund's portfolio and of funding its liquidity requirements in the interim by means of new financing arrangements. Accordingly, in May 2012, the Former Manager negotiated an extension of the maturity date of the WOF Loan from May 15, 2012 to December 20, 2012 in exchange for a fee. In addition, the Former Manager recommended that the Fund take on additional debt by way of a $4 million loan from Matrix, which, as mentioned earlier, is the parent corporation of the Former Manager (the "Matrix Loan"). The Matrix Loan is described further below. The extension of the WOF Loan and the Matrix Loan permitted the Fund to pay the amount due to Roseway on May 28, 2012, to make follow-on investments, and to pay some of the outstanding fees of the Former Manager. At about the same time, the Fund also retained an independent financial advisor, Triago Americas, Inc. ("Triago"), to solicit expressions of interest for a possible sale of a portion of the Fund's venture capital portfolio. This engagement resulted in the Newbury Transaction, which is also described below.

The Matrix Loan

[69] The Matrix Loan originally matured on July 31, 2014, bore interest at 18% per annum for the first year and 20% per annum thereafter and was secured by a charge over all of the Fund's assets. The Matrix Loan was funded by way of a $4 million loan extended by Growthpoint

Capital Corp. ("Growthpoint") to a subsidiary of Matrix (the "Growthpoint Loan") pursuant to a loan agreement dated May 18, 2012 (the "Growthpoint Loan Agreement") that was guaranteed by the Former Manager. The Matrix Loan utilized the financing facility that had been put in place for the Proposed Vengrowth Transaction. Levi says that the Matrix Loan was originally conceived of as bridge financing pending conclusion of a sale of assets that became the Newbury Transaction.

[70] The Matrix Loan and the Growthpoint Loan were back-to-back loans such that the terms of the Matrix Loan and the Growthpoint Loan with respect to interest, maturity and events of default were substantially the same. As a result, the occurrence of an event of default under the Growthpoint Loan would constitute an event of default under the Matrix Loan. A default under the Matrix Loan would, in turn, have triggered an event of default under the Roseway Documents and under the WOF Loan.

[71] The events of default under the Growthpoint Loan Agreement included the following: (i) a failure by the Fund or by the Comm Fund to pay when due any management fees owing to the Former Manager; (ii) a reduction of more than 30% of those management fees; and (iii) a breach of any of Matrix's covenants under the Growthpoint Loan Agreement. The effect of the default provisions of the Matrix Loan and the Growthpoint Loan was to put the Fund at risk of a liquidity crisis should it be unable to pay any management fees owing to the Former Manager or in the event that the Former Manager or certain of its affiliates failed to comply with the terms of the Growthpoint Loan Agreement. As a consequence of these provisions, a substantial portion of the proceeds from the Matrix Loan were used to pay management fees to the Former Manager that had been accrued.

Discussions with the OSC and the BCSC

[72] The announcement of the Matrix Loan by a press release of the Fund on May 23, 2012 prompted a letter to the Fund from the Ontario Securities Commission (the "OSC") raising certain questions relating to that transaction. The questions pertained to the purpose of the financing, the structure of the Matrix Loan, the role of Matrix in the financing arrangements as an affiliate of the Former Manager, the extent to which monies were being used to pay unpaid management fees of the Former Manager, the approval process of the Board in concluding that the Matrix Loan was in the best interests of the Fund including alternatives explored, and the basis for the determination of the IRC that the Loan was fair and reasonable for the Fund. By letter dated June 21, 2012, Ross, on behalf of the Fund, responded to each of these questions setting out the basis of the Fund's position that the Matrix Loan was in the best interests of the Fund.

[73] This was followed by a meeting between staff of the BCSC and representatives of the Fund, including Ross, and of the Former Manager, including Levi, which was held on July 11, 2012. Of note, according to the speaking notes prepared for the Fund's presentation to the BCSC at that meeting, Ross stated that "up until September 2011, the Board and the Manager believed that there was a reasonable basis for concluding that the Fund could remain on redemption through peak redemptions in February and March 2012 and beyond."

[74] After reviewing a binder of information provided by the Fund, the BCSC staff requested further information and disclosure respecting the venture capital portfolio of the Fund, the expenses of the Fund, the historical and projected cash flow of the Fund, and the Fund's plans if divestitures were insufficient to repay the WOF Loan in December 2012 or the Roseway Obligations in May 2013. With respect to the last matter, the Fund's response through its legal counsel was essentially that it was pursuing a secondary sale of assets. The Fund also indicated that, if divestitures did not generate sufficient cash flow, the options available to the Fund would include the negotiation of extensions to the applicable payment dates and further secondary sales.

The Newbury Transaction

[75] After conducting an extensive search, Triago was able to identify only one party who was interested in purchasing assets of the Fund, namely Newbury Equity Partners ("Newbury"). The Fund entered into a transaction with Newbury at the end of 2012 under which the Fund sold certain of its venture capital investments to Newbury for a purchase price of $19,159,824 (the "Newbury Transaction"). This sale occurred at a discount of 58% to the value ascribed to these investments on the books of the Fund. The proceeds of sale were applied, among other things, to repay the WOF Loan on or about December 31, 2012.

Events in 2013

[76] The SC, the IRC and the Board met on January 29 and January 30, 2013 to address various matters pertaining to the status of the Fund in light of its continuing liquidity problems at the time. The following decisions were taken at this time, among others.

[77] First, the Board approved an amendment to the Matrix Loan that deferred payment of $1 million due on January 31, 2013 to July 31, 2013 at the cost of a fee payable to Growthpoint of $160,000 plus applicable taxes.

[78] Second, at the instigation of Ross, the Board requested an independent review of the options available to the Fund given its current liquidity position. The Fund engaged The Commercial Capital Securities Inc., which operated as CCC Investment Banking ("CCC"), for this purpose by letter dated February 20, 2013.

The CCC Report

[79] CCC delivered its report in April 2013 (the "CCC Report"). The CCC Report proposed a multi-pronged approach. It concluded that, in the short-term, the Fund should continue its strategy of simultaneously seeking a restructuring of the Roseway Transaction and exploring replacement financing, although it also recommended preparation of a filing under the CCAA in case neither of the other initiatives succeeded. After addressing this short-term liquidity problem, CCC recommended, as longer-term options, consideration of a merger with another LSVCC, if feasible, and otherwise pursuing sales and exits of Fund venture capital investments on an orderly basis, a sale of the Fund's portfolio *en bloc* or in segments, or conversion to a modified closed-end fund.

The PWC Investigation

[80] Concurrently, Roseway retained PriceWaterhouseCoopers ("PWC") to examine transactions within the Defined Portfolio and Roseway's entitlement to the proceeds of sales of investments therein under the Participation Agreement. While the investigation uncovered a number of mistakes in the records maintained by the Former Manager, the only material issues pertained to the Fund's investment in Cytochroma Canada Inc. ("Cytochroma"). These issues are discussed below.

The Compliance Investigation of the BCSC

[81] On April 16, 2013, the BCSC sent GWC a letter describing the results of its compliance field examination of that corporation. The BCSC stated that it had significant concerns about the Former Manager's conduct as a portfolio manager and an investment manager. It identified nine deficiencies in the Former Manager's conduct as portfolio manager and investment fund manager of the Fund and WOF, of which two related specifically to the Fund. The BCSC also sent a further letter on April 30, 2013 regarding the delivery of records in the course of the compliance field examination. However, this letter is not material for present purposes. It should be noted that the BCSC letters represented the views of compliance staff.

[82] The BCSC required Levi and David Balsdon ("Balsdon"), the Former Manager's chief compliance officer at the time, to attend a meeting with the BCSC compliance staff in its offices around the time at which these letters were delivered to the Former Manager. The position of the BCSC compliance staff was read to Levi and Balsdon at that meeting at which time the BCSC speaking notes were apparently given to them.

[83] The Former Manager responded to these letters by letters dated May 15, 2013 and May 31, 2013, respectively, which set out the Former Manager's plans to address the matters raised by the BCSC.

The Position of the BCSC

[84] The BCSC compliance staff commented that the Fund had been in a distressed situation since 2010 and stated that, in their view, GWC had breached its statutory obligations under section 125 of the *Securities Act (British Columbia)*, R.S.B.C. 1996, c. 418 in its handling of the situation, as well as its duty of fair dealing.

[85] Section 125 reads as follows:

> Every investment fund manager must
>
> (a) exercise the powers and discharge the duties of its office honestly, in good faith and in the best interests of the investment fund, and
>
> (b) exercise the degree of care, diligence and skill that a reasonably prudent person would exercise in the circumstances.

Accordingly, the provisions of the Standard of Care and of section 125 are virtually identical.

[86] In respect of the Former Manager's fiduciary obligations and duty of care, the BCSC compliance staff considered that the Former Manager failed to consider all of the scenarios and actions dealing with the Fund's distressed situation and, in particular, in recommending that the Fund engage in the Roseway Transaction, the WOF Loan and the Matrix Loan. The BCSC staff considered that the Former Manager breached its statutory obligations in failing to assess, on an ongoing basis, the impact of winding down the Fund versus continuing to incur the costs of operations. In particular, the BCSC staff considered that the Former Manager breached its statutory obligations in failing to consider the impact of borrowing versus winding down the Fund on each occasion on which it recommended that the Fund enter into these loan transactions. The BCSC staff noted that there was no record of any wind-down analysis prior to October 2012 and that the report prepared at the time, when the BCSC raised the issue, was "overly simple." The BCSC staff stated that "[a] reasonably prudent person would have considered the possibility and impact of a wind down scenario on an ongoing basis after the [Fund] ran into liquidity issues and exit difficulties in 2010."

[87] In respect of the Former Manager's duty of fair dealing, the BCSC compliance staff stated that the Former Manager's actions in recommending that the Fund borrow money raised an issue of fair dealing with the Fund and its shareholders insofar as the continued operations had the effect of funding the payment of the Former Manager's fees. The BCSC staff noted in particular that the Matrix Loan of $4 million appeared to have funded payment of current and outstanding fees of the Former Manager totalling at least $2.65 million (the BCSC statement actually suggests $3.25 million although their reference totals the lesser amount). The BCSC staff stated that, not only did the high interest rates on the loans worsen the already distressed financial situation of the Fund and reduce the likelihood of redemptions but it also provided a payment priority to the Former Manager that it might not have had in a wind-down scenario.

The Position of the Former Manager

[88] The Former Manager expressed the view that many of the BCSC's statements represented "an attempt, with the benefit of hindsight, to substitute the Commission's business judgment for the business judgment of the Former Manager and the [Fund]." In addressing its handling of the Fund, the Former Manager made the following general comments, among others.

[89] First, it took it as a given that a "liquidation-style" wind-down of the Fund would have eliminated substantially all of the value potential in the Fund's venture capital portfolio and would have generated losses of at least 50% of the portfolio value. Second, it said that, referring to the CCC Report, an external advisor had confirmed that orderly sales of the Fund's portfolio was preferable to a "liquidation-style" wind-down. It considered that an orderly wind-down would have required several years. I note that the CCC says that the Former Manager has not accurately characterized the CCC Report in this regard. Third, the Former Manager was of the view that obtaining external financing for the Fund "on the basis that the value and the value potential preserved by the financing was expected to exceed the cost of the financing was and remains prudent and in the best interests of the [Fund]." Fourth, it said that a decision to pursue a wind-down was outside its mandate and authority and lay instead with the Board, which had approved all borrowing transactions of concern to the BCSC.

[90] The Former Manager expressed the view that, without the financing provided by the Roseway Transaction, which enabled the Fund to complete certain identified follow-on investments between May 2010 and March 2013, the Fund would have been exposed to up to $117.3 million in portfolio losses as a result of substantial or total dilution due to an inability to make the follow-on investments. It also referred to the discount in value of the assets sold pursuant to the Newbury Transaction to fund repayment of the WOF Loan in December 2012 as evidence of the discount in value likely in a "liquidation-style" wind-down.

[91] With respect to the BCSC's concerns regarding fair dealing, the Former Manager stated that the key factors in the decision to obtain external financing for the Fund included not only the ability to make follow-on investments but also the ability to continue honouring redemption requests for Class A Shares. It also referred again to the fact that the decisions were made by the Board not the Former Manager.

Resolution of the BCSC Investigation

[92] Ultimately, by letter dated August 21, 2013, the BCSC required, as a condition of the continued registration of GWC, that the Former Manager, Levi personally, and another LSVCC managed by the Former Manager, among others, provide certain undertakings to the BCSC. These undertakings included, among other things, that GWC (i) not recommend that any of the venture funds managed by it borrow money or engage in leveraging; and (ii) not recommend any transactions between the Fund and any other investment funds managed by it. These conditions did not, however, prevent the Former Manager from continuing to act as the manager of the Fund, subject to resolution of the regulatory capital deficiency described in the following section. The parties dispute the significance attached to the BCSC allegations and their ultimate resolution. This is addressed further below.

The Capital Deficiency of the Former Manager

[93] In addition, as a result of write-downs on the financial statements of GWC for the year ending December 31, 2012, GWC was in a regulatory capital deficit position. By letter dated May 9, 2013, after GWC brought this to the attention of the regulator, the BCSC formally advised GWC that a regulatory capital deficiency had existed since December 31, 2012. GWC responded by a letter dated May 13, 2013.

[94] The Former Manager was required by the terms of the Management Agreement to advise the Board of the capital deficiency. It did so on August 22, 2013 after GWC had agreed with the BCSC on August 21, 2013 to certain conditions to its registration, including giving the Fund notice of this development. Under these conditions, GWC was required, among other things, to cure the regulatory capital deficiency by October 1, 2013.

[95] To do so, among other actions, Matrix arranged to obtain a loan of $5 million from RC Morris & Company pursuant to a loan agreement dated July 31, 2013. The loan was advanced to the extent of $1 million in August 2013. The balance was advanced on October 1, 2013, after re-negotiation of the loan on September 30, 2013 required by the lender as a consequence of the Fund's termination of the Management Agreement on that day. The Former Lender says that this development resulted in more onerous terms under the loan agreement. In September 2013,

Matrix also closed the sale of its mutual funds business to a third party. The funds received from these transactions allowed Matrix to remedy the capital deficiency of GWC on October 1, 2013 as required by the BCSC.

Negotiations with Roseway

[96] During March 2013, the Former Manager conducted negotiations with Roseway with a view to restructuring the Roseway Transaction to avert a default on May 28, 2013, as the Fund did not anticipate being able to make the payments totaling $25.7 million due on that date. The Former Manager also conducted negotiations with another potential lender to refinance the Roseway Transaction, if necessary.

[97] Subsequently, CCC took over the role of negotiator on behalf of the Fund with Roseway. Over the summer of 2013, CCC negotiated a series of one-month extensions of the payment obligations under the Roseway Transaction. These were necessary as the Fund had breached certain covenants in the Roseway Documents creating an event of default thereunder. Ultimately, however, Roseway and the Fund were unable to agree on a restructuring of the Roseway Transaction.

Further Developments During the Summer of 2013

[98] By letter dated June 18, 2013, legal counsel for the Fund advised the Former Manager that the Fund was of the view that a number of expenses charged by the Former Manager to the Fund were the responsibility of the Former Manager pursuant to section 6.1 of the Management Agreement. The Former Manager responded by an email of July 5, 2013 to Ross. This was followed by a further letter dated September 19, 2013 of the Fund's legal counsel to the Former Manager addressing the Former Manager's email, reiterating the Fund's position that the expenses at issue were properly the responsibility of the Former Manager, and requesting a summary, with back-up, of all professional fees charged to the Fund during the preceding ten years. The outstanding issues between the parties pertaining to these expenses are addressed below.

[99] On July 19, 2013, the Fund repaid the Matrix Loan.

[100] In addition, the Special Committee commenced negotiations with Covington Capital Corporation ("Covington") for a possible acquisition of the Fund by one of the Covington funds. The transaction envisaged a transition period during which the Former Manager would be replaced by Covington as the manager of the Fund in order to negotiate arrangements with various parties, including Roseway and the Former Manager, which needed to be settled before a merger agreement could be agreed upon. The SC did not advise the Former Manager of this development.

Termination of the Management Agreement and Insolvency Proceedings of the Fund

[101] On September 30, 2013, the Fund terminated the Management Agreement by a letter of that date (the "Termination Letter"). The relevant provisions of the Termination Letter are set

out in Schedule B below. In asserting material breaches of the Management Agreement, the Fund relied heavily on the alleged findings of the BCSC as a result of its compliance investigation.

[102] On the same day, Covington delivered a formal but non-binding proposal to the Fund for a transition management arrangement with a view to negotiation of a merger agreement by which the Fund's assets would be acquired by a Covington fund.

[103] On October 1, 2013, the Fund obtained an initial order under the *Companies' Creditors Arrangement Act,* R.S.C. 1985, c. C-36 (the "CCAA"). FTI Consulting Canada Inc. (the "Monitor") was appointed the monitor in these proceedings. At that date, the NAV of the Fund was approximately $88 million. Subsequent to the filing, the Fund continued discussions with Covington regarding its replacement of the Former Manager as the manager of the Fund in contemplation of the proposed merger. However, after several weeks of negotiations between the parties, this proposal did not proceed further.

[104] As a result, the Fund obtained an order of Mesbur J. dated October 29, 2013 under the CCAA deeming the Former Manager to be a critical supplier in respect of certain services described in a critical transition services agreement dated October 15, 2013 (the "CTSA"). After that date, the Former Manager provided both the services described in the CTSA as well as certain other services. The claims of the Former Manager in respect of these additional services are addressed below.

Liquidity Management of the Fund

[105] A significant issue in this action is the strategic advice provided by the Former Manager to the Board regarding the actual and projected liquidity position of the Fund including the Former Manager's reporting to the Board. This issue was the subject of the expert evidence adduced by the parties, which is described below. The following section describes in some detail the documentary evidence in the record regarding the nature and extent of the Former Manager's reporting regarding the current and projected liquidity status of the Fund between 2005 and November 1, 2011, when the Fund ceased redemptions of Class A Shares. It is divided into four time periods reflecting, among other things, an increasing level of concern, and of correspondingly increasingly detailed reporting, regarding the liquidity position of, and prospects for, the Fund.

2005 to the Onset of the Economic Crisis in 2008

[106] As mentioned above, in August 31, 2005, the Fund had substantial cash and liquid assets. There is no evidence of any reporting to the Board in 2005 of the consequences for the Fund's liquidity of the CSTGF and CAVI transactions. Nor is there any evidence of financial projections in 2005 regarding the longer-term impact of the Government of Ontario's announcement of its intention to phase out the investment tax credit on LSVCC shares.

[107] In 2006, in connection with the FOF Transaction, the Former Manager advised the Board that it did not expect the Transaction to have a material impact on the Fund's liquidity position. This conclusion was supported by three statements: (1) that FOF's venture capital investment portfolio was predominantly at a later stage of development; (2) that one-third of FOF's net

assets of $36 million were in cash; and (3) that only $5.6 million of its capital constituted post-eight year or "hot money." In summary, the FOF Transaction was a relatively small transaction for the Fund.

[108] The materials for the Board meeting of April 5, 2007 contain a very simple cash flow forecast for the period ending March 1, 2008. The forecast contemplated surplus cash at that date of $35 million after deduction of all "hot money" shares and planned investments in 2007.

[109] At the Board meetings held on April 23 and June 18, 2008, the Former Manager reported to the Board that the Fund's liquidity position at December 31, 2007 was strong, being constituted by cash and liquid assets of $145 million, which represented a surplus of $80 million over the total amount of the "hot money" capital in the Fund of $65 million at that date. At the latter Board meeting, the Former Manager also projected a surplus of $80 million over "hot money" capital at December 31, 2008. This projection preceded the economic crisis that developed in the fall of 2008.

[110] The Former Manager also provided the Board and various committees with a number of reports during 2007 and 2008 regarding the impact of the ENSIS Transaction on the Fund's liquidity. In a report dated May 15, 2008, the Former Manager stated that "[w]hile the Merger will draw on [the Fund's] liquidity position, we believe the impact will be manageable." The post-merger liquidity projections provided in the same report contemplated a cash surplus in each of the calendar years between 2007 and 2012, after deduction of all "hot money" capital, although only a small surplus in the calendar year ending December 31, 2010. It is understood that this report was before the Board when it gave its final approval to the ENSIS Transaction at its meeting on June 18, 2008.

The Onset of the Economic Crisis to the Spring of 2010

[111] The economic crisis that commenced in the fall of 2008 profoundly affected financial markets, including the market for venture capital financing, the IPO and M&A markets for venture capital investments, and the market for LSVCC shares. From this point onward, the Fund experienced a deteriorating liquidity position for a number of reasons discussed below.

The Meetings in Late 2008

[112] The Former Manager did not, however, immediately signal any concern for the Fund's liquidity. At the Board meeting on November 18, 2008, the Former Manager stated that it was still projecting a surplus of $80 million after deduction of all "hot money" shares at December 31, 2008. At the IC meeting of December 3, 2008, the Former Manager advised that the Fund was "in a very good cash position."

[113] However, the Former Manager advised the IC at the meeting that it had started using a new reporting tool, being a liquidity analysis template that took into account projected subscriptions, redemptions, new investments, follow-on investments and divestitures/sales. Accordingly, commencing in 2009, the Former Manager's reporting on the Fund's liquidity position became somewhat more detailed although, as described further below, using only a single base-case. Further, in the spring of 2009, the Former Manager advised that, while previous

analyses were done on a calendar year basis, liquidity analyses going forward would be based on a March 31 year-end to incorporate the redemption experience during the RRSP season in January and February of each year.

Reporting Respecting the CMDF Transaction

[114] The Former Manager's analysis of the Fund's liquidity position in the fall of 2008 and the spring of 2009 is found in a number of reports that addressed the impact of the proposed CMDF Transaction. The focus of the reporting was on ensuring that CMDF's adverse liquidity position was not assumed by the Fund, which implicitly was regarded as having a very positive liquidity position. In order to limit any adverse impact, the merger documentation provided for a significant penalty in respect of redemptions of the Class A Shares to be issued to CMDF shareholders which occurred during the first three years after implementation of the CMDF Transaction.

[115] In these reports, the Former Manager was consistently of the opinion that, with this arrangement, the anticipated liquidity of the CMDF venture capital investment portfolio over the period to 2013 would more than offset the anticipated redemption of Class A Shares by former CMDF shareholders. In a memorandum to the IRC in October 2008, however, the Former Manager indicated that its preliminary analysis showed that there would be a net gain to the Fund's liquidity position through 2011, but a net erosion in the liquidity position by the 2012 year-end due to the expiration of the three-year period of the proposed redemption penalty.

[116] In a further memorandum to the IC for its meeting on March 19, 2009 pertaining to the proposed CMDF Transaction, the Former Manager set out the Fund's projected liquidity position both before and after the Transaction. In this context, the Former Manager stated in writing for the first time that the Fund's redemptions would reach their peak over the next few years requiring a "primary focus" on liquidity.

[117] In terms of the Fund's pre-CMDF Transaction position, the Former Manager stated that, at February 28, 2009, the Fund had $80.8 million in non-venture assets but, by the end of March 2009, was projected to encounter a liquidity deficit of approximately $84 million after deducting all of the "hot money" shares totalling $143 million. This is the first report to the Board that is in evidence that mentions the prospect of a liquidity deficit relative to the total of "hot money" shares, rather than an excess over the total of all "hot money" shares. The increase in shares eligible for redemption reflected the large sale of shares eight years earlier mentioned above. Further, the Former Manager stated that, after deducting all of the "hot money" shares in the Fund, the Fund was expected to remain in a deficit position for the foreseeable future, although the deficit was expected to diminish from 2011 onwards. The projections indicated that liquidity was expected to be about 41% of the total "hot money" shares at March 31, 2009 and 35% at March 31, 2010.

[118] In terms of the post-CMDF Transaction, the memorandum focused on the incremental impact of the CMDF Transaction on the Fund's liquidity position. The Former Manager indicated that, given the early redemption fees contemplated in respect of redemptions of the Class A Shares to be issued to the CMDF shareholders and what the Former Manager regarded as "reasonably conservative assumptions," the maturity of the CMDF venture capital investment

portfolio should result in net cash flows to the Fund that would exceed the redemption requirements in respect of such shares. This would improve the Fund's overall liquidity position for all future periods. The anticipated incremental improvement in the Fund's liquidity position from the CMDF Transaction was not, however, material as described below.

[119] The memorandum also provided some projections regarding the Fund's liquidity position assuming completion of the CMDF Transaction. The Former Manager contemplated that liquidity would be 41% of all "hot money" capital at March 31, 2009 and 45% at March 31, 2010 (compared to 41% and 35% respectively under the pre-CMDF Transaction scenario). It should be noted that the projections assumed the Fund's ability to raise significant amounts of new capital through the sale of Class A Shares during the 2010 and 2011 planning years and sizeable capital inflows from divestitures approximating $100 million per year for each of the 2010, 2011 and 2012 planning years (which is the 12-month period ending on March 31 in each of these years). The projections were therefore heavily dependent on a high level of divestiture proceeds and, to a lesser extent, on continuing sales of Class A shares.

[120] In summary, therefore, the projections essentially anticipated significantly reduced liquidity for 2009 and 2010 if the CMDF Transaction were not implemented and only a modest improvement in the projected liquidity position if the Transaction proceeded. Given this outlook, the Former Manager recommended a liquidity plan for 2009 to 2013 focused on the following: (1) generating divestitures; and (2) reducing the level of investment activity, largely by restricting investment activity to follow-on investments. In this regard, the Fund made its last new investment in April 2009.

Further Reporting During 2009

[121] The analysis in the memorandum to the IC meeting was also discussed at the Board meeting on April 23, 2009. The next meeting of the Board was held on June 16, 2009. There is no indication in the minutes of that meeting of any discussion of liquidity projections for the Fund, apart from a reference in Levi's report to the CMDF Transaction, which had closed in May, 2009, having provided the Fund with $18 million in liquidity.

[122] The Board met again on September 16, 2009. The only reference to liquidity in Levi's report to the Board at that time was that the Fund had achieved divestitures of $29.8 million in 2009 and expected to meet its liquidation (i.e. divestiture) targets for the year. However, a liquidity analysis prepared for the meeting indicated that the liquidity position of the Fund continued to be tight.

[123] The memorandum stated that the liquidity focus of the Fund had shifted from having excess liquidity as an acquisition currency for mergers to maintaining a requirement of 35% of "hot money" capital in liquid assets at all times. The memorandum noted that, at December 31, 2008, the liquidity was approximately 85% of "hot money" capital, that it had deteriorated to 40% at August 31, 2009, and that it was projected to be 52% by March 31, 2010. These projections are consistent with the projections in the memorandum to the IC for its meeting on March 19, 2009 described above although somewhat more optimistic for the liquidity position at March 31, 2010. The memorandum noted, however, that liquidity was projected to fall below 35% in February 2010 during RRSP season as a result of predicted redemptions. More

significantly, the memorandum set out four key assumptions upon which the projections were based. These included sales of $10 million and divestitures of $73 million, in each case for the rest of the period ending March 31, 2010. The memorandum noted in particular that "[v]enture exit activity is the key success factor to attaining the liquidity ratio of 52% by March 31, 2010."

[124] In response to the identified risk of a lack of liquidity during the 2010 redemption season, in the spring of 2009, the Former Manager began exploring the possibility of financing to bridge any liquidity shortfalls. At this time, bridge financing was apparently conceived of as short-term financing to bridge redemption requirements in January and February 2010 pending receipt of divestiture proceeds that were projected to restore the Fund's liquidity to approximately 52% of "hot money" capital by March 31, 2010. As discussed above, the Former Manager had discussions with traditional institutional lenders but was unsuccessful in identifying any interested parties. In the Board meetings on September 16, 2009, it reported that discussions with Comerica were not proceeding further. Ultimately, the search resulted in two offers from niche lenders to venture capital funds, including Roseway.

[125] After the September Board meeting, the Fund filed a preliminary prospectus with the provincial securities regulators in connection with its continuous offering of Class A Shares. In the course of its review, the OSC raised the issue of the level of "hot money" capital in the Fund and the level of reserves available to honour redemption requests.

[126] In a letter dated October 30, 2009 to the OSC, counsel for the Fund addressed this issue. Counsel advised the OSC that the Former Manager believed that the Fund had more than adequate liquidity to honour redemptions over the period to March 31, 2010. However, it is not possible to tie these calculations into comparable earlier projections in 2009 in evidence. More importantly, the Former Manager's response both assumed levels of divestitures and sales of Class A Shares that were significantly more than were achieved in the period to March 31, 2010 and did not address the Fund's liquidity relative to the total "hot money" capital at that date.

Reporting During the Spring of 2010

[127] There is little mention of liquidity in the Former Manager's reports to the Board at its meeting on November 17, 2009 as reflected in the minutes. The primary focus regarding liquidity at this time was a proposed amendment to the Fund's reserve policy. There is, however, a statement in a memorandum prepared for that meeting that, after testing various scenarios, "[i]n all tests, the Fund has Projected Reserves sufficient to meet Projected Cash Requirements through March 31, 2010."

[128] The perception of the liquidity position by both the Former Manager and the Fund changed rather markedly in early 2010. During this period, the IC met twice in advance of the Board meeting on April 27, 2010 to consider the deteriorating liquidity position of the Fund and the appropriate strategy going forward. In addition, the IRC met on February 24, 2010 to review the WOF Loan.

[129] The Former Manager provided projections for the Fund's liquidity position in a memorandum to the IRC for its February 24, 2010 meeting. In an appendix to that memorandum, the Former Manager projected a liquidity deficit of approximately $15 million at March 31, 2010

which would require a drawdown under the WOF credit facility of that amount. The appendix also contemplated a similar deficit at March 31, 2011, notwithstanding projected sales of Class A Shares totalling $15 million. As this projection assumed a drawdown and repayment of the WOF credit facility, the Former Manager's conclusion was that the Fund "requires an intermediate funding solution" after drawing down the WOF credit facility. Of particular note are the projections for divestitures for the 2011 planning period in this memorandum. The projected deficit of $15 million at March 31, 2011 assumed the inclusion of divestiture proceeds that were assessed as "probable", which totalled approximately $45 million (not including a $15 million transaction scheduled to close in April 2010). Accordingly, without receipt of divestiture proceeds assessed as "possible", which for the 2011 planning year totalled approximately $57 million, the Former Manager was effectively projecting a longer-term liquidity deficit for the Fund.

[130] According to the minutes, the Former Manager reported to the IC meeting on March 18, 2010 that liquidity stood at $16.9 million, $46.7 million less than had been forecast in 2009. The Former Manager stated that the most significant contributor to the negative variance was a $48.7 million shortfall in the projected divestitures. In the 2010 planning year (which would end on March 31, 2010), divestitures had been projected to be $98.1 million but were only going to be $49.4 million. For the 2011 planning year (which would end on March 31, 2012), the Former Manager indicated that, on a preliminary basis, it was targeting divestitures of $100 million "in order to maintain current liquidity levels." A consequence of the Fund's experience during the 2010 planning year was that it now depended almost entirely on divestiture proceeds to fund redemptions and follow-on investments, having depleted most of its non-venture capital assets.

[131] A memorandum dated April 7, 2010 to the IC for its meeting on April 15, 2010 indicated that the Former Manager had reviewed the venture capital portfolio of the Fund and concluded that the quality of the investments, including their stage of development and diversification, justified the Former Manager's confidence in the Fund's ability to meet its divestiture target for the 2011 planning year of $100 million. This amount must have included the divestiture proceeds characterized as only "possible" in the February memorandum to the IRC. It also noted, however, that the divestiture target had not been met in the 2010 planning year, principally due to lengthened time to achieve exits given the state of the markets and the Fund's inability to control other stakeholders in the investee companies who chose not to exit. Ultimately, as well, the memorandum also noted the need for a return to healthy and stable markets in order to meet its divestiture targets.

[132] In another memorandum prepared for the same IC meeting, the Former Manager addressed the liquidity status of the Fund. The memorandum indicated that the Fund incurred redemptions during the 12 months ending March 31, 2010 of $61.8 million, representing approximately 34% of "hot money" capital. The memorandum also set out the results of a model that projected the Fund's status starting from a cash position of $8.6 million, assuming sales of Class A Shares at $10 million per year, redemptions at 35% of "hot money" capital, and anticipated divestiture proceeds from the Fund's portfolio which, for the 2011 planning year was approximately $91 million. The model predicted a stable fund after eight years having a self-sustaining level of assets under management of approximately $98.5 million. On the basis of this model, the Former Manager concluded that the cash flow of the Fund would support

redemptions at the 35% rate without requiring drawdowns of the WOF Loan and that "the [Roseway] financing alternative is insurance for postponed venture exit activity."

The Board Consideration of the Strategic Options Available to the Fund in April 2010

[133] The Former Manager's recommendation that the Fund enter into the Roseway Transaction is central to this action. As mentioned, the Board took the decision to enter into this Transaction at its meeting on April 27, 2010. In connection with that meeting, the Former Manager prepared a number of memoranda in addition to those previously furnished to the IC, of which the following six are relevant for the issues in this action.

[134] First, at the request of the IC at its meeting on March 18, 2010, the Former Manager provided a memorandum assessing the strategic options available to the Fund. The memorandum expressed confidence in the "continuing prominence" of the Fund in the year ahead based on the following: (1) an assessment that the Fund's venture capital portfolio was in excellent shape; (2) redemption levels continuing at historic levels, being 35% of "hot money" capital; and (3) evidence of a positive change on the government relations side in Ontario. The memorandum addressed the following options: (1) ceasing redemption; and (2) a "secondary transaction" under which the Fund could divest a portion of its portfolio in return for a sufficiently large cash investment that would alleviate liquidity issues over the long-term.

[135] With respect to the option of ceasing redemptions, the memorandum stated as follows:

> Although a number of other retail venture funds in Ontario and Manitoba have chosen to cease redemptions in the past, none of those precedent decisions have proven to be beneficial to the funds' shareholders. The regulatory issues associated with the decision to cease redemptions are not trivial and, at best, give a fund a short period of time to resolve the situation. Given the illiquid nature of venture investments and the "cram-downs" investments are exposed to when follow-on investment capabilities are limited, the practical restrictions placed on a fund that ceases redemptions will almost invariably lead to major reductions in shareholder value.
>
> As a result, there are also litigation risks that must be considered. The regulatory and litigation issues are further discussed in [an attached memorandum regarding regulatory issues described below].

[136] With respect to secondary transactions, the memorandum stated that "[a]lthough the Fund's base-case liquidity analysis shows that such a secondary transaction is not necessary, such a transaction could provide vital insurance against any number of risks (for example, another capital market crisis or an unprecedented spike in redemptions)."

[137] Second, the Former Manager also prepared a short memorandum for the Board addressing "the regulatory process and some of the potential litigation risks for [an LSVCC] that

ceases redemption." Essentially, the memorandum concluded on the basis of the Former Manager's assessment of the experience of certain VenGrowth funds that there was no precedent for regulatory relief from the redemption obligations of the Fund beyond two years and that the Fund would likely have to make a fresh case on an annual basis. It also concluded that, depending upon whether a rumored class action against the VenGrowth funds was commenced and certified, if the Fund were to cease redemptions there was a risk of a similar class action lawsuit that would be expected to be "highly newsworthy" and "would likely have negative implications for the reputation of all concerned, including directors."

[138] In a third memorandum to the IC and the Board dated April 7, 2010, the Former Manager addressed the two secondary proposals to be considered by the Board. The memorandum states that "the [Fund] has a plan in place whereby net positive cash flows from the venture portfolio will be more than sufficient to meet the Fund's redemption obligations, allowing the Fund to sustain its critical mass over the long-run." The memorandum stated that, in the near term, the divestiture target of approximately $90 million for the 2011 planning year would result in net liquidity for the Fund of approximately $26 million by March 31, 2011.

[139] In this memorandum, the Former Manager set out the principal risks to realization of the Fund's cash flow plan as the following: (1) risks of delayed divestitures due to the health of the M&A markets; (2) follow-on investment requirements exceeding projections due to the state of the financing markets; and (3) redemptions exceeding expectations if there are "further material setbacks of a legislative or reputational nature" to LSVCC shares. The memorandum also concluded that the proposed Roseway Transaction would increase liquidity over the term of the Transaction until the year of repayment of principal. The Former Manager described the Roseway Transaction as an option that would provide "greater near-term liquidity to the Fund as a form of insurance against such risks".

[140] The Former Manager's view of the Roseway Transaction was summarized in the concluding paragraph of this memorandum as follows:

> Although the Fund has a considerable amount of mature venture assets to support future liquidity plans on a stand-alone basis, we believe that the [Roseway Transaction] – highlighted by the significant net positive cash flows provided to the Fund over the next 3 years – provides an important measure of insurance against the risks of liquidity that are outside the Fund's control...

[141] In a fourth memorandum, the Former Manager updated the liquidity status memorandum provided to the IC earlier in April 2010. The most significant change to the memorandum appears in the two versions of the model for the Fund which were attached as appendices to the memorandum. In these versions, the divestiture proceeds were assumed to be 75% and 50%, respectively of projected divestitures. Of note, at a level of 50% of projected divestitures, or a total of approximately $57 million (which itself appears high), the model predicted a liquidity deficit of approximately $6 million at March 31, 2011. Notwithstanding these revisions, the memorandum confirmed the conclusions expressed in the earlier liquidity status memorandum with the qualification "except where venture exits are at risk".

[142] Lastly, the Former Manager provided two memoranda regarding the proposed Roseway Transaction. In the first, which principally attached relevant documentation for Board review, the Roseway Transaction was described as "aimed at providing additional capital for follow-on financings in [the Fund's] venture portfolio". In the second memorandum, the Former Manager addressed the cost of capital under the Roseway Transaction and the long-term benefits of the Transaction.

[143] With respect to the former, the memorandum concludes that, "[b]ased on current estimates of exit timing and no changes in asset values in the Defined Portfolio, the cost of capital to [the Fund] would be $20 million paid over four years, equal to an internal rate of return (IRR) of Roseway of 31% ... which is comparable to target IRR's associated with private-company equity investments." The memorandum also indicated that an increase in the value of the Defined Portfolio from $100 million to $133 million would result in the Fund covering all the payments due under the Roseway Transaction. In this regard, the Former Manager's analysis of the value of the Defined Portfolio suggested a "conservative" increase of $47 million and a "more probable" increase of $100 million.

[144] With respect to the long-term benefit of the Transaction, the Former Manager also stated that it believed "that the Roseway transaction serves as valuable insurance, providing [the Fund] with the ability to realize on the full value of its portfolio via orderly and value-optimized exits." Using what the Former Manager described as "base case assumptions," the Former Manager estimated $74.3 million of net gains over time from the Fund's venture capital portfolio of which the Fund would retain $47.6 million, the balance being payable to Roseway pursuant to the Participation Agreement.

[145] The minutes of the Board meeting of April 27, 2010 indicate that the IC had met on April 15, 2010 and considered four strategic options for the Fund. The IC rejected option (1) - accepting the present liquidity risk in the hope that future divestment opportunities would satisfy any liquidity concerns - in favour of action to reduce the liquidity risks of the Fund in case the Fund's projections proved to be materially incorrect. The IC considered option (2) - seeking regulatory approval to ceasing redemptions - to be too uncertain for the following reasons:

> With respect to seeking to cease redemptions of GW Cdn shares, many issues would arise that make that possibility uncertain, including (i) potential class action lawsuits against [the Fund] by shareholders who seek damages for the change in redemption rights, (ii) missing out on future marketing benefits in Ontario once the liquidity issue is addressed, (iii) the conditions securities regulators would place on any request for redemptions, and (iv) the experience of other venture capital funds where redemption suspensions have resulted in lower NAVs and no benefit to shareholders...

The Minutes also reflect that the IC noted that traditional sources of debt financing were unavailable so option (3) was not feasible. As a consequence, the IC had focused on option (4), which involved obtaining external funding from non-traditional sources, and had resolved that

the Roseway Transaction was preferable to the alternative financing proposal and should be presented to the Board in greater detail.

[146] As mentioned above, the Board approved the Roseway Transaction at the meeting. The minutes of the Board meeting further reflect the fact that the Former Manager and the Board considered the Roseway Transaction to be "a form of insurance against risks related to material changes in fundraising, divestments and redemptions" and that the Former Manager recommended the Transaction to the Board. The Former Manager also stated that it considered that a principal reason for acceptance of the Roseway Transaction was that "the Fund could commit to greater amounts of follow-on financing for its entire [venture capital] portfolio, that would in turn increase the realized value of the overall portfolio". In this regard, the Former Manager restated at the Board meeting its assessment of the conservative and probable increases in value of the Fund's venture capital portfolio described above that it anticipated from further follow-on financings.

May 2010 to the Suspension of Redemptions in November 2011

[147] The Board was presented with a liquidity status model at the Board meeting held on September 30, 2010. The model indicated that the Fund's liquidity, after inclusion of the proceeds of the loan in the Roseway Transaction and projected redemptions calculated on the basis of 35% of "hot money" capital, totalled $17 million at August 31, 2010 and was projected to amount to $38 million at March 31, 2011. This represented only 13% and 35%, respectively, of "hot money" shares at these dates. These projections included projected divestiture proceeds of $73.2 million and sales of $14.9 million during the period from August 31, 2010 to March 31, 2011. Of note, the amount of liquidity at August 31, 2010 was less than the amount of the loan advanced in the Roseway Transaction. The minutes also indicate that the Chief Financial Officer reported orally to the Board on the projected results under the alternative scenarios of redemption rates of 35% and 44% of "hot money" capital and divestitures at 100% and 60% of projected divestitures. Under the most conservative of these scenarios, the Fund would experience an absolute shortfall of $2.5 million at March 31, 2011.

Projections to the End of the 2011 RRSP Season

[148] This liquidity status model was updated for the Board meeting of November 17, 2010. At this date, the Former Manager projected Fund liquidity of $15 million at March 31, 2011 after projected redemptions that were more conservatively calculated on the basis of 40% of "hot money" capital. The reduction from $38 million also reflected a reduction in projected divestiture proceeds of $8.5 million and the removal of any projected sales. For apparently the first time, the Former Manager provided alternative scenarios in its written report using 100% and 80% of projected divestiture proceeds and 40% and 44% of "hot money" share redemptions.

[149] In a memorandum to the Board for the same meeting, the Former Manager stated that it was proposing to provide biweekly reports by way of a liquidity dashboard until March 31, 2011 in view of the significance of redemption and divestiture activity for the Fund's liquidity during that period. Reflecting a growing concern, the memorandum also noted that the original projection for the planning period to March 31, 2011 contemplated divestiture proceeds of $98 million, that the projection now contemplated $90 million, and that only $24.8 million of

divestiture proceeds had been received in the seven months ending October 31, 2010. The Former Manager was now projecting divestiture proceeds of $64.2 million for the five months ending March 31, 2011.

[150] Commencing in late 2010, the SC reviewed the Former Manager's efforts to pursue the Proposed VenGrowth Transaction. In a report to the SC dated December 6, 2010, the Former Manager stated its view that the proposed transaction would strengthen the liquidity position of the Fund. It stated further that it believed that the combination of a lack of available venture capital financing and improving M&A markets for divestitures provided "an attractive opportunity to acquire mature venture holdings." In short, the Former Manager's focus on liquidity involved implementing the Proposed VenGrowth Transaction and using the improved liquidity to acquire mature venture capital assets at lowered valuations.

[151] During February 2011, the Former Manager provided a number of memoranda for various Board and committee meetings. At that time, the Board was focused principally on the level of redemptions occurring during the 2011 RRSP season. For planning purposes, the Former Manager was now conservatively projecting redemptions equal to 44% of "hot money" shares. It noted in a memorandum prepared for a Board meeting on February 17, 2011 that, if it continued, this redemption level would require substantial external financing "to supplement liquidity from near-term venture exits." The memorandum also stated that the Former Manager continued to predict a liquidity shortfall as of March 31, 2011 that had been originally projected in a previous report as of January 1, 2011, which is not in evidence. The memorandum also noted that divestitures continued to fall below projected levels. More significantly, it also noted that projected divestiture proceeds for the remaining period to March 31, 2011 were also scaled back.

[152] In a second memorandum reporting on the Fund's status as of February 18, 2011, the Former Manager reported that, at a redemption rate of 44% of "hot money" shares, its projections demonstrated that the Fund would require both the WOF Loan and a loan from Matrix in the amount of $5 million to meet the Fund's cash requirements and the covenant requirements in the Roseway Transaction, with the timing of such need depending upon the redemption experience in February.

The Position Following the End of the 2011 RRSP Season

[153] The next report of the Former Manager in evidence respecting liquidity is contained in a memorandum to the Board for its meeting of April 27, 2011. The memorandum addresses the liquidity position of the Fund as of April 15, 2011, after the end of the 2011 RRSP season. By this time, the Fund's liquidity had improved in the short-term due to two factors: (1) the annual level of redemptions for the period ending March 31, 2011, which ended up being only 24% of "hot money" capital; and (2) the closing of a large divestiture transaction after March 31, 2011, which yielded proceeds of $12 million.

[154] As a result of these factors, the Former Manager projected that "if exits and redemptions continue as expected until August 31st, then no injections from WOF or Matrix will be required." The Former Manager noted, however, that the Fund's ratio of "hot money" capital to NAV continued to rise due to lower redemptions. It also commented that the timing of divestitures

was the Fund's greatest challenge and that the exits totalling $16.9 million projected to August 31, 2011 were critical to maintaining sufficient liquidity. It further suggested that "[e]xternal financing [from the WOF Loan and the Matrix Loan] may be required to supplement liquidity from near term venture exits."

[155] The minutes of the Board meeting of April 27, 2011 reflect a report from the Former Manager that total sales of Class A Shares for the preceding 12 months totalled only $1.4 million. The minutes also state that, for the year ending March 31, 2011, divestiture proceeds totalled $50.7 million, well short of the budgeted $90 million, which was in fact initially budgeted at $98 million. The Chief Financial Officer also commented that "[t]he timing of divestments was generally lower than anticipated, mostly due to market conditions."

[156] In a subsequent memorandum for the June 8, 2011 Board meeting, the Former Manager stated that the projections as of May 27, 2011 suggested "that the Fund may continue to be self-sufficient through the end of the current and subsequent RRSP seasons." However, at a more granular level, the weekly projections that the Former Manager had been creating since the beginning of the year identified certain weekly liquidity deficits in the period to October 31, 2011 that would require short-term draws under the WOF Loan and a deferral of payment of the management fees due to the Former Manager. In the liquidity analysis attached as an exhibit to this memorandum, divestiture proceeds for the remainder of the period to March 31, 2012 were projected to be only $60.9 million.

The Reporting for the Board Meeting of September 30, 2011

[157] The next memorandum of the Former Manager was prepared for the Board meeting on September 27, 2011, at which meeting the Board resolved to cease the sale of Class A Shares. The memorandum states that, while redemptions had been tracking reasonably close to expectations, divestitures for the current planning period had declined by approximately $18 million and investment activity had increased resulting in a combined reduction in projected liquidity of $22.9 million. Total divestiture proceeds for the five months ending August 31, 2012 were $25.2 million. The Former Manager had also reduced its projections for divestitures for the remainder of the period to March 31, 2012 from $41 million to $25 million. As Levi noted, without the WOF Loan, the Fund would have been in a deficit position of approximately $7 million at August 31, 2011.

[158] The memorandum attributed the decreased rate and delayed timing of divestitures to three factors: (1) global economic uncertainty since the early summer; (2) delays in attaining clinical trial data in the case of certain life sciences investments; and (3) shortfalls in the financial performance of a few investments. The memorandum concluded that, of these factors, "the impact of the economic uncertainty seems to be playing the largest role and had been seen in the 2008-2010 timeframe."

[159] The Former Manager also provided a preliminary liquidity analysis and projection of the Fund's liquidity status at December 31, 2011 and at March 31, 2012 under four scenarios, using divestitures of $51 million and $28.7 million and redemptions at the rates of 25% and 35% of "hot money" capital. Combined with five possible redemption options, this analysis set out 20 scenarios for consideration. Under the most positive scenario of $51 million of divestitures and

unrestricted redemptions at a 25% rate of "hot money" capital, however, the projections contemplated excess liquidity of $0.7 million at March 31, 2012 after drawing down fully both the WOF Loan and a $5 million loan from Matrix under discussion. On the basis of this analysis, the Former Manager recommended that the Board convene a special meeting at the end of October, reflecting the urgency of the situation, to address "various redemption modification scenarios to address cash flow concerns…when more accurate divestment and redemption information will be available."

The Reporting for the Special Board Meeting of October 27, 2011

[160] As mentioned above, at a special meeting on October 27, 2011, the Board accepted the Former Manager's recommendation that the Fund adopt the RMP. For the purposes of this meeting, the Former Manager also prepared a lengthy memorandum.

[161] Among other things, the memorandum contained a detailed financial analysis regarding the Fund's current and projected cash position. Most significantly, the memorandum concluded that "[b]ased on the revised projections, going forward from November 1, 2011 the Fund will not have sufficient funds on hand to honour anticipated Class A Share redemption requests while continuing to participate in value-preserving follow-on investments and pay its operating expenses."

[162] The Former Manager opined that divestitures were lower than projected as a result of a heightened level of uncertainty, fears of a new recession, and resulting high levels of market volatility. The memorandum also included an extensive analysis of the 62 venture capital investments in the Fund's portfolio. Among other conclusions, the Former Manager stated its belief that "[the Fund] should be able to maintain its historic rate of $50 million a year in exits even if some targeted exits are delayed and/or exit values are adjusted downwards." Among other things, this statement reflects a downwards revision in the projections for divestitures until 2013 to the level of $50 million annually.

[163] For the first time, the Former Manager acknowledged that the Fund "had closed sales of its Class A Shares and effectively entered a wind-down phase." The memorandum also canvassed in some detail the feasibility of a number of options for managing liquidity based on the activities of the Former Manager in pursuing such options since 2010. The Former Manager recommended adoption of the RMP. It stated that its objective was "to see [the Fund] return to weekly, unrestricted redemptions within 24 to 36 months." In this regard, the memorandum stated that past orders of the securities regulatory authorities issued to other LSVCCs had generally been limited to 24 months but the Fund's application submitted by the Former Manager in respect of the RMP sought a 36-month order as the Former Manager expected that the Fund would be able to divest more than 60% by value of the Fund's venture capital investments over that period.

<u>The Expert Evidence</u>

[164] In this case, the evidence of the expert witnesses is important in establishing the standard of care required of the plaintiff for the purposes of section 3.5 of the Management Agreement. The following summarizes the evidence of the experts. I have then set out certain observations

of the Court regarding these opinions that identify certain of the issues addressed in these Reasons.

Gekiere

[165] The defendants produced as an expert Barry Gekiere ("Gekiere"), whose evidence was contained in an affidavit sworn August 5, 2016 (the "First Gekiere Affidavit"), a further affidavit sworn November 16, 2016 (the "Second Gekiere Affidavit") and a third affidavit sworn June 5, 2017 containing answers to written interrogatories (the "Third Gekiere Affidavit"). Gekiere provided a written opinion (the "Gekiere Opinion"), which was attached to the First Gekiere Affidavit, and a written response to the Varghese Opinion (described below), which was attached to the Second Gekiere Affidavit (the "Gekiere Response").

The Gekiere Opinion

[166] Gekiere was asked by the Fund to provide an expert opinion as to whether the Former Manager met the standard of care required by section 3.5 of the Management Agreement in recommending and implementing the Roseway Transaction, the WOF Loan, the Matrix Loan and the Newbury Transaction. It is his opinion that it did not.

[167] In the First Gekiere Affidavit, Gekiere summarized the basis of his opinion as follows:

> A prudent manager would have better anticipated the liquidity issues that the Fund faced in FY2009 [being the fiscal period ending August 31, 2009] and FY2010 [being the fiscal period ending August 31, 2010]. In the face of these liquidity issues in FY2009 and FY2010, the Former Manager did not take appropriate action (i.e. recommend that the Fund seek regulatory approval to cease redemptions). This caused the reserve for follow-on investments to be insufficient to make needed follow-on investments in FY2010. Accordingly, the Fund was required to take on debt, which is inappropriate for investment funds for reasons outlined [in the Gekiere Opinion]. In addition, the terms of the debt taken on by the Fund were inappropriate.

[168] Gekiere expanded upon the basis for this conclusion in the Gekiere Opinion. In Gekiere's opinion, the announcement of the Government of Ontario significantly changed the economics of the LSVCC business model such that the Former Manager should have planned for significant reductions in cash inflows from the sale of Class A Shares starting in fiscal 2009. The announced withdrawal of the investment tax credit on the sale of Class A Shares implied that, thereafter, the only major source of capital inflows for the Fund would be divestitures of the Fund's venture capital investments. Further, the Former Manager had eight years' notice that redemption levels were likely to be high in fiscal 2009 and thereafter, given the peak sales of Class A Shares in earlier years. In Gekiere's opinion, from as early as the fall of 2005, the Former Manager should therefore have been alerted to the possibility of liquidity problems starting in fiscal 2009 based on the combined impact of these two factors. Further, the Former

Manager would have realized that the Fund would be entirely dependent on divestitures to the extent that sales of Class A Shares declined commencing in or before fiscal 2009.

[169] Accordingly, the Former Manager should have recognized the need to maintain adequate reserves for follow-on investments much earlier than the fall of 2009 (during fiscal 2010), and should have considered various options to ensure such reserves much earlier than fiscal 2010. These options included scaling back or ceasing new investments much earlier than April 2009, reducing marketing and sales expenses given the likely reduction in sales of Class A Shares, analyzing more closely the potential returns on follow-on investments and rationing reserves more strictly according to such analyses, and, if necessary, halting redemptions.

[170] Instead, in Gekiere's opinion, the Former Manager focused on an acquisition strategy and "basically allowed redemptions to deplete the capital that should have remained available for follow-on investments." As a result, the Fund was unable to fund follow-on financings at the commencement of fiscal 2010 as redemptions continued to exceed cash inflows from sales of Class A Shares and divestitures.

[171] In Gekiere's opinion, given the high uncertainty in fiscal 2010 regarding the timing and amount of exits in view of the economic conditions at the time, the Former Manager compounded the situation by recommending that the Fund obtain outside capital from Roseway having fixed repayment terms rather than a true participation arrangement, or "patient capital," under which repayment would be made out of divestiture proceeds as exits occurred. In short, in his opinion, the Former Manager did not act prudently in recommending that the Fund borrow to fund follow-on investments and it was particularly imprudent to borrow on the terms of the Roseway Transaction.

[172] As a related matter, Gekiere also believes that the Former Manager's actions resulted in an unfairness to the Fund shareholders who remained after fiscal 2009 in two respects. By allowing redemptions during fiscal 2009 at the NAV per share at the time, the Former Manager was effectively reducing the NAV per share of the remaining Class A Shares. Further, by allowing redemptions during fiscal 2010 at a NAV per share that did not reflect the $17.1 million interest costs over three years under the Roseway Transaction, the remaining shareholders were bearing such costs by way of a reduction in the NAV per share of their Class A Shares.

[173] More generally, in Gekiere's opinion, the Former Manager's actions created significant and unnecessary expenses for the Fund by way of the costs of the Roseway Transaction, as well as the interest costs of the subsequent WOF Loan and Matrix Loan and the discount on the sale of assets pursuant to the Newbury Transaction. In particular, the Former Manager did not recommend suspension of redemptions of Class A Shares until November 2011, by which time, in Gekiere's opinion, the damage to the Fund's liquidity position had been done and the Fund was in a critical working capital position. This required the Fund to enter into the WOF Loan and the Matrix Loan and to sell assets at a substantial discount pursuant to the Newbury Transaction.

The Gekiere Response

[174] In the Response, Gekiere stated that it remained his opinion after reviewing documentation not previously provided to him that, with respect to the Roseway Transaction, the Former Manager did not discharge its duties in the best interests of the Fund, exercising the degree of care, diligence and skill that a reasonably prudent person would exercise in the circumstances.

[175] Gekiere summarized what he characterized as the four key points of the Gekiere Opinion as follows:

1. Future potential liquidity problems in the Fund should have been apparent to the Former Manager as early as 2005, when the Province of Ontario announced the phase out of its 15% tax credit starting in 2009. A prudent manager would have acted accordingly to ensure that adequate follow-on reserves would be available, whereas the Fund did not have adequate follow-on reserves in fiscal 2010.

2. The use of debt is inappropriate in a venture fund and the Roseway Transaction was particularly inappropriate as it was fundamentally used to fund redemptions.

3. The appropriate course of action on the part of the Former Manager should have been to recommend to the Board that the Fund seek regulatory approval to cease redemptions as early as fiscal 2009.

4. The possible rationale for the Former Manager's reluctance to seek regulatory approval to cease redemptions as early as fiscal 2009 was that it would jeopardize the Former Manager's ability to merge with other funds in order to increase assets under management and generate more fees for the Former Manager.

[176] In the Response, Gekiere reviewed in greater detail the reasons why he believed these points remained valid notwithstanding the Varghese Opinion. In particular, Gekiere made the following relevant points for present purposes.

[177] First, as discussed below, Varghese stated in the Varghese Opinion that, after the Fund had disappointing sales in the first quarter of 2006, a prudent board of directors should have taken preventative measures. Gekiere agrees with the assessment, but considers the responsibility for recommending such measures to have rested with the Former Manager.

[178] Second, Gekiere notes that Varghese's position is that the sole, or at least the predominant, reason for the liquidity problems of the Fund was the financial crisis of 2008, which had an adverse impact on the divestitures projected by the Former Manager. Gekiere's view is that the Former Manager was overly optimistic in its projections of divestitures to the point of failing to meet the required standard of care:

> The Former Manager provided the Board with overly optimistic exit projections giving the Board a false sense of comfort that exits would be sufficient for follow-on requirements and redemptions to be met. A prudent manager, especially in light of the 2008 financial crisis, would not have relied heavily on exits. Even in normal economic times it would not be prudent to rely heavily on projected exits as they are difficult to accurately predict. Given the state of the economy at that time a prudent manager would have at least erred on more conservative forecasts making the Board explicitly aware of the potential risk of not receiving sufficient capital inflows to cover follow-on investments and redemptions.

[179] Third, Gekiere is of the view that the Former Manager did not meet the required standard of care by merely providing the information described above – that is, that such actions cannot be properly characterized as "pro-active" as Varghese suggests:

> Given that the Fund could no longer rely on new sales to be a buffer for follow-on investments the only meaningful capital inflows would have to come from exits/ divestitures. If exits were to prove to be insufficient to fund both follow-on investments and redemptions, then the only logical decision for a prudent fund manager would be to seek regulatory approval to cease redemptions in order to make the follow-on investments.
>
> Given that exits were unpredictable, especially during the aftermath of the 2008 financial crisis and follow-on investments were mostly predictable and necessary to maintain, then a prudent manager would have set trigger points as to when it would be necessary to approach regulatory authorities to cease redemptions, in order to continue to fund follow-on investments. Thus, when exits started to fall below projections, the implications would have been clear to the Board and action to cease redemptions would have been taken.

The Third Gekiere Affidavit

[180] In his answers to interrogatories set out in the Third Gekiere Affidavit, Gekiere further clarified his opinion in the following respects.

[181] First, Gekiere is of the opinion that the Former Manager should have established a liquidity forecasting model by at least April 23, 2008 and should have alerted the Board at the meeting held on that date of the significant reduction in liquidity that would occur in the 2009 RRSP season (January and February 2009) should projected exits not occur. Gekiere believes that not only did this not occur but the Former Manager also provided an overly-optimistic view of the liquidity position of the Fund and its prospects in the spring of 2008 by, among other things, referring to the liquidity position of the Fund as at December 31, 2007 rather than March 31, 2008, which he estimates was $50 million lower.

[182] Gekiere's opinion regarding the course of action that the Former Manager should have taken in the spring of 2008 is expressed as follows:

> Based on all the information that would be available to the Former Manager at April 23, 2008, the Former Manager should have been informing the Board that liquidity at December 31, 2007 was at a seasonal peak and the Fund's liquidity had dropped after the 2008 RRSP season. The Former Manager should have presented the actual liquidity position at March 31, 2008. Then, the Former Manager should have presented the Board with a liquidity forecast showing that a further deterioration in Liquid Assets in the range of $70 million could be expected by March 31, 2009 before exits, with a high level of predictability.
>
> At this time, the Former Manager should have been advising the Board that the Fund would be extremely dependent on future exits, which are difficult to accurately predict. At this point a prudent fund manager would have been recommending to the Board that the level of projected exits must be scrutinized closely and if at any time the amount of Liquid Assets fell below the total projected amount of investments and redemptions, without the benefit of future exits, then ceasing redemptions would have to be considered in order to maintain reserves for follow-on investment.

[183] Second, Gekiere is of the opinion that, during fiscal 2009, the Former Manager should have advised the Board that exits may not hit the level previously projected and should have described the impact of such results on the Fund's liquidity, particularly in view of the upcoming redemptions in the 2009 RRSP season (January and February 2009).

[184] Third, Gekiere is of the opinion that, in the spring of 2009, the Former Manager should have alerted the Board to the need to approach regulatory authorities with a view to ceasing redemptions of Class A Shares prior to the 2010 RRSP season (January and February 2010). He believes that, instead, the Former Manager masked the seriousness of the Fund's liquidity position by moving to reporting of the Fund's liquidity coverage ratio based on coverage of anticipated redemptions (using the historical average of 35% of hot money) rather than on coverage of all "hot money" shares as it had done previously. If the former manner of calculating the liquidity coverage ratio had been maintained, it would have been clear that liquid assets at March 2009 were not materially more than expected redemptions during fiscal 2009. This made the Fund's liquidity very sensitive to the level of redemptions in fiscal 2009 and to the projected level of divestitures, which was in excess of $70 million over the period September 2009 to March 2010. Gekiere regards this projected level of divestitures as unrealistic at the time given the Fund's current and historical experience as well as the state of the economy in the spring of 2009.

[185] Gekiere summarizes his opinion regarding the course of action that the Former Manager should have followed in the spring of 2009 as follows:

> The Former Manager knew the Fund was now in the position that liquid assets were less than the total amount of capital needed for projected follow-on investments and redemptions, without the benefit of future exits. Since exits were not predictable and should not be relied on, a prudent manager should have been recommending to the board the need to cease redemptions.

[186] Gekiere is further of the opinion that, by not having approached the regulatory authorities in advance of the 2010 RRSP season, the Former Manager put the Fund in a position whereby redemptions could not be terminated and the Board had no choice but to approve the Roseway Transaction in April 2010 in order to be in a position to make follow-on investments. He regards the Roseway Transaction as therefore directed, in substance, toward providing financing to fund the Class A Share redemptions that had occurred earlier during the 2010 RRSP season (January and February 2010).

Varghese

[187] The plaintiff presented a report of John Varghese ("Varghese") that was appended to an affidavit sworn November 11, 2016 (the "Varghese Affidavit"). From 2005 to 2011, Varghese was, among other things, a co-owner and the chief executive officer of the VentureLink Group of Funds, which also managed an LSVCC. In addition, as the chairman of the Retail Venture Capital Association of Canada for two years and otherwise, Varghese was, by his own admission, one of the lead lobbyists between 2005 and 2010, together with Levi, for the LSVCC industry seeking to re-establish the viability of the LSVCC industry by reversing the decision of the Government of Ontario or obtaining its acceptance of a replacement programme to encourage investment in LSVCCs.

The Varghese Opinion

[188] Varghese was asked by the plaintiff to provide an opinion with respect to the standard of care of the Former Manager, as set out in the Management Agreement, and whether the Former Manager breached this standard of care and the Former Manager's fiduciary duty to the Fund as a result of the matters alleged in the pleadings in this action, the Termination Letter and the affidavit of Ross sworn August 5, 2016 in this action. It is Varghese's opinion that the Former Manager did not fail to discharge its duties in the best interests of the Fund. His opinion is based on, or relies on, the following principal conclusions.

[189] First, Varghese acknowledges that "the forecasting capabilities of the Former Manager may be questioned using hindsight." However, he is of the view that "the unforeseeable impact of the financial crisis of 2008 and 2011 would also have adversely affected forecasts and projections without it being the responsibility of the Former Manager." In short, he says that it is only with the benefit of hindsight that it is reasonable to expect that actual results could have been negatively affected by these events.

[190] Second, Varghese considered that the Board had the responsibility of establishing the Fund's strategic objectives and monitoring the Former Manager's implementation of these objectives. While he does not expressly state his view of the Former Manager's responsibilities,

it is implied from his approach that they were limited to planning and reporting on investments, redemptions, sales and the liquidity position of the Fund. In Varghese's mind, the Board had sole responsibility for identifying and planning for the Fund's liquidity risks. Accordingly, based on this division of responsibilities as well as the language of the charters of the Board committees, he considers that the Board was solely responsible for ensuring the management of redemptions of Class A Shares and, therefore, "it is not appropriate to blame the Former Manager for its failure in this regard."

[191] Similarly, he acknowledges that the dramatic decline in sales that followed the announcement of the Government of Ontario should have been known and anticipated from 2005 onward. However, Varghese attributes the responsibility for risk assessment and risk management pertaining to this development to the Board rather than the Former Manager.

[192] Further, in his summary, Varghese is clear that, in his opinion, the Board had an obligation immediately after the financial crisis of 2008 to "re-assess its risk and its strategy in the aftermath of the crisis." Varghese says there is no evidence that the Board did so but rather evidence that it continued on a "business as usual" basis. He concludes that "this demonstrates a failure by the Board to fulfill its fiduciary duties."

[193] Varghese does not, however, suggest that the Board disregarded any advice or presentation from the Former Manager proposing, advising or recommending any other course of action. Nor is there any suggestion of any such action in the evidence before the Court.

[194] Third, Varghese considered that, throughout the period following the execution of the Management Agreement in 2006, the Board mandated the Former Manager to make the Fund the largest LSVCC in Canada. He proceeded on the basis that the Board supported this strategy up to and including the Proposed Vengrowth Transaction. In this regard, he states that, in his opinion, ceasing redemptions would have had the immediate and permanent impact of derailing this mandate. Accordingly, Varghese was of the opinion that "[i]t is inappropriate [to] throw the blame upon Former Manager in hindsight for its purported apparent failure to plan for liquidity needs of the Fund in the face of the [m]andate."

[195] Varghese's opinion in this regard is neatly summarized in paragraph 14 of his opinion, which reads as follows:

> In my opinion, the Board of the Fund is not taking responsibility for its shortcomings as it attempts to blame the Former Manager for not providing liquidity planning when such an inherent conflict existed between the Board mandated growth plan and liquidity management. This is especially true given that the responsibility of the Board increased when the business environment of the Fund changed as dramatically as it did in the [LSVCC] industry.

[196] Fourth, in response to the Gekiere Opinion, Varghese noted that Gekiere had not been given access to all of the documentation to which Varghese had been given access. He considered that Gekiere would have reached a different conclusion in the Gekiere Opinion if he had been able to review such materials.

[197] In this regard, Varghese refers to the various documents described above in which the Former Manager either commented upon the likely impact of proposed mergers on the liquidity of the Fund or forecast the liquidity position of the Fund in the future. It is his view that these documents demonstrate that the Former Manager was aware of the importance of liquidity, including the need to provide for follow-on investing, and brought this to the attention of the Board. In particular, Varghese was of the view that Gekiere would not have reached the same conclusions if he had reviewed the documentation provided to the Board and the Board committees in March and April 2010 described above. I note, however, that, as discussed above, Gekiere confirmed his opinion after reviewing such documentation to the extent that he had not already done so.

[198] Fifth, Varghese is of the view that, given the Fund's liquidity position in April 2010, it is unlikely that the Fund would have received regulatory permission to halt redemptions at that time. In this regard, Varghese took a more extreme position than the Fund, which submitted only that it could not have obtained redemption suspension relief for a sufficiently long period of time to avoid a "fire sale" of its assets.

[199] Sixth, Varghese justifies the terms of the Roseway Transaction on two grounds. First, he says that they were the best terms available to the Fund. Second, he says that, had the Defined Portfolio increased in value in the order of magnitude presented to the Board by the Former Manager, Roseway's return would have reflected a true participating interest. He says the timing of the divestiture of the investments in the Defined Portfolio frustrated this increase in value. He considers, however, that the Former Manager gave the Board the necessary analysis to permit it to make an informed decision.

[200] Seventh, Varghese states that, in his opinion with reference to the Kirchner Letter, the Board "made a material error in not pursuing this *bona fide* offer as it might have been a viable solution for the liquidity issues that came in 2012 and 2013."

Observations Regarding the Expert Opinions

[201] Varghese and Gekiere agree on a number of matters that will be addressed below. The principal differences between Varghese and Gekiere come down to the following five matters.

[202] First, Gekiere is of the view that the Former Manager had the responsibility for liquidity risk arrangements, including in particular ensuring adequate reserves for follow-on investments and bringing these matters to the Board's attention. Varghese believes this responsibility lay with the Board and that the Board failed to discharge its responsibilities.

[203] Second, Varghese is also of the view, based on his reading of the record, that to the extent the Former Manager did not discharge its responsibilities, it failed to do so, and should be relieved of any responsibility for failing to do so, because it was implementing a Board-mandated strategy of growth of assets through mergers with other LSVCCs.

[204] Third, Varghese believes that, in any event, the liquidity problems of the Fund, and in particular its inadequate reserves to fund follow-on investments in April 2010, was the result of the economic crisis of 2008, which severely limited divestitures of the Fund's venture capital

investments. He is of the view that it is inappropriate to find the Former Manager liable for failing to anticipate the depth and duration of the adverse effects of this event on divestitures during the period from September 2008 to April 2010.

[205] In contrast, Gekiere is of the opinion that the Former Manager was far too optimistic in its projections of divestures during this period given that divestitures of venture capital investments were inherently uncertain even in the absence of the economic crisis of 2008. He is of the view that the Former Manager should have included much more conservative projections in its reporting to the Board and should have recommended liquidity options to conserve cash, other than debt financing, during 2009 if not earlier.

[206] Fourth, Gekiere is of the opinion that, because the Former Manager did not recommend that the Board consider options to conserve cash in order to manage its liquidity position prior to 2010, its actions left the Fund in the spring of 2010 with the Roseway Transaction as the sole option to address its liquidity problems. As mentioned, Varghese believes that the Board, rather than the Former Manager, was responsible for liquidity management, including ensuring the maintenance of adequate reserves for follow-on investments, and that, accordingly, any failure to address options earlier to maintain cash reserves for follow-on investments was the Board's responsibility.

[207] Fifth, Gekiere is of the opinion that the Roseway Transaction was an inappropriate transaction for the Fund in April 2010 because it was effectively a loan with fixed repayment terms over a relatively short period at a high interest rate. Gekiere is of the opinion that, given the liquidity position of the Fund in April 30, 2010 as a result of the Former Manager's inaction and given the financing options available to the Fund at that time, the Fund should have ceased redemptions as soon as possible, rather than enter into the Roseway Transaction. Varghese believes the Roseway Transaction was a defensible transaction either (1) because it was the best deal available at the time or; (2) because, if the divestiture projections for the Defined Portfolio had materialized, it would have resolved the Fund's liquidity problems and, in his view, the terms of the Roseway Transaction were appropriate for the potential return to the Fund. Varghese also believes these divestiture projections were not realized because of the European financial crisis of 2011, which the Former Manager could not reasonably have foreseen.

[208] For present purposes, these differences are significant because they reflect the principal issues the determination of which underpin the Court's conclusions in this action. I will therefore address the first and second issues in the following section and the remaining issues in the analysis later of whether the Former Manager breached section 3.5 of the Management Agreement.

Observations and Conclusions

[209] The following factual determinations inform the conclusions in these Reasons.

The Significance of the Roseway Transaction

[210] The evidence is clear, and I believe undisputed, that the Fund's decision to enter into the Roseway Transaction set in motion a series of events that led to the CCAA filing in 2013. As

Varghese stated in the Varghese Opinion, "[a]ll future external financing requirements arose because of the Roseway transaction and liquidity concerns created as it related to outside third party investors."

[211] The Roseway Transaction had a finite term and required interest payments of $5.7 million in each of the three years of that term. Given the Fund's inability to sell Class A Shares as a result of the phase out of the Government of Ontario investment tax credit, the Fund's ability to satisfy the Roseway Obligations, and therefore the Fund's viability, were dependent entirely on the generation of sufficient divestiture proceeds to fund such Obligations and to fund redemptions during that period. The Roseway Transaction was intended to provide liquidity as required over this term to permit the Fund to continue to honour redemptions and to make necessary follow-on investments pending receipt of divestiture proceeds sufficient to satisfy the Roseway Obligations and to restore the liquidity of the Fund.

[212] However, as described above, the Fund consistently realized divestiture proceeds of only one-half of the amounts projected at the time of entering into the Roseway Transaction. To address the resulting liquidity gap in 2011 and thereby enable the Fund to continue its activities, including honouring redemption requests, the Fund entered into the WOF Loan. As divestiture proceeds continued to fall below expectations, the Fund was forced to cease redemptions in November 2011.

[213] Notwithstanding the suspension of redemptions, the Fund's cash flow remained insufficient. To address its continuing liquidity problems including payment of interest due to Roseway, the Fund entered into the Matrix Loan in 2012. The Fund also entered into the Newbury Transaction at the end of the year, the proceeds of which were used principally to repay the WOF Loan. While the Matrix Loan was ultimately repaid in 2013, the Fund's cash flow from divestitures remained insufficient to satisfy the Roseway Obligations notwithstanding the continuing suspension of redemptions. Accordingly, when Roseway refused to restructure the Roseway Transaction, in the absence of any refinancing alternatives, the Fund's sole option was a CCAA filing while it negotiated a potential merger that ultimately did not proceed.

[214] Accordingly, the central issue in this action is whether the Former Manager met the Standard of Care in the period prior to and including the spring of 2010 when the Fund entered into the Roseway Transaction. While similar issues are presented by the decisions to enter into the WOF Loan and the Matrix Loan, these transactions are a direct consequence of the Roseway Transaction. Accordingly, the recommendation to enter into these transactions would not have breached the Standard of Care under most circumstances unless the recommendation to enter into Roseway Transaction itself breached the Standard of Care. I have therefore not addressed these latter issues in any detail in these Reasons.

<u>The Respective Responsibilities of the Former Manager and the Board</u>

[215] As discussed above, the obligations of the Former Manager for strategic direction of the Fund are the subject of a significant difference of opinion between the experts and a matter of significance for the conclusions of Gekiere and Varghese. The issue is also important in several respects for the Court's conclusions. However, I do not think that this is a matter within the expertise of the parties' experts as it engages a legal issue.

[216] Gekiere proceeds on the basis that liquidity management was the responsibility of the Former Manager under the Management Agreement. He understands that role to encompass more than merely regular reporting to the Board in a manner that permitted an informed assessment by the Board of the Fund's current and projected liquidity position. In his view, the Former Manager was also responsible for the timely identification of future liquidity problems and pro-active recommendation of options to mitigate such concerns in order to maximize the value of the Fund's venture capital investments by ensuring the capacity to make necessary follow-on investments.

[217] Varghese proceeded on the basis that the Board was responsible for approval and oversight of the "overall vision, objectives and long-term strategy" of the Fund. Conversely, in his view, the Former Manager was responsible for implementing the Board's vision and strategy and achieving its objectives while managing the associated risks. Accordingly, in his view, the Board was responsible for approving a strategic plan and overseeing the Former Manager's implementation of the plan as well as monitoring the Fund's performance against the strategic plan.

[218] In my view, Varghese's approach to the division of responsibilities does not reflect the realities of the relationship between the Board and the Former Manager in the present context for the following reasons.

[219] The venture capital industry is a sophisticated sector of the investment market. It requires expertise not merely in the making and monitoring of investments. It also requires effective management of cash flows to ensure that necessary follow-on investments can be made to maximize the value of a fund's investments. This is particularly the case in respect of LSVCCs because their cash flows are dependent on future sales of shares to fund redemptions as well as divestitures. The Board members were not, and were not expected to be, experts in the management of an LSVCC. It was therefore inherent in the present circumstances that the Board would look to the Former Manager for the development and recommendation of a strategic plan for the Fund.

[220] Further, the management of the Fund's liquidity position could not practically be divorced from oversight of the Fund's objectives and strategic plan. Liquidity management involved an integration of the Fund's current and projected cash inflows and cash outflows as described above. In particular, it required a detailed assessment of the future cash needs, and likely divestiture values and timing, of its venture capital investments. After the announcement of the Government of Ontario, it also required a realistic assessment of the future market for the sale of the Fund's Class A Shares. The Board necessarily had to rely on the Former Manager for all of this advice as part of the Former Manager's reporting of the Fund's current and projected liquidity position. It also had to rely on the Former Manager's advice regarding the likely consequences of the Fund's projected performance for the liquidity position of the Fund and identification on a pro-active basis of policies to address projected liquidity deficits.

[221] I accept that the Board had the obligation to approve and supervise the implementation of a strategic plan for the Fund. That does not, however, exclude the Former Manager's obligation to develop and recommend a viable and realistic strategic plan for the Fund as well as to monitor, on its own, the Fund's performance relative to the plan and to pro-actively recommend options or

changes to the Fund's strategic plan in response to adverse developments. The Board members were not in a position to develop an independent analysis, or additional options for the Fund, particularly in view of the lack of any employees of the Fund itself. On the other hand, they were in a position to, and had an obligation to, assess the quality of the reporting to them, including the analysis and recommendations of alternative courses of action to the Fund, and to require that such reporting and recommendations meet best practices in the industry.

[222] Accordingly, I conclude that, in the present circumstances, the responsibility for the development of the Fund's business strategy was a joint responsibility of the Board and the Fund. In the present circumstances, it is not realistic in my view to find that either the Board or the Former Manager had the sole responsibility, or the principal responsibility, for liquidity management. Each party was intimately and regularly involved in the supervision of the liquidity management of the Fund. I note that, in its closing submissions, the Former Manager accepted that the Services included the provision of strategic advice to the Board regarding, among other matters, liquidity management. This position effective renders the issue of the Board responsibility for liquidity management, as assumed by Varghese, irrelevant, given that the principal issue is not the Board's actions but the Former Manager's actions. In any event, for present purposes, I find for the foregoing reasons that the Former Manager was equally responsible with the Board for the management and oversight of the Fund's liquidity position.

Did the Board Mandate a Growth Strategy?

[223] The Varghese Opinion proceeds on the basis that the Board established and maintained a strategy of asset growth through acquisitions and mergers throughout the period of the Former Manager's engagement. The Former Manager also asserted this position in its pleadings and elsewhere, although, as discussed below, it modified this position somewhat in its closing submissions. The evidence for this alleged growth mandate is principally as follows.

[224] First, section 7.1(b) of the initial management agreement, which dealt with the Former Manager's relationship with the Other GrowthWorks Funds, read as follows:

> The Manager covenants and agrees with the Fund that:
>
> ...
>
> (b) the Manager's intent is to work with the Funds to achieve the objective of the [Other GrowthWorks Funds]:
>
> (i) being a truly national fund group, by both raising capital and investing across Canada (other than British Columbia);
>
> (ii) being a national LSVCC leader;
>
> (iii) ultimately being the largest LSVCC group in the country (outside of Quebec); and

(iv) ultimately being the largest LSVCC group managed by the Manager (or its affiliates).

[225] This language was reformulated in the Management Agreement in section 7.1(b) as follows:

> The Manager covenants and agrees with the Fund that:
>
> ...
>
> (b) the Manager's intent is to work with the Fund to achieve the objective of the GrowthWorks Funds
>
> (i) being a national LSVCC leader;
>
> (ii) ultimately being part of the largest LSVCC group in the country (outside of Quebec); and
>
> (iii) ultimately being the largest LSVCC group managed by the Manager (or its affiliates).

[226] Second, Varghese refers to a management information circular sent to shareholders in connection with the acquisition of CSTGF and CAVI in 2005, which described as a benefit of these transactions that the Fund would "become one of the largest labour-sponsored investment funds ... in Canada." The Former Manager refers to similar language in documentation provided to the Board on April 6, 2006 in connection with the FOF Transaction. Varghese also referred to the language of a recital in the Participation Agreement in the Roseway Transaction, which he considered confirmed the existence of the growth mandate. This recital does not support such an interpretation given the text which refers only to allowing the Fund "to pursue its business objectives" without defining those objectives. It is therefore disregarded.

[227] I am not persuaded that the Board specifically mandated a strategy of asset growth throughout the period of the Former Manager's relationship with the Fund, and in particular after 2007, for the following reasons.

[228] First, the evidence is clear that the growth of the LSVCCs was an objective that made economic sense for the Former Manager. The more the assets under management, the more fees the Former Manager would receive. In addition, the Former Manager was able to achieve economies of scale. More fundamentally, the business model of Growthworks was based on the LSVCC model.

[229] However, growth by itself was not necessarily of any particular benefit to the Fund. In this regard, the reasons given by the Former Manager to explain the Fund's alleged growth strategy are not compelling. While growth could result in greater diversification of assets, diversification is not a necessary consequence of growth. It is dependent on the assets to be acquired. More significantly, diversification is a separate objective that was never formally discussed as a strategic goal, apart from the extent of diversification resulting from particular proposed merger transactions. The Former Manager also considered that size would result in a

greater fund-raising capability through the sale of Class A Shares and an enhanced venture asset deal flow. However, these possible benefits were negated by the decision of the Government of Ontario in 2005 and the lack of liquidity after April 2009 to fund new investments, respectively. The Former Manager also suggested that growth would permit retention of capable investment personnel. This was a benefit to the Former Manager but not the Fund, given that the Former Manager was already obligated contractually to provide capable management. Lastly, as Ross testified, growth might have reduced the management expense ratio of the Fund. However, there is little evidence of a material benefit to the Fund in this regard from the mergers in which it participated.

[230] Second, there is no evidence whatsoever of the alleged growth strategy in the records of the meetings of the Board and its committees. In addition, both Ross and Hopkins deny that the Board ever adopted such a strategy.

[231] Rather, the evidence is that the language for the alleged growth strategy came from the Former Manager. It was initially derived from its proposal in 2002 and incorporated into the initial management agreement in the context of the Former Manager's relationship with the other funds that it managed. There is no evidence of any discussion around the language change in the Management Agreement in 2006. Moreover, a new provision incorporated into the Management Agreement to which the Former Manager points – to accommodate the issuance of shares on future mergers without the need for further amendments to the Management Agreement specific to such shares – did not significantly change the agreement and therefore does not evidence any strategic direction of the Fund. Similarly, there is no evidence of any discussion of the Board specific to this language suggesting a greater significance.

[232] Third, the absence of any reference to the alleged benefits of growth in the documentation pertaining to the merger transactions after 2006 is at least as significant as the language identified by the Former Manager in the earlier documentation. There is no suggestion that the merger transactions were being undertaken in furtherance of the alleged strategy.

[233] Fourth, whatever the truth of the Former Manager's assertion with respect to the circumstances surrounding its original engagement in 2002, the world changed dramatically after the announcement of the Government of Ontario in 2005 and even more dramatically after the economic crisis of 2008. Thereafter, a growth strategy only made sense to the extent that it improved the liquidity position of the Fund directly or indirectly. The evidence establishes that both the Board and the Former Manager approved the merger transactions commencing in 2008 on the basis of criteria that did not include growth *per se* and certainly did not place growth above the impact on the Fund's liquidity.

[234] Lastly, and in any event, as the Former Manager itself acknowledged in its closing oral submissions, the Former Manager had an obligation to act prudently regardless of whether or not it would further a growth strategy even if one existed. That obligation included advising the Board if it considered that a proposed merger transaction or other action was imprudent or inappropriate for the Fund. The Former Manager also acknowledged that the Fund did not participate in any transaction that the Former Manager believed to be imprudent or inappropriate in order to further the alleged growth strategy. In particular, it does not justify the Roseway Transaction on the basis that it furthered the alleged growth strategy in some manner nor does it

say that it would not have recommended the Roseway Transaction but for the alleged growth strategy. More significantly, there are no actions of the Fund that the Former Manager says that it recommended because of the alleged growth strategy but would otherwise have opposed. Accordingly, the Former Manager does not actually justify any of its actions on the grounds of the existence of a Board-mandated growth strategy notwithstanding the comments of its own expert, Varghese. For this reason, I consider the existence of the alleged growth strategy to be irrelevant to the issues in this action.

Was The Former Manager's Reporting on the Fund's Liquidity From 2008 to November 2011 Misleading?

[235] The Fund says that the Former Manager breached the Standard of Care in the comprehensibility of its reporting regarding the Fund's liquidity position. In particular, the Fund says that the liquidity analyses starting in 2009 are difficult, if not impossible, to understand and appear to put forward financial results that conflict with each other. The implication is that the Board was misled by such reports.

[236] The Former Manager's reports to the Board and its committees between 2008 and April 2010, which is the crucial period for the purposes of this action, have been set out above. As they are relevant not only for this issue but also for the central issue of whether the Former Manager breached the Standard of Care, I have summarized the principal themes of the reports in this period in the following paragraphs.

[237] Prior to 2009, the Former Manager's reports contemplated a surplus of liquid non-venture capital assets over the total of all "hot money" shares. The Former Manager indicated for the first time in a memorandum to the IC for its meeting on March 19, 2009 that it projected the following: (1) a liquidity deficit after deducting all "hot money" shares of $84 million at March 31, 2009 with liquidity representing 41% of all "hot money" shares at that date; and (2) a liquidity deficit at March 31, 2010 with liquidity representing 45% of all "hot money" shares, assuming completion of the CMDF Transaction. At this time, the Former Manager recommended a liquidity plan focused on divestitures and reduced investment activity, as a result of which the Fund made its last new investment in April 2009.

[238] These projections were largely repeated in a memorandum for the Board for its meeting on September 16, 2009. That memorandum did, however, set out the four key assumptions on which the projections were based, which included sales of $10 million and divestitures of $73 million in the period between August 31, 2009 and March 31, 2010. By this time, the Former Manager had commenced a search for financing to bridge a possible temporary liquidity deficit during the 2010 RRSP season, starting with traditional institutional lenders.

[239] At the Board meeting of November 17, 2009, however, the Former Manager provided the advice that its testing indicated that the Fund's projected reserves were sufficient to meet projected cash requirements through March 31, 2010. The reporting in March and April 2010 is described in detail above and will not be repeated here. In summary, however, it reflects the Former Manager's advice that the Fund's non-venture capital assets had been liquidated to fund redemptions during the 2010 RRSP season as a result of the negative variance in respect of actual divestiture proceeds over projected levels. However, the Former Manager considered that,

on reasonable assumptions, the Fund could continue having stable cash flow to support a venture capital portfolio of approximately $100 million. To achieve this stability, however, the Former Manager recommended the Roseway Transaction as "insurance" against unanticipated liquidity challenges.

[240] I acknowledge that the presentation of the liquidity position of the Fund in these reports is not entirely "user friendly," particularly as the approach of measuring liquidity as a percentage of "hot money" capital is difficult to assess for reliability until after the end of the projection period. Further, it is not always possible to compare actual historical experience with projections based on the Former Manager's presentations, which are essentially always forward looking, particularly as the Former Manager never reported the projected versus the actual results other than in narrative form from time to time. In addition, the changing use of fiscal periods, calendar years and planning periods poses a challenge to understanding the Former Manager's reports on a comparative basis.

[241] However, the liquidity analyses provided to the Board did set out the Former Manager's assessment of the current and projected liquidity status of the Fund from time to time, as well as certain assumptions underlying the analyses at a high level and the order of magnitude expected for the forecast periods. There is no evidence that the Board regarded these liquidity reports as confusing or incomprehensible notwithstanding the change in the reporting periods. In particular, while the use of the revised liquidity coverage ratio could have had the effect of masking the deterioration in the Fund's liquidity position, there is no evidence prior to the commencement of this litigation that the Board considered that it had been misled in this respect.

[242] Accordingly, the principal issues with the liquidity analyses are: (1) the quality of the reporting regarding the Fund's current and future liquidity position; (2) the timeliness of the presentation of options available to the Fund to conserve cash flow; (3) the adequacy of the presentation of the options available to the Fund regarding liquidity management; and (4) the sufficiency of the presentation of the risks of implementation of the Roseway Transaction in the Former Manager's recommendation of that Transaction. These issues are discussed below.

Applicable Law

[243] The principal issues in this action pertain to the right of the Fund to terminate the Management Agreement pursuant to section 8.2(c) of that Agreement. Section 8.2(c) reads as follows:

> 8.2 The Fund may terminate this Agreement (subject to compliance with any applicable requirements of corporate or securities laws, regulations or policies) as follows:
>
> ...
>
> (c) upon a material breach of this Agreement by the Manager where written notice of such breach is given to the Manager by the Fund and, if such breach is capable of being remedied, the

> Manager has not remedied the breach within 60 days after such notice is received by the Manager; ...

[244] An important question that arises is the definition of a "material breach" for the purposes of section 8.2(c).

[245] This is a matter of contractual interpretation of the Management Agreement as the term "material breach" is not defined in that Agreement. The general principles pertaining to such an exercise are set out in *Ventra Inc. v. Sunrise Senior Living Real Estate*, 2007 ONCA 205, 85 O.R. (3d) 254, at para. 24. The interpretation of a "material breach" must be informed by the terms of the Management Agreement and the surrounding circumstances known to the parties at the time of the formation of the contract, including the context in which it was negotiated: see *Sattva Capital Corp. v. Creston Moly Corp.*, 2014 SCC 53, [2014] 2 S.C.R. 633, at para. 47.

[246] The Former Manager submits that a "material breach" means a "fundamental breach" as that term is understood in the common law. It relies on certain case law that suggests that a material breach is a breach that is substantial or goes to the root of the contract: see, in particular, *BA Capital Inc. v. Stream Oil & Gas Ltd.,* 2011 ABQB 91 at paras. 21-23.

[247] The Former Manager also says that the interpretation should be informed by the provisions of section 8.2(e). This provision stipulates that the Fund may terminate the Management Agreement on the fifth anniversary following a special resolution of the shareholders ratifying a Board resolution. As a related matter, the Former Manager further suggests that it is relevant for the interpretation of the Management Agreement that the Fund ceased to have any employees upon the Former Manager's assumption of the management of the Fund.

[248] In the circumstances in which courts have addressed whether a breach of contract was material in the sense of constituting a fundamental breach justifying the common law remedy of rescission of contract, the issue for the court is whether a party has failed to perform its primary obligation under the contract thereby depriving the other party of substantially the entire benefit of the contract: see, for example, *Syncrude Canada Ltd. v. Hunter Engineering Co.*, [1989] 1 S.C.R. 426. Such cases typically arise in the context of the operation of an exclusion clause in a contract. These are not the present circumstances.

[249] The present action involves the exercise of a contractual right of termination by the Fund, rather than the exercise of a right of termination under the common law by virtue of a fundamental breach. I do not read the decision in *BA Capital Inc.* as providing that, in such case or otherwise, a "material breach" must mean a "fundamental breach" as that term is understood for the purposes of the common law.

[250] Accordingly, I do not find the case law upon which the Former Manager relies to be of any assistance in this case except to the extent that, as the motion judge noted in *BA Capital Inc.*, at para. 23, "[t]he determination of material breach is fact specific and dependent upon the conduct and the contract at issue."

[251] As mentioned, the Former Manager suggests that the Fund's only right of termination is a right to terminate for fundamental breach. In my view, this is far too high a standard. The interpretation of a "material breach" for the purposes of section 8.2(c) of the Management Agreement must, however, be informed by the relationship between the Former Manager and the Fund. In this regard, the following considerations are relevant.

[252] First, as the Former Manager notes, under the Management Agreement, it is responsible for the management of essentially all of the Fund's operations and day-to-day activities. This requires a considerable investment in employees and infrastructure on the part of the Former Manager. One of the purposes of the five-year transition period contemplated by section 8.1(e) of the Management Agreement is to permit the Former Manager to recover this investment and to phase out its unnecessary operations on an orderly basis in the event of a termination of its role. Another purpose is to allow the Former Manager to participate in profits in the form of the IPA Dividends arising on successful divestitures of the Fund's venture capital assets. This suggests that a "material breach" must be a breach of sufficient significance to warrant overriding the financial benefit to the Former Manager of these transition and profit sharing arrangements.

[253] Second, on the other hand, there is clearly room for a breach that entitles the Fund to terminate the Management Agreement on less than five years' notice for actions that do not amount to a fundamental breach at common law. As a drafting matter, this intention is clear from the inclusion of a separate right of termination in section 8.2(c). As a substantive matter, it should be implied from both the extent of the Former Manager's control over the activities of the Fund as well as from the Former Manager's fiduciary obligations to the Fund.

[254] If a "material breach" had been intended to be a breach that resulted in the Fund not receiving what it contracted to receive – that is, a "fundamental breach" – there would have been no need for an additional contractual event of default. In such circumstances, the Management Agreement would have been terminable in its own right under the common law principles of fundamental breach. If the parties had intended to create a contractual right of termination for fundamental breach, the Agreement would have contained language to that effect either by way of a reference to the concept of a fundamental breach or by way of a description of the circumstances constituting a fundamental breach.

[255] More substantively, this approach to the definition of a "material breach" ignores the significant fact that the Fund represents the investment of the Class A shareholders. In this regard, the Board has fiduciary obligations which effectively must inform the Former Manager's actions. This fiduciary context implies that there must be a right of the Fund to terminate the Management Agreement if the actions of the Former Manager result in a significant adverse effect on the shareholders' investment or otherwise significantly jeopardizes that investment.

[256] Balancing these considerations, I conclude that a "material breach" of a term of the Management Agreement should be interpreted to be a breach that threatens the continued viability of the Fund from either a financial or a reputational perspective or otherwise has, or could reasonably be expected to have, a significant adverse effect on the NAV of the Fund.

Analysis and Conclusions Regarding the Claims of the Parties

[257] There is considerable interaction between the claims of the Former Manager and the counterclaims of the Fund for damages. I propose to address these issues by first addressing the claims of the Former Manager and then turning to the claims of the Fund.

Did the Fund Have the Right to Terminate the Management Agreement?

[258] In the Termination Letter, the Fund alleged six categories of breaches of the Management Agreement. In the course of this proceeding, the Fund has refined the material breaches of the Management Agreement upon which it relies to comprise the following four alleged defaults of the Management Agreement:

1. A breach of section 3.5, that is a failure to meet the Standard of Care;

2. A breach of sections 3.9(a) and 3.11, being a failure to keep proper books and records;

3. A breach of section 3.4, being a failure to comply with applicable securities legislation and regulatory requirements; and

4. A breach of section 6.1, being a failure to pay certain normal operating expenses of the Fund.

The Fund submits that the actions of the Former Manager in respect of each of these breaches constituted a "material breach" for the purposes of section 8.2(c) of the Management Agreement that entitled it to terminate the Management Agreement pursuant to that provision.

[259] The Former Manager submits that its actions did not give rise to any "material breach" for the purposes of section 8.2(c) of the Management Agreement and, accordingly, the Fund did not have the right to terminate the Agreement.

[260] I propose to address this issue by addressing each of these alleged defaults in turn, dealing first with the specific actions upon which the Fund alleges material breaches have occurred and then, to the extent necessary, setting out my conclusions regarding whether such actions constituted a "material breach" for the purposes of section 8.2(c) of the Management Agreement.

Alleged Breach #1: Breach of the Standard of Care

[261] The principal issue in this action is whether the Fund had the right to terminate the Management Agreement pursuant to section 8.2(c) by reason of the existence of a material breach of the Standard of Care by the Former Manager.

[262] More specifically, the Fund says that the Former Manager breached the Standard of Care by failing to exercise the degree of care, diligence and skill that a reasonably prudent person in the position of the Former Manager would have exercised in the period between 2008 and 2010 in failing to recommend that the Fund cease redemptions of its Class A Shares prior to, or during

the spring of, 2010 and, instead, in recommending that the Fund enter into the Roseway Transaction and subsequently both the WOF Loan and the Matrix Loan. As mentioned, I will address this question by addressing first whether the Fund has established a breach of the Standard of Care and then whether any such breach is a "material breach" for the purposes of section 8.2(c) as that term has been interpreted above.

Did the Former Manager Breach the Standard of Care?

[263] The Fund asserts that the Former Manager acted negligently in a number of respects that have been identified by Gekiere, upon whose opinion it relies. I will address this position after first addressing a preliminary issue raised by the Former Manager.

Preliminary Issue

[264] The Former Manager submits that, even if the Court were to determine that the Roseway Transaction was an inappropriate transaction for the LSVCC in hindsight, the Court should not find that it breached the Standard of Care in recommending the Transaction for two reasons.

[265] The first reason is that, according to the Fund, it is protected by the "business judgment" rule. The simple answer to this submission is that the "business judgment" rule is a common law rule whereas the present action addresses whether or not a contractual standard of care has been satisfied. The present action therefore does not engage the "business judgment" rule.

[266] As a related matter, I also do not think that the Board's involvement in the approval of the Roseway Transaction necessarily excludes a finding adverse to the Former Manager except in circumstances in which the Board expressly mandated a course of action that the Former Manager opposed, which are not the present circumstances. There is nothing in the Management Agreement that expressly provides a safe harbour for actions approved by the Board. Nor do I think that the Board's acceptance of the Former Manager's recommendations constitutes evidence in its own right that the recommendations satisfied the Standard of Care, given the Board's oversight responsibilities.

[267] There is also an important policy issue at play in this case. The Fund was a fiduciary for the money of its Class A shareholders. The Board had an obligation to manage that money responsibly. It engaged the Former Manager to perform that management function, including the provision of strategic advice to the Board regarding liquidity management. The Former Manager held itself out as having specialized knowledge in the area of LSVCCs and was well aware of the Board's obligations. The Former Manager had an obligation to make recommendations that satisfied such obligations. I think it is therefore inappropriate to find that the Board's acceptance of the recommendations of the Former Manager, by itself, negatives any finding of a breach of the Standard of Care.

[268] The more difficult issue is the Former Manager's second argument – that the Court should not apply hindsight to decide this issue. I agree to the extent that it is necessary to ask whether the Former Manager's recommendation of the Roseway Transaction was reasonable in the context in which this recommendation was made.

[269] This is a challenging test to apply. A court must be reluctant to second-guess strategic recommendations made by an experienced investment fund manager, or to evaluate the quality of reporting on liquidity management matters upon which such recommendations were based, particularly in circumstances in which the recommendations were considered and accepted by the Board. However, I see no legal impediment to making such determinations even after the fact. The issue is whether, in the circumstances, there was no reasonable justification for the recommendations to the Board and, similarly, whether the reporting to the Board was so inadequate that it did not reasonably support such recommendations. In this case, the issues are informed by expert evidence as to the Standard of Care expected of a fund manager of an LSVCC in the period after the economic crisis of 2008. The Court's determinations herein reflect its findings regarding the applicable Standard of Care, as informed by the expert evidence before the Court, taking into consideration the market environment created by the economic crisis as well as pre-2008 events. It is not simply applying hindsight to fix responsibility for the Fund's subsequent history.

Did the Former Manager Breach the Standard of Care?

[270] While I do not accept the entirety of the Fund's position or Gekiere's analysis, I am of the view that the Former Manager breached the Standard of Care in the following four inter-related actions:

(1) During the period between 2008 and 2010, it provided inadequate reporting to the Board regarding the future liquidity position of the Fund;

(2) It failed to raise the option of ceasing redemptions until after the 2010 RRSP season;

(3) It failed to provide an adequate assessment of the options available to the Fund at the time of its recommendation of the Roseway Transaction; and

(4) It recommended that the Fund enter into the Roseway Transaction despite evidence at the time that this was an inappropriate transaction for the Fund.

I will address each of these findings in turn. I would add that I think the same considerations apply in large measure to the Former Manager's recommendation that the Fund enter into the WOF Loan. However, as mentioned above, given the centrality of the Roseway Transaction, any issues pertaining to the WOF Loan are secondary and I have therefore limited my analysis to the events leading up to and including the Former Manager's recommendation of the Roseway Transaction.

The Former Manager's Reporting of the Liquidity Risks of the Fund and their Potential Consequences During the Period 2008 to April 2010

[271] An important issue in this action is the quality of the Former Manager's reporting to the Board in the period following the economic crisis of 2008. As mentioned, I propose to concentrate on the period to and including the Board meeting of April 27, 2010 at which the

Roseway Transaction was approved, given the significance of the Roseway Transaction for the fate of the Fund.

[272] The experts agree that, in hindsight, the Former Manager's projections for the Fund's liquidity in this period as set out in its reports to the Board were overly optimistic. They also agree that this was principally due to overly optimistic projections of divestitures in this period, and secondarily of sales of Class A Shares. Moreover, they also agree that the low level of divestitures in this period, while due to a number of factors, was principally due to the weak M&A and IPO markets through which the Fund would expect to sell or otherwise divest its venture capital investments. The experts disagree, however, on whether the Former Manager's liquidity reporting met the Standard of Care notwithstanding these overly optimistic liquidity projections.

[273] Varghese believes that the failure of the Fund to meet the liquidity targets in the Former Manager's reports was due to the state of the M&A and IPO markets for the divestiture of the Fund's venture capital investments. He is of the view that the Former Manager should not be held to be responsible because the state of these markets was beyond its control and was unpredictable. Moreover, based on his view of the respective responsibilities of the Former Manager and the Board, he believes that the Former Manager discharged its responsibilities by providing the liquidity reporting to the Board described above and that any failure to appreciate the liquidity problems of the Fund in a timely manner or to consider options to address such liquidity concerns rested with the Board.

[274] Gekiere believes that, given the inherent uncertainty of the markets for venture capital investments in normal markets, and given the Fund's reliance on divestitures to maintain its liquidity for the reasons discussed above, the Former Manager had to meet a higher standard in respect of its liquidity reporting after the economic crisis of 2008. He considers that the Former Manager's reporting was inadequate in two principal respects. First, he considers that the Former Manager failed to apply conservative assumptions for divestitures, or at least to provide alternative projections based on more conservative assumptions, reflecting the Fund's actual experience of divestitures after the economic crisis of 2008. He also considers that the Former Manager should have established thresholds that would have required the Board to address the deteriorating liquidity position of the Fund on a pro-active basis when the thresholds were exceeded.

[275] The Former Manager's reports during the period from the economic crisis to April 2010 have been summarized above. From that summary, I conclude that Varghese is correct in observing that the Former Manager was aware of the significance of liquidity for the Fund and provided reports respecting the projected liquidity position of the Fund as of March 31, 2010. It also recommended a liquidity plan in the spring of 2009 and pursued a financing option commencing in the summer of 2009 to address unanticipated liquidity problems. However, the issue in this section is not merely whether the Former Manager was aware of the future liquidity issues facing the Fund or whether the Former Manager provided the Board with reports on the Fund's liquidity and recommendations for conserving cash or otherwise dealing with liquidity challenges. Rather, the issue is whether such reports and recommendations were adequate given the financial and economic circumstances of the Fund after the economic crisis of 2008.

[276] As mentioned, a court should be cautious about second guessing the actions of an investment fund manager with the benefit of hindsight. In particular, a court should avoid finding that projections were unrealistic at the time of their creation in circumstances in which unanticipated market developments beyond the control of a party were the predominant factor in a failure to meet such projections. Nevertheless, this action presents circumstances that are sufficiently unusual and extreme that I conclude that the Court is justified in finding that the Former Manager's reporting to the Board was inadequate in two inter-related respects: (1) in its overestimation of the liquidity position of the Fund based on unduly optimistic and unjustifiable projections; and (2) in its failure to consider alternative scenarios given the Fund's continuing adverse experience regarding divestitures. I will address the first issue in this section and the second in the next section after addressing my assessment of the expert evidence on these issues.

[277] As a preliminary matter, I regard these issues as matters properly informed by the expert evidence before the Court. In reaching the determinations on these issues, I have preferred the evidence of Gekiere over that of Varghese on these issues, as well as on the remaining issues in respect of the alleged breach of the Standard of Care, for three reasons in particular.

[278] First, the Varghese Opinion is based upon, or coloured by, a number of assumptions that the Court has rejected. In particular, Varghese proceeds on the basis that the Board mandated a strategic plan that placed the highest priority on growth. He considers that the Former Manager was released from responsibility for the consequences of any failure to address liquidity issues as a higher priority because it was required to respond to this mandate. Given the conclusion above that there was no growth mandate, I have rejected this position of Varghese.

[279] Second, the Varghese Opinion relies on the view that the Board's failure to fulfil its responsibilities of oversight and management of the Former Manager relieved the latter of responsibility for any failure to meet the Standard of Care in the performance of the Services. Given my view of the joint responsibility of the Board and the Former Manager for liquidity management, I have also rejected this position of Varghese.

[280] There is a further important implication of the Court's finding on the allocation of responsibilities. Varghese is critical of the Board's inaction in a number of respects, which he is of the opinion constituted negligence. In particular, he is of the opinion that, from the first quarter of 2006, after the disappointing sales in the RRSP season, "a prudent board should have known and anticipated the dramatic decline in sales that followed and should have taken preventative measures from that moment in time." Varghese's view that the Board failed in its risk assessment and management function in relation to this development is equally an indictment of the Former Manager. Similarly, Varghese believes the Board failed in its duty of care to reassess the liquidity risk and business strategy of the Fund in 2008 in the aftermath of the economic crisis in that year. This is equally a failure on the part of the Former Manager. In short, given the Court's view of the joint responsibility of the Former Manager and the Board for liquidity management, Varghese's criticisms of the Board's failure in this regard are equally criticisms of the Former Manager's actions that support the Fund's position that the Former Manager breached the Standard of Care.

[281] Lastly, on occasion, Varghese overstepped his role as an expert and acted as an advocate for the Former Manager. This advocacy was reflected, among other things, in his reliance for the

purposes of his opinion on a number of matters which were well beyond his specific expertise or knowledge, including the likely position of the securities regulatory authorities to a cessation of redemptions in the spring of 2010 and the likely outcome of the transaction proposed in the Kirchner Letter. With respect to the latter in particular, there is no basis for his conclusion that the Kirchner Letter represented a *bona fide* offer in the sense that it would have resulted in a sale in the discount range suggested in the letter nor is there a basis for his conclusion that a consummated transaction would have been a "viable solution" to the Fund's liquidity problems at the time.

[282] In the end, however, the issue comes down to whether the Former Manager's reporting adequately identified and pro-actively addressed the financial and economic circumstances of the Fund in the period following the economic crisis of 2008.

[283] Gekiere says that, given the acknowledged need for increased liquidity in fiscal 2009 and thereafter from circumstances that pre-dated the economic crisis, as discussed above, and given the inherent uncertainty of divestitures apart from the effect of the economic crisis, a higher standard was required of the Former Manager in its reporting on liquidity-related issues in the period between 2008 and April 2010 than was provided to the Board.

[284] In this regard, the Former Manager's reporting of the liquidity position of the Fund evolved over the period between 2008 and November 2011. In broad terms, as set out above, the Former Manager's reporting in the period prior to April 2010 essentially relied on a base case that reflected a single set of assumptions regarding projected sales and divestitures with one exception discussed below. Beginning with the Board meeting of September 30, 2010, the Former Manager began to provide an analysis based on alternative levels of divestiture proceeds and redemptions rates. Ultimately, in its memoranda for the Board meetings on September 27, 2011 and October 27, 2011, the Former Manager provided to the Board a considerably more detailed analysis of the potential outcomes given differing levels of redemption and divestitures.

[285] In my view, the content required of the Former Manager in its reporting to the Board on the actual and projected liquidity position of the Fund from 2008 had to be informed by two general considerations.

[286] First, the Fund's circumstances in 2008 required that the Former Manager elevate the level of its reporting regarding the current and projected liquidity of the Fund over that which it provided prior to the economic crisis of 2008 for the straightforward reason that, even without the 2008 economic crisis, the Fund's liquidity was going to be significantly reduced commencing with the 2009 RRSP season. By 2009, the Fund had a significantly reduced capacity to raise additional capital by the sale of Class A Shares and had made its last new investment. The Fund was also facing a predictable steep increase in redemptions. These factors were reflected in the Fund's equally predictable increasing dependence on divestitures and corresponding increase in the risk of a liquidity default.

[287] Second, the economic crisis of 2008 significantly adversely affected the M&A and IPO markets and thereby further increased the risk of a liquidity default arising from a potential inability to achieve divestitures in the amount and on the timeframe previously anticipated.

[288] Accordingly, as a "mature" fund, the focus of the Fund had to be the maximization of the value of the existing portfolio with a view to maximization of the return of capital to the existing Class A shareholders. That focus, in turn, required that the Fund concentrate on maximizing the ability of the Fund to maintain its capacity to fund follow-on financings of its portfolio to achieve an orderly divestiture of that portfolio. In addition, in its actions, the Fund had to ensure fairness among its Class A shareholders.

[289] The Former Manager's reporting needed to assist the Board in its determination of the course of action that best achieved these objectives. In particular, the Board required credible reporting regarding two principal factors: (1) the increasing level of redemptions, as a result of events that pre-dated the economic crisis of 2008; and (2) capital inflows, given the very uncertain IPO and M&A markets for the divestiture of the Fund's venture capital investments and the increasingly difficult market for the sale of additional Class A Shares.

[290] Based on the evidence before the Court, I accept Gekiere's opinion that the Former Manager's reporting to the Board was inadequate for the following three principal inter-related reasons.

[291] First, the Former Manager's projections regarding the amount and timing of divestitures for the 2009 and 2010 planning years, as well as of further Class A Share sales, were not merely optimistic. The evidence is that they were unrealistic because they were not based on the economic and political environment facing the Fund at the time. I accept Gekiere's assessment that the combination of the factors described above affecting the Fund's liquidity position required that the Former Manager's reporting to the Board contemplate, at a minimum, levels of divestitures and sales of Class A Shares that reflected the actual experience since 2008, rather than the levels necessary to maintain redemptions and follow-on investments at projected levels.

[292] In particular, despite the experience in fiscal 2008 and 2009, the Former Manager optimistically projected divestitures of approximately $100 million in fiscal 2010. Further, despite the experience in that year, it maintained a similar projection for fiscal 2011. There is no discussion in the materials before the Board that justifies the Former Manager's optimism regarding the recovery of the IPO and M&A markets implied by these projections in either fiscal year. Similarly, there was no justification for the Former Manager's projection of the level of continuing sales of Class A Shares in those years. As a related matter, as discussed below, there was also no documentary support for the values ascribed to the Defined Portfolio in connection with the approval of the Roseway Transaction.

[293] Second, as mentioned, the Former Manager's reporting on the Fund's projected liquidity position up to and including April 2010 relied on a single base-case that used a single set of assumptions regarding sales and divestitures. The Former Manager merely referred in narrative form to the risks to the Fund's liquidity of inadequate divestitures. It did not include alternative liquidity scenarios that addressed levels of divestiture proceeds that reflected the Fund's recent experience. Indeed, the reporting lacked any quantitative analysis permitting an assessment of the likelihood of such outcome. This reporting was inadequate given the Fund's circumstances in the period between 2008 and April 2010. If the Former Manager chose to present its base case using optimistic assumptions, it should also have provided alternative scenarios, or a sensitivity

analysis, based on the recent historical experience in order to permit an assessment of the viability of the base case.

[294] The Former Manager did begin liquidity reporting in greater detail using a new template in the spring of 2009. That form of reporting did consider alternative levels of redemptions. However, in fact, the level of redemptions remained close to 35% of "hot money" capital in each of the years between 2008 and 2012. The fluctuations in the level of redemptions during this period were not, by themselves, a significant contributor to the Fund's liquidity problems in 2010, as opposed to the absolute level of redemptions, which was. The real risk to the Fund's liquidity, as the Former Manager repeatedly stated in its memoranda, was the amount and timing of divestitures and, secondarily, the level of sales of new Class A shares. There was, however, no sensitivity analysis presented around various divestiture scenarios.

[295] I acknowledge that the liquidity models appended to the liquidity status memorandum delivered to the Board for the meeting of April 27, 2010 did present a projection for the 2011 planning year using divestiture proceeds amounting to 50% and 75% of projected divestitures, apparently for the first time. However, there is no indication that the Former Manager drew the Board's attention to the implications of these models. Nor did the Former Manager alter its conclusions from the first draft of that memorandum. It simply inserted the phrase "except where venture exits are at risk". Instead, the Former Manager continued to rely on the results of these models to demonstrate the long-run viability of the Fund rather than to focus attention on the risk of a liquidity default in the next twelve months. In short, instead of facing the potential consequences of these alternative scenarios, the Former Manager drove on with its recommendation of the Roseway Transaction.

[296] Accordingly, the memoranda provided eighteen months later in the autumn of 2011 stand in a stark comparison with the extent of reporting and the degree of analysis provided prior to and at the time of the Roseway Transaction. Against this standard of reporting, which I agree with Gekiere represented the quality of reporting that was necessary to satisfy the Standard of Care from and after the 2008 economic crisis, the Former Manager's reporting up to April 2010 was clearly inadequate.

[297] Third, for the same reasons, I conclude that Gekiere is correct in his view that these circumstances required the Former Manager to articulate threshold levels at which it would be necessary to consider alternative means of maintaining follow-on investments and an orderly divestiture process if the cash flow projections proved inadequate. There is no evidence that the Former Manager ever approached its reporting on liquidity management on this basis.

[298] For the foregoing reasons, I therefore find that the Former Manager did not satisfy the Standard of Care in its reporting to the Board regarding the liquidity position of the Fund between the 2008 economic crisis and April 2010.

The Former Manager's Recommendations to the Board Regarding Options for Dealing with the Liquidity Challenges of the Fund During the Period Between 2008 and April 2010

[299] From the summary of the Former Manager's reporting to the Board during the period from 2008 to April 2010, it is clear that the Former Manager did not provide the Board with options for consideration with a view to averting a possible liquidity squeeze until after the 2010 RRSP season, other than a debt financing to address temporary liquidity deficits.

[300] Both Varghese and Gekiere agree that the economic crisis of 2008 fundamentally changed the market for divestitures, and required a re-assessment of the Fund's strategy and its risks, including its liquidity risk. There is, however, no evidence of any formal recognition, let alone action, on the Former Manager's part in this regard, at least until the spring of 2009 when the Former Manager recommended that the Fund cease making new investments and concentrate on divestitures. However, even then, the Former Manager's recommendation of ending new investment was belied by its continued recommendation of the CMDF Transaction. Essentially, as Varghese noted, both the Fund and the Former Manager continued on a "business as usual" basis until the end of 2009.

[301] Further, as Varghese observes, there also does not appear to have been a recognition on the part of the Board, and I would therefore add on the part of the Former Manager, of the need to address the liquidity position of the Fund on an immediate basis in the fall of 2009. There was no discussion of liquidity options at the Board meeting on November 17, 2009 apart from a report on the Former Manager's efforts to obtain traditional financing. Varghese and Gekiere both agree that, by this time, such a discussion had become critical, although Varghese places responsibility for this failing on the Board. This is all the more significant given that the Former Manager was itself aware of the potential for such a situation in the fall of 2009 for the reasons discussed above and had already had discussions with prospective lenders including Comerica Bank and the Royal Bank who declined to offer financing.

[302] The result was two-fold. First, the Board was presented with a radically different liquidity position in the spring of 2010 from the position that the Former Manager projected as late as November and early December of 2009. The Board was effectively presented with a long-term, rather than a temporary, liquidity deficit. Second, as a consequence of the Former Manager's assessment of the Fund's liquidity position and its concentration on its preferred option of a debt financing for which it had not yet been successful in identifying a lender, the Former Manager failed to recommend consideration of the option of ceasing redemptions at any time during 2009. By the time the full extent of the Fund's liquidity difficulties in early 2010 was placed before the Board, the 2010 RRSP season had ended. Accordingly, the option of suspension of redemptions to preserve the cash flow that was paid out on redemptions during that period was lost.

[303] Given the circumstances of the Fund in late 2009, I conclude that, by this time, the Former Manager should have recommended consideration of all of the options for dealing with a liquidity deficit if it materialized in the spring of 2010, including a cessation of redemptions. I therefore also find that, because the Former Manager's actions pre-empted the Fund's consideration of a cessation of redemptions prior to the 2010 RRSP season, the Former Manager further failed to satisfy the Standard of Care.

[304] There is a larger picture to this analysis to be addressed. The Fund attributes the Former Manager's actions to a self-interested desire to maintain or increase its management fees, which

required growth in the value of the Fund's venture capital portfolio. While I do not accept this view as the principal explanation of the Former Manager's actions, it raises a fundamental question regarding its motivation and the consequences for the Fund. As the Former Manager recognized, belated in my view, in a memorandum for the October 27, 2011 Board meeting described above, the Fund "had effectively entered a "wind-down phase." In my view, the Former Manager failed to appreciate that this was the economic reality of the Fund in the spring of 2010 with the significant consequences that these circumstances had for the Fund's prospects as an on-going investment fund. Moreover, the former Manager's denial of this reality continued until the autumn of 2011, by which time it was too late to remedy the situation.

[305] Both Varghese and Gekiere agree that a prudent manager had to appreciate that the LSVCC model was "broken" after the announcement of the Government of Ontario in 2005. While it was not unreasonable to lobby for a reversal of that decision, or for acceptance of a replacement proposal, it was not reasonable to factor any such considerations into projections for share sales unless and until there was an actual legislative change. Nevertheless, despite the significant drop in sales after the announcement of the Government of Ontario, which Varghese describes as "drastic," the Former Manager continued to include sales projections in its liquidity reports for which there was no reasonable basis for the years commencing in 2010 and to refer optimistically to prospective legislative developments as a basis for its optimistic projections.

[306] More generally, as stated above, by late 2009, the Fund was a "mature" fund in the sense that it had only a negligible capacity to raise additional capital by the sale of Class A Shares and had made its last new investment. It was therefore not appropriate to proceed on the basis of a strategic plan for the Fund that assumed an indefinite future for the Fund based on the sale of additional Class A Shares to new shareholders in the absence of an actual legislative change. The focus of the Fund should have been on the maximization of the returns to the existing Class A shareholders of the proceeds of the existing venture capital portfolio.

[307] As mentioned, the Former Manager appears to have turned a blind eye to this reality believing instead that the Fund was fundamentally viable, that it was experiencing temporary liquidity challenges only, and that the Fund would be restored in due course to the status of a viable ongoing fund that was able once more to rely on cash inflows from the sale of Class A Shares. Indeed, the Former Manager ardently wished to believe that the Fund was not only viable as an ongoing retail fund but also that it was able to exploit the opportunities presented by other LSVCCs that were experiencing liquidity problems. The overall impression, which is reflected in certain language in the Former Manager's memoranda, is that the Former Manager's approach was driven by an unquestioned assumption that the best course of action for the Fund was business "as usual" – including, in particular, maintaining redemptions – rather than a course of action which maximized the return of capital to the existing Class A shareholders on an orderly basis based on a more objective assessment of the actual financial and economic circumstances of the Fund in 2009 and 2010. In short, it appears that is, that "the wish was father to the thought."

[308] These unrealistic views of the Former Manager are reflected, for example, in the memorandum to the IC for its meeting on March 18, 2010 in which the Former Manager opined that the Fund was in excellent shape based, among other factors, on an assessment that the Fund's venture capital portfolio was in excellent shape and a positive change on the government

relations side. As mentioned above, there was no basis for assessing the Fund's status based on the state of government relations at the time. More significantly, while comfort regarding the inherent value of the venture capital portfolio in a value-maximizing divestiture process was a necessary condition of proceeding with the Roseway Transaction, the more important issue was the likelihood of completing such a value-maximizing divestiture process within the timeframe imposed by the Roseway Transaction. This was not addressed in any memoranda in April 2010 but was rather assumed.

[309] This mindset also appears to have driven the Former Manager's approach to its projections for divestitures and sales of Class A shares. The best example is found in the Former Manager's report on liquidity to the IC meeting of March 18, 2010. The minutes of that meeting report that "in light of the projected redemptions in the 2011 Planning Year as well as operating expenses, the Manager is proceeding on the assumption that divestitures will need to exceed investment activity by upwards of $70 million to maintain current liquidity levels. Investment activity is estimated at $23 million this coming year..., the Manager is preliminary [sic] targeting $100 million of divestitures in the 2011 Planning Year." In other words, the Former Manager established the divestiture target of $98 million to accommodate the Fund's requirements to maintain redemptions and make its projected follow-on financings despite the historical experience, the continuing impact of the 2008 economic crisis on the markets, and an acknowledged inability to control divestiture decisions of the other shareholders in the Fund's venture capital investments.

[310] Similar language appears in a memorandum to the IC dated April 7, 2010 for its meeting on April 15, 2010. In this memorandum, the Former Manager stated that "[t]o build a strong liquidity position for the Fund, we are planning for another strong years of exits. At this time, we have preliminarily targeted $100 million of venture exits to occur during the 2010/2011 RRSP year." Apart from the suggestion that the planning year just ended was a "strong year of exits", which is clearly incorrect, it is very difficult to reconcile the $100 million projection with the projections in the memorandum to the IRC for its meeting in February 2010 which has been described above. That memorandum suggests that such targets could only be reached if divestitures were achieved that had only a "possible" level of occurrence, i.e. were not "probable" according to the Former Manager's own weighting scale.

[311] I appreciate that this language could be said to evidence no more than an intention on the part of the Former Manager to try to bring to fruition various divestiture opportunities that it had identified. In my reading of all the circumstances, however, this would be a misreading of what was happening. It is one thing to identify possibilities. It is quite another to base projections on such activity without a high probability of realization, as appears to have occurred in this instance.

[312] This mentality is also reflected in the financial model that the Former Manager prepared suggesting that the Fund would settle into a steady-state of approximately $98.5 million. It was also the motivation for a number of actions after the Roseway Transaction – in particular, the pursuit of the Proposed VenGrowth Transaction.

[313] Such a preference for continuation of the Fund as an on-going investment fund is natural enough, given that GrowthWorks' business model was based on LSVCCs. However, by

proceeding in this manner and in concentrating on these activities in 2009, 2010 and 2011, the Former Manager did not provide the Board with any analysis or recommendations regarding alternative views of the best interests of the Class A shareholders as they existed in 2009 and 2010. Rather, the Former Manager's advice and recommendations reflected an unquestioned view of the best interests of the Fund as a going concern having an indefinite future, including on-going turnover in its Class A shareholder base. As a consequence, among other things, not only did the Former Manager fail to consider adequately the risks of a liquidity deficit arising from the continuation of redemptions given the economic environment for divestitures, but it also did not consider the fairness issues identified by Gekiere pertaining to continued redemptions after entering into the Roseway Transaction.

[314] In my view, the foregoing actions constituted a failure on the part of the Former Manager to meet the Standard of Care in its advice to the Board regarding the options available to the Fund in respect of the liquidity management of the Fund and the best interests of its existing Class A shareholders.

The Former Manager's Presentation of the Options Available to the Fund in April 2010

[315] The Fund submits that the Former Manager did not present the options available to the Fund to address its liquidity concerns in the spring of 2010 in an unbiased and thorough manner that satisfied its obligations of diligence and skill. For its part, as evidence that there was a thorough airing of the Fund's options, the Former Manager points, among other things, to the fact that the IC examined the alternatives in two meetings prior to the Board meeting of April 27, 2010. It also points to the memoranda prepared for those meetings of the Board and the IC which have been described above.

[316] I find that the Former Manager failed to present the options available to the Fund in an adequate manner. In this regard, the following five general considerations are of primary significance.

[317] First, the Former Manager characterized the Roseway Transaction as a form of "insurance." In my view, this was not an accurate characterization of the Transaction at the time that it was recommended to the Board for the following reasons.

[318] The evolution of the concept of the Roseway Transaction as "insurance" for the Fund bears close examination. In 2009, the Former Manager initiated a search for a lender with a view to providing short-term financing to bridge redemptions, particularly during the 2010 RRSP season, pending receipt of divestiture proceeds expected shortly after the close of that season. When no traditional lender was identified, the Former Manager arranged the WOF credit facility in early 2010. This credit facility was recommended as fulfilling the need for such short-term financing.

[319] In a memorandum prepared for the April 27, 2010 Board meeting, the Former Manager stated that "the [Fund] has a plan in place whereby net positive cash flows from the venture capital portfolio will be more than sufficient to meet the Fund's redemption obligations, allowing the Fund to sustain its critical mass over the long-run." As described above, in the memoranda presented to the Board by various representatives of the Former Manager, the Roseway

Transaction was presented in a number of ways that treated the Roseway Transaction as a means of ensuring that the Fund was able to realize this plan. In particular, the Roseway Transaction was described as "insurance against the risks to liquidity that arise outside the Fund's control," as "providing the Fund with the ability to realize on the full value of its portfolio via orderly and value-optimized exits" and as "insurance for postponed exit activity."

[320] As actually used, the Roseway Transaction served as a medium-term bridge financing to permit continuing redemptions and to finance follow-on investments over a three-year period pending receipt of divestiture proceeds by the end of that period that would materially exceed the cost of the Roseway Transaction. In other words, the Roseway Transaction was, in essence, a three-year loan that was intended to fund redemptions pending receipt of divestiture proceeds that were not expected to restore the Fund's liquidity on a more permanent basis until the end of that period.

[321] Accordingly, insofar as the Roseway Transaction was presented as "insurance," I think that is a mischaracterization for three reasons. First, the loan was fully advanced in May 2010 rather than dispersed as required from time to time to address short-term liquidity needs and repaid from time to time when liquidity was restored. By the time the Roseway Transaction closed, it funded a long-term liquidity deficit rather than functioned as a temporary bridge loan. Second, I accept Gekiere's characterization that the Roseway Transaction was not used to fund future redemptions. Essentially, it funded the redemptions of Class A Shares that had occurred in the 2010 RRSP season, as such redemptions had resulted in the longer term liquidity deficit that was addressed by the Roseway Transaction. Third, given the foregoing, I do not think there was any reasonable basis for the statement in the memorandum to the IC for the meeting on April 15, 2010 regarding strategic options for the Fund that "the Fund's base-case liquidity analysis shows that… a secondary transaction [i.e. the Roseway Transaction] was not necessary...". In fact, the opposite conclusion was expressed very clearly in the February memorandum delivered in connection with the IRC meeting at that time described above.

[322] The second general consideration is that, in presenting the Roseway Transaction as "insurance," the Former Manager failed to set out the very real inherent risks of the Transaction. As mentioned above, from the outset, the viability of the Roseway Transaction was tied to the timing of, and the proceeds to be realized on, the divestment of the Fund's portfolio of venture capital companies, in particular the investments comprising the Defined Portfolio. The Roseway Transaction made economic sense only if sufficient investments included in the Defined Portfolio could be divested in an orderly way that realized an increase in value of approximately $33 million within three years (from a base of $100 million) and could be carried until such time, including funding any necessary follow-on investments. There is, however, no evidence that the risk that the foregoing scenario would not materialize was discussed with the Board. To the contrary, the only discussion appears to be the Former Manager's statement that it believed the value of the Defined Portfolio to be substantially greater that its $100 million carrying value. As a related matter, there is very little, if any, sensitivity analysis that would have permitted such an assessment of risks.

[323] The third general consideration is that the analysis of the Fund's liquidity position in April 2010 was based on two assumptions that were unduly optimistic at that time. As mentioned, in its memorandum to the IC for its meeting on March 18, 2010, the Former Manager

expressed confidence in the Fund's "continuing prominence" based, among other things, on evidence of a positive change on the government relations side. There was no basis for building such an assumption into a recommendation at that time. In addition, the Former Manager based its projections for the Fund's liquidity on divestitures of approximately $100 million in the 2011 planning period despite, as mentioned, two years of divestitures of approximately $50 million, no evidence of material improvements in the markets at that time, and its own internal probability assessment of the occurrence of divestitures totaling this amount, as set out in the memorandum to the IRC in February 2010.

[324] Fourth, the Former Manager presented the option of cessation of redemptions in an unduly drastic manner without having had any direct discussion with the BCSC regarding its position on such an option. As is demonstrated in its later conversations with the BCSC, the Former Manager conceived of the option of the cessation of redemptions as necessarily implying a "liquidation-style" wind down of the Fund over a very short period of time with significant attendant losses in the realized value of its venture capital investments. It did not consider the possibility that the securities regulatory authorities might have permitted a more orderly wind down over a longer period of time.

[325] I appreciate that the Former Manager had regard to the orders previously granted by securities authorities to other LSVCCs. However, the Fund was not alone among LSVCCs in experiencing a liquidity problem in 2010. This was an ongoing challenge for the securities regulators as well. All parties were concerned with preserving shareholder value on a basis that was fair to all shareholders. As the subsequent discussions with the BCSC, and in particular an email of the BCSC dated July 23, 2012, indicate, it is at least as likely that the securities regulatory authorities would have been prepared to be more flexible than the Former Manager assumed if it had initiated the process much earlier. Further, as the Former Manager itself noted later, the Fund's position was more favourable than the circumstances of the other funds in respect of which orders had been granted by the securities regulators in that a materially larger proportion of the value of its NAV represented investments in advanced stage companies. The Former Manager argued for a three-year period for the RMP eighteen months later on this very basis.

[326] In any event, the Former Manager failed to explore the possibility of a longer-term wind-down scenario with the BCSC prior to providing the advice it did. It was inappropriate for the Former Manager to have advised the Board that the securities commissions would have imposed a liquidation-style wind down over a short period of time in the absence of any such discussions with such authorities.

[327] Finally, in my view, for the reasons set out above, the appropriate manner of comparison of the Roseway Transaction option against a cessation of redemptions was an assessment of which option would maximize returns to the existing Class A shareholders. There is, however, no evidence of any assessment of the options on this basis. As the BCSC noted, there was no assessment of the likely returns in an orderly wind-down scenario until October 2012. Instead, the memoranda on the cessation of redemptions alternative referred to the risk of a class action lawsuit, for which there is no evidence of a real risk in the record, and concluded that the likely result would be the sale of the Fund's assets by merger or otherwise at a steep discount. Even if the merger or sale scenario had occurred, it is not clear on the evidence before the Court that this

would have resulted in lower returns to the existing Class A shareholders as the memoranda assumed. While there would undoubtedly have been a reduction in portfolio value if this option had been pursued rather than the Roseway Transaction, it is certainly arguable that the existing Class A shareholders would have been better off. More fundamentally, it is also arguable that this was the proper course of action from a legal perspective in order to treat all of the existing Class A shareholders fairly in circumstances where there was a real likelihood that the Fund was no longer viable from a liquidity perspective.

[328] Accordingly, I conclude that the Former Manager also failed to satisfy the Standard of Care in its advice to the Board regarding the alternatives to the Roseway Transaction that were available to the Fund in the spring of 2010 to address its liquidity difficulties, in particular, the option of the cessation of redemptions.

The Former Manager's Recommendation of the Roseway Transaction

[329] The central issue in this action, as mentioned, is whether the Roseway Transaction was an appropriate transaction for the Fund in April 2010. This issue must be examined in the context of whether, given the liquidity problems facing the Fund at the end of 2009, the better course of action was for the Fund to enter into the Roseway Transaction or to cease redemptions prior to the 2010 RRSP season. I am satisfied that the evidence establishes that the Board's decision to enter into the Roseway Transaction was objectively a bad decision in that the Fund would have been better advised to cease redemptions in 2009 rather than to enter into the Roseway Transaction for the following reasons.

[330] The summary history set out under "The Significance of the Roseway Transaction" demonstrates that, in retrospect, the Roseway Transaction set in motion the circumstances that resulted in the CCAA proceedings in 2013 given the Fund's insufficient receipt of divestiture proceeds to repay the loan after entering into the Transaction. In this respect, I think both parties agree that the "die was cast" with the Roseway Transaction. After April 2010, because the Roseway Transaction required a fixed repayment after a three-year term, rather than participation in divestiture proceeds from the Defined Portfolio as and when received, the fate of the Fund depended critically upon receipt of divestiture proceeds in an amount and within a time frame sufficient to repay the Roseway Obligations.

[331] I have no doubt that the Former Manager sought unsuccessfully to obtain, and would have preferred to be able to recommend, a financing that did not entail a fixed term for repayment. Nevertheless, the fact that the Roseway Transaction was the best available financing option does not make it an appropriate transaction for the Fund as Varghese appears to argue. Nor, did it relieve the Former Manager of its obligations to consider whether a cessation of redemptions was preferable to the financing that was available to the Fund.

[332] I am also satisfied on the evidence that a cessation of redemptions was a viable option for the Fund if it had been implemented prior to the 2010 RRSP season and perhaps even at the time of acceptance of the Roseway Transaction. In this regard, it is relevant that the experts agree that a decision to cease redemptions prior to the commencement of the 2010 RRSP season would have provided more than adequate cash flow to fund the follow-on investments of the Fund that was, instead, provided by the Roseway Transaction and would have avoided any risk of default

by the Fund thereafter. Further, in the absence of discussions with the BCSC at the time, I do not think that it was reasonable to proceed on the basis that the outcome to the Class A shareholders would have been worse than the actual outcome of the Fund.

[333] I therefore have no hesitation in finding that the Roseway Transaction was an inappropriate transaction for the Fund in the sense that, if they were to have the opportunity to reconsider the decision with the benefit of hindsight, the Former Manager and the Board would have recommended that the Fund cease redemptions prior the 2010 RRSP season rather than enter into the Roseway Transaction.

[334] The issue for the Court, however, is whether the Former Manager failed to meet the Standard of Care in recommending that the Fund enter into the Roseway Transaction. Based on the evidence discussed below in particular, I conclude that the Former Manager did breach the Standard of Care in doing so for the following reasons.

[335] First, and most fundamentally, the Roseway Transaction entailed the Fund's assumption of a level of risk that was inappropriate for a retail venture capital fund. The evidence before the Court from both Gekiere and Varghese establishes that debt financing was inappropriate for an LSVCC except perhaps in the circumstances of short-term borrowings to bridge a temporary liquidity deficit. The inability of the Fund to raise additional capital by the sale of Class A Shares made the Fund entirely dependent upon the timely receipt of divestiture proceeds. However, the inherent uncertainty of the timing and amount of divestiture proceeds, even apart from the effect of the 2008 economic crisis, made debt financing unduly risky. The absence of any similar borrowings by any other LSVCC is powerful evidence that the Roseway Transaction involved a greater level of risk than was prudent for an LSVCC. In short, the Roseway Transaction unduly and unrealistically increased the level of risk associated with the Fund.

[336] In this regard, it is important to note that the venture capital investment fund model, whether private or public, is premised on funding by means of equity capital rather than debt because of the inherent riskiness of venture capital investments. As mentioned above, even before the economic crisis of 2008, venture capital funds relied on equity financing because the timing and amount of divestitures of venture capital assets is unpredictable for a myriad of reasons. It therefore does not make economic sense to lever a venture capital portfolio by incurring debt having a fixed repayment term, particularly a relatively short term of three years. Such a financing could only be justified, if at all, in circumstances where there was a very high level of certainty of receipt of cash inflows to the borrower, whether by way of share sales or divestitures, to fund the debt service including repayment. Otherwise, the effect of such leverage would be to materially increase the investment fund risk without increasing the rate of return.

[337] The Fund points to an internal analysis that the Roseway Transaction permitted the Fund to participate in follow-on financing that resulted in the preservation of value totaling approximately $117 million. This is, however, an incomplete analysis for present purposes. There is no reason why such preservation of value could not have been funded by a cessation of redemptions which would have yielded at least as much cash flow as the principal amount of the loan in the Roseway Transaction. This preservation of value cannot therefore be conceived of an incremental profit that would not also have been obtained if the Fund had ceased redemptions in 2009.

[338] Second, as discussed above, the Roseway Transaction was based on projections regarding the realizable value of the Defined Portfolio within the term of the Transaction, and the Fund's liquidity position in the future, that were also unduly, and unjustifiably, optimistic. With respect to the necessary realized values of the Defined Portfolio, there is no evidence that such values were realized within the term of the loan, much less that the Fund achieved the "conservative" increase in value of $47 million or "the most probable" increase of $100 million referred to in the minutes of the April 27, 2010 Board meeting, which was the Former Manager's assessment of the portfolio value. More importantly, there was no evidence in the memoranda prepared for the Board that supported these higher values for the Fund's venture capital portfolio. With respect to the projections for divestitures, even if the Former Manager's confidence in the realizable value of the Fund's venture capital portfolio in a world of healthy and stable markets was justified (which has not been established), the Former Manager assumed a level of divestitures that was not warranted by the market experience in the two prior years and was not justified in terms of any recent sustainable improvements in the market. As mentioned, it also appears to have been contradicted by its own assessment of "probable" versus "possible" divestiture proceeds during the 2011 planning year as set out in its February 2010 memorandum to the IRC.

[339] Third, although Varghese's evidence was intended to support the Former Manager's position, it was premised on the existence of a growth mandate from the Board and a view of the respective responsibilities of the Former Manager and the Board that the Court does not accept. I understand the implication of Varghese's evidence to be that, if these assumptions are removed, he would not have considered the Roseway Transaction to be an appropriate transaction for the Fund as an LSVCC and would not have recommended it to the Board in the spring of 2010. Further, while the Former Manager and Varghese are of the opinion that the rate of interest in the Roseway Transaction was appropriate for a private venture capital transaction, that is not the same as saying that the loan itself was appropriate for a venture capital fund. In short, I read Varghese's evidence as agreeing that the Roseway Transaction entailed too high a level of risk for an LSVCC.

[340] Fourth, I agree with Gekiere that the adoption of the Roseway Transaction, rather than a cessation of redemptions, entailed a real issue of fairness among the Class A shareholders that was not addressed by the Former Manager in its memoranda to the Board. By permitting redemptions to occur in the 2010 RRSP season and the 2011 RRSP season at a NAV that did not reflect the cost of the Roseway Transaction, much less the ultimate consequences of repayment, the Former Manager's actions resulted in an unfairness to shareholders who did not redeem their Class A Shares in 2010 and 2011.

[341] Fifth, as discussed above, the Former Manager's recommendation was based on an unduly restrictive and, in any event, uninformed view of the likely response of the BCSC and other securities regulatory authorities to a cessation of redemptions. The Former Manager proceeded on the basis that the cessation option would severely limit the time period in which the Fund would be permitted by the BCSC to divest the Fund's investments and wind-down the Fund. As discussed above, I consider that it was at least as likely, based on the status of the Fund's venture capital portfolio and the content of the subsequent discussions with the BCSC staff, that the securities regulators would have been more flexible than the Former Manager

portrayed to the Board if the Fund had approached the securities regulatory authorities on a more timely basis. In any event, it is by no means clear that the returns to the Class A shareholders under a cessation of redemptions scenario would necessarily have been less than the returns after implementation of the Roseway Transaction if the latter had been subjected to an analysis based on more realistic cash flow projections.

[342] Based on the foregoing, I conclude that the Former Manager's recommendation of the Roseway Transaction in the spring of 2010, rather than of a cessation of redemptions, also failed to satisfy the Standard of Care.

Was the Former Manager's Breach of the Standard of Care a "Material Breach"?

[343] The Court's conclusion regarding the nature of a "material breach" for the purposes of section 8.2(c) of the Management Agreement has been set out above. For the following reasons, I find that the actions of the Former Manager addressed above collectively constituted a "material breach" of the Standard of Care entitling the Fund to terminate the Management Agreement pursuant to that provision.

[344] In summary, the Former Manager breached the Standard of Care in recommending that the Fund enter into the Roseway Transaction in April 2010, rather than recommending a cessation of redemptions and commencing an orderly wind-down process at or before that time. In doing so, the Former Manager tied the future viability of the Fund to its ability to achieve divestiture proceeds over a limited three-year term sufficient to repay the principal and to pay the substantial amount of interest due under the Roseway Transaction. For the reasons discussed above, by entering into the Roseway Transaction, the Fund assumed an unduly high level of risk that was not warranted for a public investment vehicle of the nature of an LSVCC. Moreover, the recommendation of the Former Manager regarding the Roseway Transaction was based on an estimate of the value of the Fund's venture capital investment portfolio, in particular the Defined Portfolio, that was not justified by recent experience or otherwise. These actions significantly jeopardized the financial viability of the Fund on and from the date of entering into the Roseway Transaction by materially increasing the risk of a liquidity deficit and consequential material loss of value arising on a default under the Roseway Transaction.

[345] For clarity, this finding is not dependent upon, or based upon, the subsequent insolvency of the Fund. In my view, the Former Manager's recommendation of the Roseway Transaction was the culmination of a number of actions described above that collectively constituted a "material breach" for the purposes of section 8.2(c) of the Management Agreement no later than the date of the Roseway Transaction entitling the Fund to terminate the Management Agreement from and after the date of the Roseway Transaction. Further, this was not a default that was capable of being cured nor, in any event, was it cured at any time thereafter.

[346] Accordingly, I find that the Fund was entitled to terminate the Management Agreement pursuant to section 8.2(c) thereof on September 30, 2013 as contemplated by the Termination Letter.

Alleged Breach #2: Failure to Keep Proper Records

[347] The Fund alleges three independent breaches by the Former Manager of its obligations in sections 3.9(a) and 3.11 of the Management Agreement.

[348] First, the Former Manager has acknowledged that it co-mingled the shareholder data pertaining to the Fund with the shareholder data pertaining to the shareholders of the Other Growthworks Funds. It was therefore unable to deliver an electronic shareholder data base accessible to the Fund after termination of the Management Agreement as required by section 8.5 of the Management Agreement. In order to obtain such a data base, the Fund ultimately engaged a third party referred to as "IAS." It appears to be undisputed that the Fund incurred a cost of $85,400 to separate the data.

[349] Second, the Fund says the accounting records were in a poor state. The evidence in support of this allegation pertains principally to certain mistakes uncovered by PWC when it conducted the investigation on behalf of Roseway in 2013 described above. Of these irregularities, the most material pertained to the Fund's accounting of the Fund's investment in Cytochroma.

[350] This matter appears to have arisen as a result of Roseway's decision to invest $176,085 in a follow-on financing of Cytochroma in excess of the amount of Roseway's follow-on investment contemplated by the Participation Agreement. The Fund did not make its own follow-on investment in this Cytochroma financing. The PWC investigation unearthed two problems with this investment.

[351] First, it appears that there was an accounting error pertaining to the treatment of Roseway's 14% interest in the shares received in this financing. This accounting error was corrected with the result that the Comm Fund received 100% of the shares received on the follow-on financing, of which 14% were held for Roseway.

[352] Second, a dispute arose between the Former Manager, on behalf of the Fund, and Roseway regarding the entitlement to certain "Old Warrants" received by the investors in Cytochroma. This dispute is discussed further below. It was resolved by a settlement agreement in 2015 pursuant to which the amount of $1,045,462 was payable by the Fund together with a percentage of certain future payments described below. The Fund asserts that it suffered a loss of $923,947.12 for which the Former Manager is responsible.

[353] In my view, the foregoing matters do not either individually or collectively constitute a material breach of sections 3.9(a) and 3.11 of the Management Agreement entitling the Fund to terminate the Management Agreement pursuant to section 8.2(c). The co-mingling of shareholder data prior to termination of the Former Manager did not jeopardize the continued viability of the Fund. The aggregate amount of the Fund's damage claim, even including the amount in respect of the Cytochroma interest, does not meet the standard of a "material breach" for the purposes of section 8.2(c) of the Management Agreement set out above. In addition, and in any event, for the reasons set out below, the Fund's claim for damages in respect of its Cytochroma interest is dismissed.

[354] In addition, the Fund says that the Former Manager did not provide the books and records of the Fund for over a year after the termination of the Management Agreement despite several demands of the Fund. The Former Manager disputes this characterization of the circumstances pertaining to its delivery of these books and records. However, as this interaction occurred after the termination of the Management Agreement, it cannot, in any event, give rise to a breach thereunder. The related damage claim of the Fund is addressed later in these Reasons.

Alleged Breach #3: Failure to Comply with Securities Legislation

[355] The Fund alleges two separate bases for termination of the Management Agreement pursuant to section 3.4 of the Management Agreement, which required compliance by the Former Manager of all securities laws, regulations and policies.

Breach of the Statutory Duty of Care, Diligence and Skill

[356] Under section 3.4 of the Management Agreement, the Former Manager agreed to comply with all securities laws and regulations, and other requirements of securities regulatory authorities, insofar as they relate to its duties and obligations under the Management Agreement. As described in detail above, after completing its compliance review, the BCSC compliance staff expressed the view that GWC had breached its fiduciary obligations and its duty of care under s. 125 of the *Securities Act (British Columbia)* and its duty of fair dealing under s. 14 of the *Securities Rules*, B.C. Reg. 194/97 and s. 11.1 of *National Instrument 31-103 Registration Requirements, Exemptions and Ongoing Registrant Obligations*.

[357] Based on the finding of a "material breach" under s. 3.5 of the Management Agreement above, I think that it necessarily follows that the Former Manager also breached section 3.4 of the Management Agreement for the same reasons. This conclusion is based on the virtually identical language of s. 125 of the *Securities Act (British Columbia)* and section 3.5 of the Agreement.

[358] However, the Fund argues that the Court should attach a far greater significance to the statements of the BCSC compliance staff in its letters in 2013 to the Former Manager. The Fund argues that the matters identified by the BCSC were "serious" and that neither the Former Manager nor the Court can challenge these findings. Because of the virtually identical language of s. 3.5 of the Management Agreement and s. 125 of the *Securities Act (British Columbia)*, the Fund effectively argues that the Former Manager and the Court are bound by the findings of the BCSC compliance staff in respect not only of this alleged breach, but also in respect of alleged breach #1.

[359] For the following reasons, I do not accept this argument of the Fund and I therefore made no mention of it in the analysis above regarding the Former Manager's breach of s. 3.5 of the Management Agreement.

[360] The statements of the compliance staff of the BCSC do not constitute findings that GWC breached the provisions of the securities legislation referred to above. The matters raised by the compliance staff did not proceed to a regulatory hearing before the BCSC. They are therefore not findings, or admissions, made in a hearing before the BCSC. Nor are they findings, or

admissions, agreed to by GWC in a settlement agreement with the BCSC that might give rise to the argument of abuse of process as in *Ciavarella v. Schwartz*, 2014 ONSC 5061 at paras. 35-36, to which the Fund refers. The statements represent only the views of the compliance staff of the BCSC. Moreover, the issues raised by the compliance staff of the BCSC were resolved by undertakings and conditions that permitted GWC to continue to carry on business and, accordingly, that permitted the Former Manager to continue to act as the manager of the Fund.

[361] In support of its position, the Fund retained Patricia Taylor, a lawyer in private practice who formerly acted as Senior Legal Counsel for the BCSC. In that capacity, among other things, Ms. Taylor advised compliance staff regarding potential regulatory action. Her opinion regarding the significance to be attached to the statements made by the compliance staff is the following:

> ...the matters raised by the BCSC were substantial events requiring the board of the fund to consider the conduct of the Manager relating to the management of the Fund. The events leading to the imposition of the conditions and undertakings were more than minor or technical matters.

[362] I do not find this opinion to be either relevant or helpful. The issue is not whether the matters raised were "more than minor or technical matters," but rather the legal effect of the conclusions of the BCSC compliance staff. This opinion avoids reaching a conclusion on this issue although it purports to address it.

[363] Accordingly, I do not consider the alleged breach of applicable securities legislation to give rise to an independent event of default under section 3.4 of the Management Agreement that entitled the Fund to terminate the Agreement apart from the finding of a material breach of s. 3.5 of the Management Agreement. Nor do I consider that the position of the BCSC compliance staff demonstrates, or establishes, a breach of the Standard of Care that is *res judicata* in this action. Rather, the breach of s. 3.4 of the Management Agreement is a secondary breach that arises solely by virtue of the fact that the Fund succeeded in demonstrating a breach of the Standard of Care under s. 3.5 of the Agreement.

The Capital Deficiency of GWC

[364] The Fund also purports to rely on the breach of securities regulations arising from the failure of GWC to maintain the required minimum capital. As mentioned, the Former Manager acknowledged this failure in its letter to the BCSC dated May 31, 2013.

[365] The failure of GWC to maintain the required level of capital constituted a default under section 12.1 of *National Instrument 31-103 Registration Requirements, Exemptions and Ongoing Registrant Obligations*. However, section 8.2(c) of the Management Agreement provided that a sixty-day cure period existed in respect of a curable default.

[366] In this case, the Termination Letter was sent on September 30, 2013. GWC cured the capital deficiency on October 1, 2013. Accordingly, the Fund cannot rely upon the capital

deficiency of GWC as an event of default that permitted it to terminate the Management Agreement under section 8.2(c) thereof.

Alleged Breach #4: Failure to Pay Normal Operating Expenses of the Fund

[367] As discussed in greater detail below under the heading "Damages Alleged in Respect of the Alleged Breach #4 Regarding Non-Payment of Certain Expenses," the Fund alleges a number of particular instances in which it says the Former Manager failed to pay expenses of the Fund that it was contractually obligated to pay.

[368] Whether these alleged breaches constitute, either individually or collectively, a "material breach" for the purposes of section 8.2(c) of the Management Agreement depends upon the resolution of these claims. Based on the Court's determination that, of these various claims, the Former Manager is only liable to reimburse the Fund for the amount of the KPMG audit expenses, the Proposed VenGrowth Transaction expenses and the Roseway-related management fee reduction, which total only approximately $1.2 million, I find that these claims do not give rise to a "material breach" for the purposes of section 8.2(c) of the Management Agreement.

Analysis and Conclusions Regarding the Former Manager's Damage Claims in Respect of the Termination of the Management Agreement

[369] The Former Manager claims damages on the termination of the Management Agreement that fall into three categories that will be discussed in turn.

Damages for Breach of Contract

[370] The Former Manager claims damages in the amount of $11,541,364 representing the fees to which it says it would have been entitled if the Management Agreement had been terminated under section 8.2(e). This claim proceeds on the basis that, in the absence of a right to terminate the Management Agreement under section 8.2(c), the Fund should be treated as effectively having been terminated under section 8.2(e). Accordingly, the damages claimed represent its calculation of the amount it would have received over the five-year transition period contemplated by that provision.

[371] Given the finding above that the Fund was entitled to terminate the Management Agreement pursuant to section 8.2(c) as a result of a material breach of the Standard of Care, there is no basis for this claim. There is no language in that provision, nor is there any other provision in the Management Agreement, that provides for a payment to the Former Manager of prospective management or administration fees post-termination in the circumstances of a valid termination under section 8.2(c). This claim is therefore dismissed.

Unpaid Capital Retention Fees

[372] The Former Manager claims the amount of $775,603.72 in respect of "unpaid capital retention" fees. These fees are contemplated by section 5.2(b) of the Management Agreement and pertain to commissions paid to third-party investment dealers on the sale of Class A Shares. The Management Agreement contemplated that the Former Manager would pay all commissions

payable to investment dealers in respect of such sales and that it would, in turn, be repaid by the Fund in equal installments over eight years. The amount claimed represents the aggregate of the amounts to be repaid in respect of Class A Shares sold less than eight years prior to the commencement of the CCAA proceedings.

[373] While the amounts being repaid are included in the administration fees payable under section 5.2 of the Management Agreement, these arrangements amount, in substance, to an interest-free loan by the Former Manager to the Fund repayable in equal installments over eight years. As such, in the absence of language in the Management Agreement that specifically provides otherwise, I see no reason why this amount should not be repayable by the Fund notwithstanding termination of the Management Agreement pursuant to section 8.6(a) thereof.

[374] In this regard, I note that this claim differs from the NAV-based management and administration fees in sections 5.1 and 5.2(a) in an important respect. In the normal course, a fee for future management or administration services would not be payable to a departing manager as it would duplicate the fee to be paid to the incoming manager. Such duplication would not arise, however, in respect of the "unpaid capital retention fees." The only issue would be the risk of an overpayment as a result of future redemptions before the expiry of the eight-year period. This is not, however, a realistic concern in the present circumstances after the commencement of the CCAA proceedings.

[375] I also note that section 8.6(a) refers to any unpaid Administration Fees, as contrasted with any reimbursable expenses accrued to the date of termination. On this basis, I do not think that the Former Manager's claim is limited to the amount of fees that are accrued as of the date of termination or are payable pursuant to section 5.2(b) in the year of termination of the Management Agreement.

[376] Based on the foregoing, I conclude that the Former Manager has a valid claim for reimbursement of the full amount of this claim.

Unpaid Incentive Payment Amounts

[377] Section 4.2(d)(i) of the share conditions of the IPA Shares provides for the payment of IPA Dividends as follows:

> The holder of the IPA Shares shall be entitled to receive, the directors shall declare where permitted by the Act and the Corporation shall pay, cumulative dividends on the IPA Shares payable as of the end of each fiscal quarter, on the following terms and conditions
>
> (i) the dividends shall be equal to:
>
> A. 20% of the Realized Gains and Income on each New Venture Investment; and

> B. 15% of the Realized Gains and Income on each Existing Venture Investment; …

[378] Section 4.2(f) of the share conditions provides for a payment of IPA Dividends on termination of the Former Manager as the manager of the Fund:

> Upon termination of the holder of the IPA Shares as a manager of the Corporation, the holder of the IPA Shares shall be entitled to receive an amount equal to the sum of:
>
> (i) all declared but unpaid dividends on the IPA Shares, and
>
> (ii) dividends in an amount equal to the cumulative dividends to which the holder of the IPA Shares would have been entitled pursuant to paragraph (d) above, whether or not dividends were actually declared by the directors, assuming that all Venture Investments had been disposed of as of the effective date of such termination at the estimated fair value of such investments calculated in accordance with the Corporation's usual valuation policies….

[379] The Former Manager claims that it is entitled pursuant to section 4.2(f)(ii) to payment of dividends on the IPA Shares equal to the total of realized gains and income from four venture capital investments that were divested prior to termination of the Management Agreement. The total amount claimed is $672,390.61.

[380] In support of its position that it is entitled to the earned, undeclared and unpaid dividends, the Former Manager relies on: (1) the language of section 4.2(f)(ii); and (2) the Fund's treatment of earned, undeclared and unpaid dividends in its financial statements.

[381] The Fund does not dispute that this amount was earned in the sense that the Former Manager is entitled to receive dividends in such amount pursuant to the provisions of section 4.2(d)(i) of the share conditions of the IPA Shares, subject to compliance with the terms of that provision. However, it submits that the Former Manager is not entitled to be paid such amount in the absence of a Board resolution declaring a dividend in such amounts on the IPA Shares, which the Board is prevented from passing in view of the solvency provisions of section 42 of the CBCA.

[382] In my view, the language of section 4.2(f)(ii) does not support the Former Manager's position that it is entitled to payment of the amount claimed by way of an IPA Dividend on the IPA Shares in the present circumstances for the following reasons.

[383] The Former Manager relies on the words "whether or not dividends were actually declared by the directors" in section 4.2(f)(ii). If section 4.2(f)(ii) provided that the Former

Manager was entitled to receive the amount contemplated thereby otherwise than as "dividends," the result might well be different. However, section 4.2(f)(ii) is quite explicit. It provides that the Former Manager is entitled to "dividends in an amount equal to the cumulative dividends *to which [the Former Manager] would have been entitled pursuant to paragraph (d)* above..." (emphasis added). Section 4.2(d)(i) provides, among other things, that "the directors shall declare *where permitted by the Act* and the [Fund] shall pay" the earned amounts (emphasis added). This language requires the Fund to make any amount owing pursuant to section 4.2(f)(ii) payable by way of a dividend. It also makes the Board's obligation to declare the contemplated dividend dependent upon the CBCA and, in particular, satisfaction of the solvency provisions in section 42 of that statute.

[384] As the share provisions are clear that the earned amounts are to be paid to the Former Manager in the form of dividends, and, in any event, as it is not disputed that, in the present circumstances, the directors could not satisfy section 42 of the CBCA if they were to declare a dividend in respect of such amounts, the Board has no obligation to declare such dividend and the Fund therefore has no obligation to pay any amount to which the Former Manager is otherwise entitled pursuant to section 4.2(f)(ii). In short, there is no amount to which the Former Manager would have been entitled pursuant to section 4.2(d)(i) of the share conditions of the IPA Shares.

[385] In addition, I do not find the financial statement treatment of these earned amounts as probative of the legal issue in this proceeding for three reasons.

[386] First, the financial statement treatment of these amounts as a liability in years prior to 2013 is undoubtedly correct in the context of a going-concern entity. Regardless of any legal issue surrounding the need for a declaration of a dividend, these amounts were required to comply with the business arrangements between the Fund and the Former Manager.

[387] Second, the concept of a liability for accounting purposes is broader than the concept of a legally enforceable obligation at law. In fact, the accrual of a contingent liability in respect of the IPA Shares demonstrates this reality. There is, therefore, no necessary inference of a legally enforceable obligation to be derived from the accounting treatment of this claim in the financial statements of the Fund.

[388] Third, there is no evidence of any issue of compliance with the CBCA solvency test that was raised in respect of such earned amounts at the time of finalization of the financial statements. Further, and in any event, there is no evidence that the legal issue presented by this action was addressed in the preparation of the financial statements.

[389] I also note that Mesbur J. reached a similar conclusion on similar language in another case also involving the Former Manager reported at 2017 ONSC 5009, which is currently under appeal. While I agree with the reasoning in that case, I have not relied specifically on that decision in reaching the conclusion expressed herein.

[390] Based on the foregoing, I conclude that the Former Manager is not entitled to its claim for the amount of accrued IPA Dividends in the amount of $672,390.61.

Unpaid Fees and Financing Fees for September, 2013

[391] The Former Manager also claims unpaid management and administration fees in the amount of $352,668. This amount represents the Former Manager's fees for the period of September 2013 calculated in accordance with the Management Agreement.

[392] The Fund has not disputed the Former Manager's claim for this amount. The Former Manager is therefore entitled to the amount of this claim. I note, however, that payment of this amount is subject to the provisions of the document dated August 14, 2013 entitled "Direction to Pay" regarding the Former Manager's obligation to pay the audit fees of KPMG in respect of the audit for the Fund's fiscal year ending August 31, 2013.

Claims of the Former Manager for Transition Services

[393] The Former Manager makes the following five claims for services that it provided, or contracted for, after the date of termination of the Management Agreement that were not contemplated in the CTSA (collectively, the "Transition Services"). The Fund did not appoint a successor manager for the Fund. The Monitor in these CCAA proceedings has neither provided, nor proposed providing, the services at issue. Even if not directly applicable in the absence of a successor manager, the provisions of section 8.6 of the Management Agreement are also relevant. Section 8.6(b) provides that, if the Agreement was terminated pursuant to section 8.2, the Fund would pay the Former Manager "all reasonable transfer, wind down and transition costs incurred by ... the Manager as a result of having to transition operations to a successor manager." I will address each claim in turn.

Concentra

[394] Concentra is the group RRSP trustee for all of the funds managed by the Former Manager. RRSP accounts must be held by a licensed RRSP trustee in order for RRSP tax benefits to accrue to a shareholder of the Fund. As the Former Manager was not a licensed RRSP trustee, it retained Concentra to provide this service.

[395] The Former Manager advised that the cost of processing tax forms on the transfer of Class A shares from RRSPs to RIFs by shareholders who turn 71 would be would be $7,000 for 2013. A year later, it advised that the cost for 2014 would be $63,000. On December 4, 2014, the Fund notified the Former Manager that it would not cover the fees for Concentra. However, the Former Manager continued to engage Concentra until March 31, 2016.

[396] The Former Manager claims $94,781.29 according to the Monitor's Eighteenth Report dated January 26, 2017 (the "Eighteenth Report"), although at trial the Monitor suggested that the amount was now $184,664.75 based on an allocation of the Concentra fees among the Fund and the other GrowthWorks Funds according to the number of shareholders of the funds.

[397] The evidence establishes that it was necessary for the Fund to engage a group RRSP trustee to avoid adverse tax consequences for a material number of its shareholders, not merely for the preparation of tax-related materials for the transfer of Class A Shares from RRSPs to RIFs. While Ross said that the Fund was engaging a third party to provide the tax-related

services for 2014, there is no evidence that the Fund actually finalized an agreement with an alternative trustee to act as the group RRSP trustee nor is there evidence that the Fund engaged a third party service provider to process the tax-related forms during the period for which Concentra provided services. Nor has the Fund demonstrated that the fees associated with Concentra are higher than any alternative trustee that it proposed to engage. On this basis, it is reasonable for the Fund to pay these fees on the *quantum meruit* principle.

[398] The Fund argues that, since the Former Manager has not paid Concentra any of the amounts it seeks in this action, it has not demonstrated a loss. I do not agree. The evidence establishes that Concentra has invoiced the Former Manager a total of $230,377.86 for its fees from October 1, 2013 to March 31, 2014. As such, the Former Manager has incurred a liability or expense for which it is entitled to be reimbursed.

[399] On the other hand, while it is not clear how the Former Manager's claim for $94,781.29 was arrived at, I am not persuaded that an allocation based on the number of shareholders of the Fund is appropriate. The cost of continuing to act as a bare trustee of RRSP accounts would appear to be essentially independent of the number of shareholders. Further, the cost of processing any tax-related materials for the Fund's shareholders would be considerably less for the Fund after sales and redemptions ceased than it would be for the Other GrowthWorks Funds that have remained active.

[400] Accordingly, I find that the Former Manager is entitled to its claim of $94,781.29 for reimbursement of the amount owing to Concentra for services provided by that corporation.

Just Systems

[401] The Former Manager claims $67,259.51, according to the Eighteenth Report, for fees payable to Just Systems for the use of software that permitted the Fund, and the Former Manager, to access the Fund shareholder database. The total fees invoiced by Just Systems to the Fund and the Other GrowthWorks Funds during the relevant period, being January 1, 2014 to September 30, 2014 was $118,500. The Fund has paid $27,550.49 plus taxes, representing its share on an "assets under administration" basis. The Former Manager says the appropriate allocation basis should be the number of shareholders. It therefore claims an additional $67,259.51 as the difference calculated on this latter basis.

[402] The Fund does not dispute that it used the software during the relevant period and therefore is obligated to pay the cost thereof that is attributable to services in respect of the Class A shareholders of the Fund. However, the Former Manager co-mingled the data of the shareholders of all of the funds that it managed with the result that the fees charged to the Former Manager for the use of this software by all of the funds managed by it must be allocated to the Fund on some basis.

[403] The Fund believes that the total fees payable to Just Systems should be allocated based on the assets under management of the Fund relative to total assets under management of the Former Manager. It says this is consistent with the Former Manager's proposal with respect to the Just Systems' fees provided to the Fund on November 27, 2013 and approved by the Fund. The Former Manager says that it mistakenly contemplated an "assets under administration"

allocation basis in its proposal. It advised the Fund in 2014 that it considered that the fees ought to be allocated instead on the basis of the relative number of shareholders of each fund.

[404] The Former Manager's 2013 proposal contemplated the allocation of fees on an "assets under administration" basis. Whether this claim is conceived of as a continuation of the agreement formed when the Fund accepted and acted upon the Former Manager's proposal or as a claim for reimbursement of reasonable expenses on a *quantum meruit* basis, the evidence does not establish a compelling basis for departing from the "assets under administration" principle. In particular, as with the Concerta claim, I am also not satisfied that the relative use of the software is best represented by the number of shareholders of a fund for which there are no sales or redemptions. Accordingly, the Former Manager is only entitled to be paid an amount equal to the Just Systems' fees allocated as between the Fund and the Other GrowthWorks Funds on the basis of "assets under administration".

[405] The Former Manager's claim is therefore dismissed.

FundSERV

[406] FundSERV licensed software to the Former Manager that permitted individual brokers to connect to the shareholder database to make changes to a shareholder's account, including in particular making redemption requests, without having to involve the Former Manager. At the Fund's request, the Former Manager terminated this service in March 2014. The Former Manager seeks reimbursement of the FundSERV fees for the period from September 30, 2013 to March 2014 on a *quantum meruit* basis. The amount of this claim is $34,627.

[407] The Fund says that it did not require this service after the commencement of the CCAA proceedings as there were neither share transfers nor redemptions after that date. The Fund also says that it did not direct the Former Manager to incur this cost.

[408] The evidence establishes that the Fund did not require this service during the period from September 30, 2013 to March 2014, when the service was terminated, as neither redemptions nor transfers could occur after the commencement of the CCAA proceedings, other than transfers from RRSPs to RIFs. The limited amount of account servicing required in respect of changes to shareholder information could have been done manually at a reduced cost and was, in fact, so managed later. This should have been well-known to the Former Manager at the time of commencement of the CCAA proceedings. Insofar as this resulted in an increase in telephone calls to the Former Manager's call centre, the cost is being reimbursed pursuant to a separate claim addressed below.

[409] Based on the foregoing considerations, I conclude that the Former Manager's claim for reimbursement of FundSERV fees to March 2014 should be dismissed.

Accounting Services

[410] Under the CTSA, the Fund agreed to pay for the Former Manager's accounting services. Section 3 of the CTSA provided that payment for the costs of such services:

> ...will be calculated as the sum of the time expected to be spent by each employee performing Critical Transitional Services at an hourly rate equal to the actual annual salary of the individual employee, plus benefits <u>and other employment costs related to that person</u>, divided by 1840 working hours per year. [Emphasis added].

[411] The Former Manager submits that "other employment costs related to that person" includes its overhead including rent. Accordingly, in addition to the direct employment costs of $91,698.36 billed to the Fund, the Former Manager applied a further charge of 60% of this amount on account of such "other employment costs".

[412] This issue raises an issue of contractual interpretation of the relevant provision of the CTSA. I think it is clear that "other employment costs related to that person" must relate to other costs directly pertaining to the employment of an individual directly involved in providing accounting services. As such, it excludes the costs of persons who provide support services included in overhead but who do not directly provide accounting services to the Fund.

[413] In this regard, it is significant that the provision speaks to "other employment costs" rather than to "other costs" and it addresses only costs "related to that person" rather than costs related to other persons whose employment indirectly bears on the provision of the services provided under section 3 of the CTSA. Moreover, the term "other employment costs" does not extend to other non-employment costs that are typically included in overhead costs, such as leasehold costs, software licence fees, telecommunications costs, etc. as these cannot be characterized as "employment costs related to that person" regardless of who that person is. This suggests that "other employment costs" was not intended to apply to overhead as that term is generally used. As a related matter, the language also does not support the application of a 60% factor to determine such "other employment costs". The language requires identification of the actual costs of an individual.

[414] Based on the foregoing, I conclude this claim should be dismissed.

Customer Support Services

[415] The Former Manager claims $94,630.96 for the provision of customer support services for the period from October 1, 2013 to February 28, 2014 when it stopped providing these services. These costs appear to relate primarily to a call-centre maintained by the Former Manager for all of the funds that it manages.

[416] The Fund says an agreement to provide these services was negotiated between the parties but it was never signed. It says there was no agreement for the provision of these services, no direction from the Fund to provide these services, and no reference to them in the CTSA.

[417] However, the Fund required a third-party provider to provide information to its shareholders after the commencement of the CCAA. A monitor often provides such services. Nevertheless, in this case, it does not appear that the Fund engaged the Monitor to provide such

services. In any event, there is also no evidence that the Monitor could have provided these services at a lower cost than the costs charged by the Former Manager.

[418] Based on the foregoing, I conclude that the Former Manager is entitled to be reimbursed for the direct employment costs of providing these services on a *quantum meruit* basis.

[419] It is understood that the total amount charged to the Fund and the Other GrowthWorks Funds for the relevant period is $138,040.91. There is a dispute as to whether these costs should be allocated on the basis of the number of shareholders or on an "assets under administration" basis.

[420] I conclude that the Former Manager's costs of providing this service should be allocated between the Fund and the Other GrowthWorks Funds on an "assets under administration" basis, rather than on the basis of the number of shareholders as the Former Manager submits. As mentioned, the extent and nature of shareholder queries regarding a solvent and an insolvent fund are likely to be quite different such that there is no clear basis for concluding that allocation on the basis of the number of shareholders would be more appropriate than an allocation on the basis of the "assets under administration".

[421] The Former Manager also included an overhead charge equal to 60% of the direct employee costs in its claim. In principle, the Former Manager should be entitled to a charge for overhead. However, I agree with the Fund that the 60% figure applied by the Former Manager is not defensible, given that it represents an allocation of employee costs at a single point in time in October 2013, which therefore disregards the acknowledged wind-down of operations after that date. In the absence of evidence that establishes the actual overhead costs over the relevant period and therefore permits a reasonable markup that reflects these costs, I conclude that the Former Manager has failed to establish the amount of the compensable costs for overhead.

<u>Analysis and Conclusions Regarding the Fund's Damage Claims</u>

[422] The Fund asserts claims for damages arising from each of the four breaches of the Management Agreement alleged against the Former Manager that were discussed above. I will address each in turn.

<u>Damages Alleged in Respect of the Breach of the Standard of Care</u>

[423] The Fund seeks damages totalling $28,640,000 for breach of the Standard of Care. This comprises the following:

(1) $17.1 million of interest costs in respect of the Roseway Transaction;

(2) $5 million of default interest payable in respect of the Roseway Transaction;

(3) $1.32 million of interest costs payable in respect of the WOF Loan;

(4) $720,000 of interest costs payable in respect of the Matrix Loan; and

(5) $4.5 million on account of legal, financial advisory and accounting expenses alleged to arise by virtue of the Former Manager's breach.

[424] There are two issues regarding this claim, which will be addressed in turn: (1) an assertion of the Former Manager that this claim is barred by the *Limitations Act, 2002*, S.O. 2002, c. 24, Sched. B; and (2) the principles on which this claim is based. In this latter regard, the claim for $4.5 million is an omnibus claim for expenses incurred in respect of each of the four alleged breaches of the Management Agreement that will be addressed later.

Limitation Period Defence

[425] The Former Manager commenced this action by a Statement of Claim, pursuant to the claims procedure order in the CCAA proceedings, that was filed and served on or about March 5, 2014. The Fund issued and served its Statement of Defence and Counterclaim on or about February 25, 2015. The Former Manager submits that, insofar as the Counterclaim asserts damages for breach of the Former Manager's obligations pursuant to the Standard of Care, the Counterclaim set out therein is statute-barred by virtue of the provisions of s. 4 of the *Limitations Act*, which provides for a two-year limitation period from the date of discovery of a claim.

[426] The Former Manager says that, given the nature of the Fund's claim for breach of the Standard of Care, the Fund knew or ought to have known that it had a claim regarding the Former Manager's alleged breaches of the Management Agreement much earlier, perhaps as early as 2009. The Fund submits that it did not discover the claim for breach of the Standard of Care until mid-2013. It says that it could not have been aware of the facts upon which it bases its claim until that time.

[427] The Fund's position is expressed in paragraph 53 of the Statement of Defense and Counterclaim as follows:

> 53. Despite the significant Management Fees paid by the Fund to the Former Manager, the Former Manager failed to adhere to the Standard of Care required under the Management Agreement, including its obligation to exercise reasonable care and diligence in performing its duties under the Management Agreement. This became apparent to the Fund midway through 2013 as a result of two significant developments: the Fund's attempts to restructure its arrangements with Roseway and avoid defaulting on the Roseway Obligations; and an investigation by securities regulators into the affairs of the Former Manager and its subsidiary, GWC.
> ...

[428] In addition, the Fund argues that the assertion of its claim would have been premature prior to termination of the Former Manager. In particular, it says that the Fund could not reasonably have known of its claim prior to 2013 while the Fund was still performing well and was liquid. In addition, it says that the Former Manager was continuing to present potential solutions to the Fund's liquidity problems until the commencement of these legal proceedings and that the Fund reasonably relied on this activity as a potential solution to such problems. The

Fund analogizes this situation to the circumstances in *Brown v. Braun*, 2016 ONCA 325, 84 C.P.C. (7th) 231, in which, at paragraph 18, the Court of Appeal concluded that it was not legally appropriate for a claim to be discoverable while the medical treatment at issue in that case was continuing.

[429] I have reached the conclusion, for the reasons set out above, that the Former Manager failed to meet the Standard of Care in 2009 and 2010 and, in particular, in recommending the Roseway Transaction in 2010. The issue is when these actions became discoverable.

[430] Section 5 of the *Limitations Act* provides as follows:

> (1) A claim is discovered on the earlier of,
>
> (a) the day on which the person with the claim first knew,
>
> > (i) that the injury, loss or damage had occurred,
> >
> > (ii) that the injury, loss or damage was caused by or contributed to by an act or omission,
> >
> > (iii) that the act or omission was that of the person against whom the claim is made, and
> >
> > (iv) that, having regard to the nature of the injury, loss or damage, a proceeding would be an appropriate means to seek to remedy it; and
>
> (b) the day on which a reasonable person with the abilities and in the circumstances of the person with the claim first ought to have known of the matters referred to in clause (a).

[431] In this case, the losses or damages claimed are the costs incurred by the Fund in respect of the Roseway Transaction principally and, secondarily, of the WOF Loan and the Matrix Loan.

[432] The issue of discoverability pertains to discovery of the facts upon which a claim is based or asserted. In this case, the relevant facts were fully known to the Board by November 2011.

[433] As mentioned above, in a memorandum prepared for the April 27, 2010 Board meeting, the Former Manager stated that "the [Fund] has a plan in place whereby net positive cash flows from the venture capital portfolio will be more than sufficient to meet the Fund's redemption obligations, allowing the Fund to sustain its critical mass over the long-run." The Roseway Transaction was presented by the Former Manager as insurance that would ensure that this plan would be realized. Accordingly, the premise of the Roseway Transaction was that it represented "insurance" to the Fund against potential liquidity problems that would require the Fund to cease redemptions, among other things. On the basis of the Former Manager's projections, the Roseway Transaction would permit the Fund to carry on making redemptions in the ordinary course while, at the same time, making the necessary follow-on investments to achieve value-maximizing divestitures. The WOF Loan was intended to serve a similar purpose.

[434] However, by November 2011, it was abundantly clear that this plan had failed and that the survival of the Fund required a cessation of redemptions. Accordingly, the Fund was in possession of all of the facts necessary to assert the claim of breach of the Standard of Care that is now being asserted no later than November 2011 when the Board resolved to cease redemptions. By that time, it was obvious that the Fund should have been advised to suspend redemptions, or to adopt other cash conserving measures before the commencement of the 2010 RRSP season, rather than to enter into the Roseway Transaction and subsequently the WOF Loan. In addition, it was also obvious that the Former Manager's projections for divestitures and sales of Class A Shares, including the potential value from the Defined Portfolio, upon which the decisions to enter into the Roseway Transaction had been based, were unduly optimistic. Moreover, if there remained any doubt regarding the Board's knowledge of facts establishing its claim for breach of the Standard of Care, the Matrix Loan made the Fund's claim abundantly clear. By the time of this transaction, the circumstances set in motion by the Roseway Transaction required a third loan notwithstanding that redemptions had ceased six months earlier.

[435] I would add that the Newbury Transaction provided further evidence of the basis for the Fund's claim in this action. Each of the Roseway Transaction and the WOF Loan were intended to bridge any liquidity deficits in order to permit the Fund not only to maintain redemptions but also, as mentioned, to fund necessary follow-on investments of its venture capital portfolio companies and thereby ensure an orderly divestiture process that maximized disposition proceeds. The Matrix Loan was required to fund follow-on financings and the interest payable to Roseway notwithstanding, as mentioned, the suspension of redemptions. The Newbury Transaction involved a premature disposition of a number of the Fund's venture capital investments at a significant discount to the Fund's carrying value for those investments at a time when redemptions had already ceased. In short, the need for the Newbury Transaction in order to avoid a further default under the Roseway Transaction, and to repay the WOF Loan, amply demonstrated not only that these transactions had failed to achieve their intended purposes but also that the Fund should, instead, have ceased redemptions, or adopted other cash considering measures, at a much earlier date.

[436] Given the foregoing, I do not see any force to the analogy with the decision in *Brown v. Braun*. This is not a situation in which the Former Manager was in a position to rectify an error acknowledged by the parties. The Fund had incurred liabilities that were irreversible. The only "remedy" was adoption of a completely different strategy that should have been adopted in lieu of the Roseway Transaction.

[437] I also do not accept that the Fund did not discover the cause of action until it received the BCSC letters, or attempted to restructure the Roseway Transaction, in 2013. Discoverability pertains to knowledge of the facts giving rise to a cause of action, not to the receipt of opinions from third parties that the actions of a party may not have met a standard of care. In taking this position, the Board is disregarding its own responsibilities in accepting the recommendations of the Former Manager.

[438] Based on the foregoing, I therefore find that the Fund's counterclaim for damages arising as a result of breach of the Standard of Care is statute barred pursuant to s. 2 of *the Limitations Act*.

The Quantification of Damages

[439] Given the foregoing conclusion, it is unnecessary to address the Fund's damage claim and I therefore decline to address this issue.

Damages Alleged in Respect of the Alleged Breach #2 Regarding the Failure to Keep Proper Books and Records

[440] The Fund asserts two principal claims for damages in respect of this alleged breach by the Former Manager.

The Data Base Claim

[441] The Fund claims $85,400 that it says was incurred to separate the co-mingled shareholder data. As mentioned above, the Former Manager has acknowledged that it co-mingled the shareholder data pertaining to the Fund with the shareholder data pertaining to the shareholders of the Other GrowthWorks Funds. Accordingly, it was unable to deliver an electronic shareholder data base accessible to the Fund after termination of the Management Agreement as required by section 8.5 of the Management Agreement.

[442] It appears to be undisputed that the Fund incurred a cost of $85,400 to engage a third party, IAS, to separate the data, although it is not possible to isolate this work from the IAS invoices in evidence in this action. Accordingly, this amount is payable by the Former Manager to the Fund as damages for breach of section 8.5.

Cytochroma Claim

[443] The Fund claims $923,947.12 as damages in respect of the dispute regarding the entitlement to the "Old Warrants" received by investors in Cytochroma as described above. The Former Manager took the position that the Fund owned these securities and that they formed part of the Defined Portfolio in the Roseway Transaction. Roseway took the position that it received the securities on a Cytochroma follow-on financing in early 2012 in which the Fund did not participate. The Fund's claim represents the value of 86% of the shares of Cytochroma's parent, valued as of the date of their sale, plus 10% of additional sales proceeds payable to Roseway referred to as "milestone payments," representing the difference between the amount stipulated in the settlement agreement referred to above and 14%.

[444] The Fund says these amounts were received by Roseway as the result of the mistaken execution of a document described as an "Acknowledgement and Receipt" (the "Acknowledgment") by a representative of the Former Manager, Joseph Regan. The Fund says the effect of the Acknowledgement was to give Roseway an entitlement to 100% of the proceeds of the sale of the shares into which the Old Warrants were converted on the sale of the Fund's Cytochroma interest, rather than 14% as agreed pursuant to the Participation Agreement.

[445] The Acknowledgment states that "the securities acquired by [the Fund] under the Cytochroma Financing will be owned directly by [the Fund] and form part of the Roseway Portfolio and Roseway shall be entitled to 100% of the Divestment Proceeds from such

securities." For this purpose, "Roseway Portfolio" does not appear to be defined while "Divestment Proceeds," which is defined in the Participation Agreement, means the proceeds received by the Fund from a "Defined Portfolio Company."

[446] The issue between the Fund and Roseway was whether the Old Warrants were "securities acquired by [the Fund] under the Cytochroma Financing," which is defined as "a financing on or around March 26, 2012." As mentioned above, the issue was resolved in a settlement agreement dated May 22, 2015. Pursuant to this agreement, the Fund agreed to pay Roseway $1,045,462 together with the milestone payments referred to above.

[447] While it is quite possible that Regan should not have executed the Acknowledgement, it is not clear that Roseway's position was solely attributable to this document. On its face at least, I do not think that the language in the Acknowledgment is dispositive of the issue. More significantly, the dispute between the Fund and Roseway was never litigated. Instead, the Fund chose to enter into the settlement agreement to resolve this issue and certain other issues between the Fund and Roseway. Therefore, the legal issue of the entitlement to the Old Warrants, and of the alleged negligence of Joseph Regan in executing the Acknowledgement, was never judicially determined. To be clear, the evidence before the Court in this action is not sufficient to establish that Regan was negligent in executing the Acknowledgment.

[448] In these circumstances, the Fund cannot demonstrate that the amounts claimed represent a loss caused by the alleged negligence of the Former Manager either in the form of its record keeping in respect of the Cytochroma investment or as a result of the execution of the Acknowledgement. Accordingly, the Fund's claim for damages in respect of the Cytochroma interest is denied.

Damages Alleged in Respect of the Alleged Breach #3 Regarding the Failure to Comply With Securities Legislation

[449] As noted above, the Fund has asserted two separate breaches by the Former Manager of section 3.4 of the Management Agreement. It also asserts two separate claims in respect of legal fees that it says were incurred in engaging counsel to advise the Fund with respect to each alleged breach.

[450] Specifically, the Fund seeks reimbursement of legal expenses that it says were incurred in connection with the Former Manager's response to the matters raised in the letters of the BCSC compliance staff in 2013 described above. In addition, the Fund seeks reimbursement of its legal expenses incurred in respect of GWC's failure to satisfy the capital adequacy rules under applicable securities legislation in 2013.

[451] In each case, these expenses are attributable entirely to the actions of the Former Manager. The expenses pertain to the Former Manager's obligation under section 3.4 of the Management Agreement to comply with applicable securities legislation, in this case legislation pertaining to its continued registration thereunder. In my view, these expenses constitute expenses that fall under section 6.1 of the Management Agreement for the following reason.

[452] Section 6.1 provides that the Former Manager shall pay all normal operating expenses of the Fund incurred in providing the Services. The Services include, by virtue of section 3.1(c), ensuring compliance in all material respects with securities laws, regulations and policies relating to the operation of the Fund. The legal expenses involved were incurred in addressing issues related to the Former Manager's continued registration under applicable securities legislation which was a condition of the Fund's own compliance with applicable securities legislation. The fact that GWC's registration was not revoked as a result of the BCSC compliance investigation or that it was able to cure its capital deficiency did not exclude a valid concern on the part of the Fund for GWC's status or the need for legal advice regarding that status and its potential impact on the Fund.

[453] In respect of the expenses pertaining to the capital deficiency, I think that they are also payable by the Former Manager by way of indemnification pursuant to section 9.7 of the Management Agreement by virtue of the Former Manager's default under section 3.4 of that Agreement.

[454] Accordingly, I conclude that, in principle, these legal expenses are payable by the Former Manager. I have dealt with the Fund's claim for reimbursement of these expenses as part of the omnibus claim of $2.5 million addressed below.

Damages Alleged in Respect of the Alleged Breach #4 Regarding Non-Payment of Certain Expenses

[455] The Fund alleges a number of instances in which it says the Former Manager failed to pay expenses of the Fund that it was contractually obligated to pay. I will address each allegation after first setting out the relevant provisions of the Management Agreement.

[456] Pursuant to section 6.1 of the Management Agreement, the Former Manager was responsible for paying the normal operating expenses of the Fund as follows:

> 6.1 The Manager shall pay all normal operating expenses of the Fund incurred in providing the Services, including without limitation:
>
> ...
>
> (b) audit and legal fees;
>
> (c) insurance premiums for directors and officers liability, errors and omissions and comprehensive business insurance equal to the current aggregate annual amount of insurance coverage carried by the Fund for the most recently completed financial year prior to the date of this Agreement or such higher amount as is reasonably required by the Fund (or such other coverage as is approved by the Board and the Manager from time to time); ...

[457] Conversely, the Fund was responsible for paying any "unusual or extraordinary expenses," as set out in section 6.2 of the Management Agreement:

> 6.2 Notwithstanding Section 6.1, the Fund shall be responsible for any expenses or charges incurred in respect of the following:
>
> ...
>
> (b) the auditor's fees incurred in connection with more frequent audit of matters other than the annual audit;
>
> ...
>
> (e) any unusual or extraordinary expenses incurred by the Fund outside the normal scope of the Services such as, for illustrative purposes: expenses incurred as a result of litigation or arbitration involving the Fund, the previous manager of the Fund or the current or former portfolio companies, payments by the Fund to third parties pursuant to indemnity provisions between the Fund and such third parties under agreements entered into prior to the Effective Date, or interest in other than very short term borrowings to fund redemption of Class A Shares.

Auditing Expenses for the 2013 Fiscal Year

[458] The Fund says it is owed $350,696.83 in respect of auditing expenses for the 2013 fiscal year that ended on August 31, 2013. This claim pertains to an invoice of KPMG for services provided in respect of the audit before the date of termination of the Former Manager. The Former Manager is otherwise obligated to pay these fees pursuant to section 6.1(b) of the Management Agreement. However, the Former Manager resists this claim on the basis that the KPMG invoice was not rendered until after the date of termination. I do not accept the Former Manager's position for the following reasons.

[459] First, these audit services were rendered prior to the termination of the Management Agreement. As such, the obligation to pay these fees accrued prior to such termination. The date of delivery of the KPMG invoices is of no relevance for the determination of the Former Manager's liability to pay such fees under section 6.1(b) in the absence of any express wording in that provision supporting the Former Manager's position.

[460] Further, as mentioned above, the Former Manager is entitled to receive its management and administration fees to the date of termination of the Management Agreement. In return for the receipt of such fees, the Former Manager agreed in section 6.1(b) of the Management Agreement to be responsible for the ordinary course audit fees of the Funds. Given this agreement, I see no reason why audit fees that were incurred in the period for which the Former Manager is receiving its management fees as addressed above should not payable by the Former Manager.

[461] Finally, any issue regarding these fees is also foreclosed by the fact that the KPMG invoice would have been rendered earlier but for discussions between the Former Manager and KPMG regarding a payment schedule to accommodate the Former Manager's cash flow position.

[462] Accordingly, I find that the Former Manager is obligated to reimburse the Fund for the amount of the KPMG audit fees in respect of the Fund's fiscal period ending August 31, 2013.

Roseway Reduction

[463] As mentioned, pursuant to the defined portfolio services agreement with Roseway described above, the Former Manager agreed to provide services to Roseway in relation to the Defined Portfolio for an annual fee of $100,000. The Former Manager also agreed with the Fund to a corresponding reduction to the management fees payable by the Fund. This reduction was applied in 2010. The Former Manager also provided the stipulated services to Roseway in 2011, 2012 and 2013 but was not paid by Roseway in those years. The Former Manager did not apply the fee reduction in any of these years. It takes the position that the reduction of the Fund's management fees does not apply in the circumstances of non-payment by Roseway of its fees.

[464] This matter raises a simple contractual issue between the Former Manager and the Fund. It does not engage the issue of the application of sections 6.1 and 6.2 of the Management Agreement. It is my understanding that no limitation period issue is asserted by the Former Manager in respect of this claim.

[465] There is no merit to the Former Manager's position. There were two separate agreements – one between the Former Manager and Roseway and another between the Former Manager and the Fund. There is no suggestion that the Former Manager tied them together when the Roseway Transaction was entered into. Moreover, given the inherent conflict of interest that was addressed in these arrangements, it would not have been appropriate to tie them together. Most significantly, the Fund is not in a position to pursue Roseway for the amounts payable to the Former Manager as it is not a party to the agreement between the Former Manager and Roseway.

[466] Accordingly, I see no basis for the Former Manager's position. It is in a position to pursue Roseway for payment of its account. However, regardless of payment, it was obligated to reduce the fees owing by the Fund pursuant to the Management Agreement by $300,000. It therefore owes the Fund this amount.

Legal and Advisory Fees for the 2011 to 2013 Fiscal Years

[467] The Fund claims that the Former Manager improperly charged three categories of claims to the Fund during the 2011 to 2013 fiscal years totalling $2,378,933. In each case, the Former Manager treated these expenses as "unusual or extraordinary." The Fund's position is that they were not "unusual or extraordinary" and were therefore payable by the Former Manager under section 6.1 of the Management Agreement. I will address each claim in turn.

Expenses Related to Debt Financings

[468] The Former Manager has charged the Fund with legal and consulting expenses that were incurred in relation to the Fund in respect of the Roseway Transaction, the WOF Loan and the Matrix Loan, including the Growthpoint Loan. The total amount is $939,259.50.

[469] The Fund says that if, as the Former Manager argued, it was reasonable for the Fund to incur this debt, these expenses should not be treated as "unusual or extraordinary." The Fund also says that, as "insurance," such expenses would constitute expenses "reasonably required to conduct the Fund's usual daily operation in an efficient manner" and, as such, would qualify as general expenses covered by section 6.1. In addition, it also says that it would have factored these costs into its decision-making if the Former Manager had advised the Fund of its position at the time of approval of the transactions, particularly the Roseway Transaction.

[470] The Fund cannot have it both ways. It argues on the one hand that the Roseway Transaction, the WOF Loan and the Matrix Loan were extraordinary transactions that addressed enterprise-threatening liquidity risks, that they were imprudent, and that they were unique to the Fund in that there is no evidence of similar borrowings by any other LSVCC. On the other hand, it also suggests that such transactions were reasonably required to conduct the Fund's usual daily operations in an efficient manner and were entered into the ordinary course of its business. It is also disingenuous to suggest that the Fund would not have entered into the Roseway Transaction if the Board had been apprised that it was to be responsible for its legal expenses in connection with this Transaction.

[471] Further, these expenses were disclosed to the AVC and the auditors of the Fund at the time of preparation of the audits of the Fund for the 2010, 2011 and 2012 fiscal years. The failure of either entity to raise the payment of these expenses at the relevant time is itself evidence of their respective views of the proper characterization of these expenses.

[472] Accordingly, I find no breach of section 6.1(b) of the Management Agreement in respect of these expenses and no obligation on the part of the Former Manager to reimburse the Fund for these expenses. Instead, these are "unusual or extraordinary" expenses that are to be borne by the Fund pursuant to section 6.2(c).

Expenses Pertaining to the Proposed Vengrowth Transaction

[473] The Former Manager also charged the Fund expenses totalling $547,104 pertaining to the Proposed Vengrowth Transaction. The Fund says that the Former Manager was obligated to pay these expenses on two grounds. The Fund says that such a finding would be consistent with a specific agreement between the Fund and the Former Manager to the effect that the Former Manager would pay all costs associated with this Transaction. It also says that the Former Manager was obligated to bear such expenses pursuant to *National Instrument 81-102 5.6(i)(h)*, which provides that "mutual funds participating in [the transaction] bear none of the costs and expenses associated with the transaction."

[474] The expenses in question apparently comprise $513,670 incurred in connection with the establishment of the proposed credit facility that was required to support the purchase of the

VenGrowth shares and $33,425 incurred in connection with independent legal advice provided to the Fund with respect to the Transaction.

[475] I would observe that the provisions of *National Instrument 81-102* are not directly relevant to this issue. Section 5.6 of that Instrument merely sets out the conditions for a transaction that would be exempted from the need for approval of the securities regulatory authorities. The issue for the Court is, therefore, the nature of the specific agreement between the parties.

[476] In accordance with the principles set out in sections 6.1 and 6.2 of the Management Agreement as discussed above, the expenses at issue are properly characterized as "unusual or extraordinary expenses" for which the Fund would ordinarily be responsible. However, the Fund says that the Former Manager agreed to bear all of the expenses of the Fund in relation to the Proposed VenGrowth Transaction.

[477] There is evidence of such agreement. Levi acknowledged on his cross-examination that the Former Manager paid the expenses of the Proposed VenGrowth Transaction. David Jennings, the corporate counsel to the Fund, understood that there was such an agreement. Further, the management information circular for the annual and special meeting of the shareholders of the Fund on June 28, 2011, at which the Proposed VenGrowth Transaction was approved, stated at page 24 that "[t]he manager of [the Fund] will pay all of the reasonable, incremental costs associated with the Merger incurred by [the Fund]." I also note that the minutes of the meeting of the Board held on April 27, 2011, at which Levi was present, stated, in connection with a discussion of the status of the Proposed VenGrowth Transaction, that "[a]nother Board member was informed that all costs associated with the potential VenGrowth merger, including the cost of independent counsel, have been borne by the [Former Manager]." None of these references to the Former Manager's obligation were qualified in terms of any particular expenses. The only qualification was the reference to "reasonable expenses" in the management information circular, which is not at issue in respect of this matter as put to the Court.

[478] Based on the foregoing, I conclude that the Former Manager improperly caused the Fund to bear the expenses of the Proposed VenGrowth Transaction at issue in breach of an agreement with the Fund that it would bear all of the Fund's expenses in regard to that Transaction. I would add that, if there had been an issue of whether the agreement was intended to extend to the costs in respect of the credit facility, in view of the agreement, the Former Manager should have raised the issue at the time. The Former Manager is, therefore, obligated to reimburse the Fund the amount of such expenses.

Legal Expenses Incurred in Connection With Certain Sales Transactions and the RMP

[479] The Former Manager also allocated the costs of independent legal advice to the Fund in respect of the potential sales transaction with Kirchner and in connection with the Newbury Transaction. In addition, the Former Manager charged the Fund with the legal expenses associated with the negotiations with the BCSC regarding the RMP. The actual amounts allocated to these matters is not before the Court, although they appear to total $892,569.50.

[480] In my view, these legal expenses are properly charged to the Fund as "unusual or extraordinary" expenses pursuant to section 6.2 of the Management Agreement for the following reasons.

[481] All of these expenses pertain to the orderly wind down of the Fund, which was the consequence of the decision of the Board to cease redemptions in October 2011. From that point forward, it cannot be said that the Fund was carrying on in a "business as usual" manner in its consideration of the sale of assets or the suspension of redemptions. Moreover, the purpose of the sales transactions, and one of the purposes of the RMP, was to prevent an immediate default under the Roseway Transaction and consequential insolvency proceedings.

[482] In respect of expenses for the proposed Kirchner Transaction and the Newbury Transaction, I would add that the principles applied above in respect of the claim for expenses pertaining to the Roseway Transaction, the WOF Loan and the Matrix Loan are equally applicable to these expenses. In respect of the RMP expenses, the fact that the Board may have preferred a complete cessation of redemptions is irrelevant. The Board authorized the Former Manager to pursue the RMP with the result that the Fund is obligated to pay the expenses in connection therewith.

[483] Accordingly, the Fund's claim for damages in respect of the Former Manager's alleged breach of section 6.1 regarding these matters is dismissed. These are also "unusual or extraordinary" expenses that are to be borne by the Fund pursuant to section 6.2(c).

Expenses Incurred in Prior Years

[484] The Fund has also asserted a claim of $781,000 for each of the 2009 and 2010 fiscal years for similar, but unspecified, improper charges for legal and accounting fees in those years. This amount is calculated as one-third of the aggregate amount claimed by the Fund in respect of the 2011 to 2013 fiscal years as discussed above, that is, it represents the average of the Fund's claim of improper expenses in those three fiscal years. The Fund says the Court should draw an adverse inference that similar improper charges occurred during the 2009 and 2010 fiscal years from the failure of the Former Manager to provide a breakdown of the legal and accounting fees for such fiscal years and its actions in charging the challenged expenses to the Fund.

[485] This claim is dismissed for the following three reasons. First, it is entirely speculative and without any evidentiary foundation. Second, given the Court's conclusions regarding the Fund's allegations of improper charges in the 2011 to 2013 fiscal years, there is no basis for inferring that any material amount of expenses were improperly allocated to the Fund as "unusual or extraordinary expenses" in any earlier period. Third, the Fund's position also ignores the fact that the Board and the AVC, as well as the Fund's auditors, were responsible for reviewing the legal and accounting expenses of the Fund in the course of carrying out their respective responsibilities and had a full opportunity to raise the appropriateness of these fees at the time.

Omnibus Claim for Legal, Financial Advisory and Accounting Expenses

[486] In addition to the foregoing claims, the Fund has asserted an omnibus claim for legal, financial advisory and accounting fees, and other expenses totalling $4.5 million that it says were

incurred in respect of each of the categories of damages asserted by the Fund. This claim is dismissed for the following reasons.

[487] First, as set out above, the Fund's claim for breach of the Standard of Care has been dismissed. Accordingly, there can be no associated claim for legal expenses related to pursuing such a claim.

[488] Second, with respect to the Fund's claim for damages alleged to have resulted from a failure to keep proper books and records, the Court has dismissed the substantial majority in amount of these claims, namely the claim in respect of the Cytochroma interest. There is no evidence of any legal expenses associated with the services of IAS in separating the co-mingled shareholder data. The remaining claim in this category pertains to the alleged cost of "repeatedly requesting delivery of the Fund's database and records" after termination of the Management Agreement. This did not involve a material amount of time or cost, is not itemized, and is not evidenced in any way, apart from a few letters, the cost of which would have been modest at best.

[489] Third, with respect to the Fund's claim that the Former Manager breached applicable securities legislation, the Fund says it has incurred the cost of having counsel review and advise on the Former Manager's failure to comply with such legislation in respect of the two matters in 2013 mentioned above. I have concluded above that the Former Manager is obligated to pay any such expenses pursuant to section 6.1 of the Management Agreement. However, there remains the issue of quantum. While there may have been some cost attributable to legal advice regarding each of these matters, it would also appear to have been modest in each case. In any event, there is no evidence of the actual amount of the legal fees or other expenses incurred in respect of either of the alleged breaches of securities legislation. This claim is therefore denied for this reason.

[490] Lastly, with respect to the Fund's claim for reimbursement of certain alleged normal operating and other expenses, although there may have been some expenses associated with these claims, it is not possible to identify the amount of such costs and expenses of the Fund as they have not been itemized and are not evidenced by any invoice or payment. Moreover, most of these claims, namely the KPMG audit fees for 2013, the fee reduction related to the Roseway defined portfolio services agreement and the fees incurred in connection with the Proposed VenGrowth Transaction, do not appear to have involved any legal or other costs beyond the costs of this proceeding.

[491] Accordingly, I find that, to the extent the Fund would otherwise have any remaining claims for legal, financial, advisory and accounting expenses after taking into consideration the larger amount of costs associated with the more significant claims that have been dismissed or otherwise dealt with, the Fund has failed to establish the amount of any such losses.

Conclusion and Costs

[492] For the reasons stated above, the Former Manager's claim for damages as a result of an alleged wrongful termination of the Management Agreement is dismissed except to the extent of its claim for unpaid management and administration fees accrued to the date of termination and

its claim for unpaid incentive payments. The Fund's counterclaim for damages for breach of the Standard of Care is also dismissed on the basis that it is barred by virtue of the provisions of the *Limitations Act, 2002*. The remainder of the claims asserted in this action, being claims of the Former Manager for Transition Services and of the Fund for damages based on certain other alleged breaches of the Management Agreement, are determined as set out above. In this regard, in the course of this trial, the amounts of certain of such claims have been subject to some variation. If there are any outstanding issues between the parties with respect to the application of the determinations herein regarding such amounts, or the quantum thereof, they should schedule a 9:30 a.m. appointment with the Commercial List office. Similarly, if the parties are unable to agree on costs in respect of this action, they should also schedule a 9:30 a.m. conference to address an appropriate procedure for resolution of this issue.

[492]

Wilton-Siegel J.

Released: May 18, 2018

SCHEDULE "A"

The IPA Shares have the following rights and restrictions;

(a) the holder of IPA Shares Is entitled to receive dividends (herein, "IPA Dividends") based on realized gains and income from venture capital investments. For venture capital investments made after November 29, 2002 (the "IPA Start Date"), the IPA Dividends will be equal to 20% of the realized gains and income from each such venture, subject to certain adjustments;

(b) before any IPA Dividends can be paid in respect of any venture capital investment, the following conditions must be met:

(i) the total net realized and unrealized gains and income of the Fund from its portfolio of venture capital investments since the IPA Start Date must have generated a minimum annualized rate of return;

(ii) the compounded annual internal rate of return (including realized and unrealized gains and income from prior partial dispositions of that venture capital investment or otherwise) from the venture capital investment since its acquisition by the Fund must equal or exceed 12% per year; and

(iii) the Fund must have fully recovered a cash amount at least equal to the principal invested in the venture capital investment. In addition, the payment of any IPA Dividend is subject to the restrictions in the CBCA generally applicable to the payment of dividends;

(c) IPA Dividends in respect of venture capital investments made prior to the IPA Start Date will be equal to 15% of the realized gains and income from each such venture capital investment subject to certain adjustments;

(d) IPA Dividends are calculated and payable quarterly. To the extent they are not declared by the Board and paid when payable, they are cumulative;

(e) except as required by law, the holder of IPA Shares is not entitled to vote;

(f) subject to the restrictions in the CBCA generally in respect to the payment of dividends, if the holder of the Class C shares is terminated as a manager or investment manager of the Fund, the holder of the IPA Shares will be entitled to receive all declared but unpaid IPA Dividends and an amount equal to the IPA Dividend that would be payable assuming all venture capital investments were sold at that time, with the holder's entitlement to such dividends arising as and when a particular venture investment is disposed of.

SCHEDULE "B"

(a) The Manager is in material breach of Sections 3.4 and 3.5 of the Management Agreement. By letters to GWC dated April 16, 2013 and April 30, 2013 and in comments made by Staff of the BCSC to GWC in a related meeting (copies of which are attached hereto as Exhibits "A", "B" and "C" (a written transcript of such comments, respectively), the British Columbia Securities Commission (the "BCSC") has, as part of its most recent compliance field examination of GWC, found, and it is the position of the Fund, that GWC and the Manager (as GWC conducts registerable activities for the Manager) breached a number of provisions of applicable securities laws in connection with the provisions of Services to the Fund following:

(i) In breach of section 125 of the Securities Act (British Columbia) (the "BC Securities Act") and Section 3.5 of the Management Agreement, GWC breached its fiduciary duty to the Fund. The BCSC found that GWC did not exercise the powers and discharge the duties of its office in the best interests of the Fund, nor did GWC exercise the degree of care, diligence, and skill that a reasonably prudent person would exercise in the circumstances, and that GWC has preferred its own interests to those of the Fund and other funds managed by the Manager and GWC. GWC's failure to consider all the scenarios and actions for dealing with the Canadian Fund's distressed financial situation was not in the best interests of the Fund.

(ii) GWC violated section 2, chapter 3 of its Policies and Procedures Manual ("PPM"). The PPM requires GWC to act "in the best interest of an investment fund managed by GrowthWorks". In violating the provisions of its PPM, GWC also breached section 11.1 and NI 31-103 Registration Requirements, Exemptions and Ongoing Registrant Obligations ("NI 31-103"). Section 11.1 of National Instrument 31-103 required GWC to apply policies and procedures that establish a system of controls and supervision sufficient to manage the risks associated with its business in accordance with prudent business practices.

(iii) In breach of Section 14 of the Rules, made under the BC Securities Act, GWC did not deal fairly with the Fund when recommending that the Fund borrow $33.5 million over the period from May 2010 to May 2012.

(iv) GWC violated section 2, chapter 3 of its PPM. The PPM requires GWC to avoid any activities, interest or associations which might interfere or give the appearance of interferences with the Independent exercise of their judgment, in the best interest of its managed funds. As GWC did not deal fairly when recommending

the Canadian Fund borrow $33.5 million over the period May 2010 to May 2012, it violated its PPM. In violating the provisions of its PPM, GWC also breached section 11.1 of NI 31-103. Section 11.1 of NI 31-103, required GWC to apply policies and procedures to establish a system of controls and supervision sufficient to manage the risks associated with its business in accordance with prudent business practices.

(v) In breach of Section 11.1 of NI 31-103, GWC failed to establish, maintain, and apply policies and procedures that establish a system of controls and supervision sufficient to provide reasonable assurance that the firm and each individual acting on its behalf complies with securities legislation and manage the risks associated with its business in accordance with prudent business practices.

(b) The Manager is in material breach of Section 3.4 of the Management Agreement. By a memorandum dated August 22, 2013 from GWC to the Board, GWC advised the Board that GWC is in breach of Section 12.1 of NI 31-103 and that certain conditions have been placed on GWC as a registrant for purposes of applicable securities law;

(c) By a memorandum dated June 4, 2013 from the Manager to the Audit Committee to the Board, the Manager admitted that it had made an error in connection with a follow-on financing by the Fund in Cytochroma Inc. ("Cytochroma") in the first quarter of 2012 when the Manager improperly allocated to GrowthWorks Commercialization Fund Ltd. securities of Cytochroma that should have been allocated to the Fund. The Manager subsequently failed to make due inquiries when Cytochroma initially delivered securities to the Manager in respect of that financing. Those securities in Cytochroma were subsequently exchanged for common shares of OPKO Health, Inc. in connection with the sale of Cytochromas. As a result, 88, 403 common shares of OPKO Health, Inc. remain in the control of GrowthWorks Commercialization Fund Ltd., a separate investment fund. The Manager has not taken any action to rectify this matter. Accordingly, the Manager has materially breached its obligations under (i) Section 3.5 of the Management Agreement to (A) act in the best interests of the Fund, and (B) exercise the degree of care, diligence and skill that a reasonably prudent person would exercise in the circumstances, and (ii) Section 3.9(a) to provide proper books of account and records for the Fund;

(d) In connection with the Cytochroma transaction referred to in clause (c) above, a senior employee of the Manager at the time, Joseph Regan, has advised representatives of the Fund that he did not carefully read, before signing on behalf of the Fund, an Acknowledgement and Receipt between the Fund and Roseway that purports to impose on the Fund material

contractual obligations in favour of Roseway with respect to the beneficial ownership of, and entitlement to divestment proceeded from, the sale of securities of OPKO Health, Inc. That document is now relied upon by Roseway as a basis for claiming from the Fund approximately $1.9 million in proceeds realized by the Fund in connection with the sale of those securities of OPKO Health, Inc. In executing that document without due (or any) consideration to its legal effect from the standpoint of the Fund, the Manager has materially breached its obligations under Section 3.5 of the Management Agreement, to (i) act in the best interests of the Fund, and (ii) exercise the degree of care, diligence and skill that a reasonably prudent person would exercise in the circumstances;

(e) In connection with a reconciliation prepared by PricewaterhouseCoopers ("PWC") on behalf of Roseway Capital S a.r.l. ("Roseway") with respect to participating interest payments owing by the Fund to Roseway under the Participation Agreement dated May 28, 2010 between the Fund and Roseway, PWC discovered numerous errors by the Manager in relation to the accounts maintained by the Manager on behalf of the Fund and the calculation in payment of those participating interest payments to Roseway. These errors on the part of the Manager have caused the Fund to incur significant payments to Roseway and significant professional fees and expense. Accordingly, the Manager has materially breached its obligations under (i) Section 3.5 of the Management Agreement to exercise the degree of care, diligence and skill that a reasonably prudent person would exercise in the circumstances, and (ii) Section 3.9(a) of the Management Agreement to keep proper books of account and records for the Fund; and

(f) As set forth in the letters of the Fund's counsel, McCarthy Tétrault LLP dated June 18, 2013 and September 19, 2013, the Fund has improperly used the authority granted to the Manager under Section 3.1 of the Management Agreement to act on behalf of the Fund by causing the Fun to pay legal and accounting expenses that the Manager is required to pay pursuant to Section 6.1 of the Management Agreement. As a result, the Manager has materially breached its obligations under Sections 3.3, 3.5 and 6.1 of the Management Agreement.

CITATION: Growthworks WV Management Ltd. v. Growthworks Canadian Fund Ltd., 2018 ONSC 3108
COURT FILE NO.: CV-13-10279-00CL
DATE: 20180518

ONTARIO

SUPERIOR COURT OF JUSTICE

BETWEEN:

GROWTHWORKS WV MANAGEMENT LTD.
Plaintiff

- and -

GROWTHWORKS CANADIAN FUND LTD.
Defendant

REASONS FOR JUDGMENT

Wilton-Siegel J.

Released: May 18, 2018