Court of Appeal File Numbers: M42068
Superior Court File No. CV-12-9667-00CL

COURT OF APPEAL FOR ONTARIO

IN THE MATTER OF THE *COMPANIES' CREDITORS ARRANGEMENT ACT*, R.S.C. 1985, c. C-36, AS AMENDED

AND IN THE MATTER OF A PLAN OF COMPROMISE OR ARRANGEMENT OF SINO-FOREST CORPORATION

RESPONDING FACTUM OF THE AD HOC COMMITTEE OF NOTEHOLDERS

(Motion for Leave to Appeal from Sanction Order)

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I. OVERVIEW

1. This factum is submitted by the Ad Hoc Committee of Noteholders (the "**Ad Hoc Committee**") of Sino-Forest Corporation ("**SFC**") in response to the motion for leave to appeal certain portions of the Sanction Order (defined below) by Invesco Canada Ltd., Northwest & Ethical Investments L.P. and Comité Syndical National de Retraite Bâtirente Inc. (collectively, the "**Moving Parties**").

2. After many months of proceedings, SFC's Plan of Compromise and Reorganization pursuant to the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36 (the "**CCAA**") and the *Canada Business Corporations Act*, R.S.C. 1985, c. C-44 (the "**Plan**") was overwhelmingly approved by its creditors (99.96% in value and 98.81% in number) at a creditors' meeting held on December 3, 2012. On December 10, 2012, the Honourable Justice Morawetz of the Ontario Superior Court of Justice (the "**CCAA Court**") granted an order (the "**Sanction Order**")

approving the Plan in its entirety, including Article 11 of the Plan (discussed below). The Plan was implemented on January 30, 2013.

3. Pursuant to the Plan, the noteholders of SFC (including the members of the Ad Hoc Committee which held approximately 50% of SFC's approximately $1.8 billion principal amount of note debt) became the shareholders and noteholders of "Newco", the newly formed entity to which substantially all of SFC's assets were transferred pursuant to the Plan.

4. The Moving Parties now seek leave to appeal only paragraphs 40 and 41 of the Sanction Order, which approved Article 11 of the Plan. Article 11 of the Plan sets out a framework pursuant to which the third party defendants to the Sino-Forest class actions, such as Ernst & Young LLP ("**Ernst & Young**"), could receive a release under the Plan in certain circumstances and states explicitly that any such release will only be granted if numerous conditions are met, including further court approval of the proposed settlement.[1] As such, Article 11 of the Plan provides only a framework for the potential future court approval of releases for third party defendants, such as Ernst & Young, who may reach settlements with the plaintiffs in the class actions (as such, the "**Framework for Future Releases**").

5. Through the E&Y settlement and the development of Article 11 and its Framework for Future Releases, SFC was able to reach agreements with all of the main third party defendants to the class actions (including Ernst & Young, the other former auditor, BDO Limited, and all of SFC's underwriters) concerning the Plan and its sanction.

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[1] Subsection 8.2(z) of the Plan and Section 11.1 of the Plan, Motion Record of the Appellants, Tab 4(A).

6. Once developed and incorporated into the Plan, Article 11 and the Framework for Future Releases was considered by the creditors at the December 3rd creditors' meeting when they overwhelmingly approved the Plan, and was considered by the CCAA Court at the December 10th sanction hearing when it granted the Sanction Order.

7. Article 11 was an important part of removing opposition to the Plan and achieving a timely implementation of the Plan. Article 11 forms an important part of the compromise solution that the Plan – like all CCAA plans – represents for all stakeholders of SFC.

8. The inclusion of the Framework for Future Releases was proper, fair, reasonable and important in the context of SFC's restructuring. Moreover, the Framework for Future Releases approved as part of the Plan and the Sanction Order is only that – a framework or process for considering potential future settlements and related releases. That process requires another hearing and, if a release is thought fit, another Order. Article 11 and its approval did not affect the rights of the Moving Parties to object to a proposed class action settlement and/or release at any such further hearing.

9. For these and the other reasons set out below, the Ad Hoc Committee submits that Article 11 is an important and proper part of SFC's Plan, as approved by its creditors and the CCAA Court. It is the Ad Hoc Committee's position that the CCAA judge did not err in granting the Sanction Order or any part of it and, accordingly, the Moving Parties' motion for leave to appeal should be dismissed.

II. FACTS

10. The Ad Hoc Committee adopts the facts summarized in the endorsement of the Honourable Justice Morawetz released on December 10, 2012 (the "**Sanction Order Reasons**") and in the factum of SFC. Certain of these facts, which form the basis for the Ad Hoc Committee's position, are repeated below.

11. To the extent of any conflict between the facts as summarized in the Sanction Order Reasons or the SFC factum, and the facts as stated by the Moving Parties, the Ad Hoc Committee disagrees with the facts as set out in the Moving Parties' factum.

12. SFC sought relief under the CCAA on March 30, 2012 in order to restructure its business as soon as possible for the benefit of its stakeholders.[2] SFC and the Court-appointed monitor (the "**Monitor**") repeatedly noted the urgency of the CCAA proceedings. On several occasions, the Monitor stated in its reports the need to complete the restructuring as soon as possible to preserve the value of the SFC business.

13. Prior to implementation of the Plan, SFC was a Canadian holding company whose assets and business were comprised entirely of its subsidiaries. No effective restructuring of SFC's business would have been possible without a complete separation of the business and the assets from the Canadian parent/defendant (SFC).[3] This was the stated objective of the CCAA proceedings since their commencement – to separate as soon as possible SFC's business and

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[2] Affidavit of W. Judson Martin, sworn January 11, 2013 (the "**Martin January 11 Affidavit**"), paras. 11-13, Motion Record of Sino-Forest Corporation, Tab 1 (B), p. 37; Sanction Hearing Endorsement of Justice Morawetz dated December 12, 2012, paras. 18-19, Motion Record of the Appellants, Tab 7.

[3] Affidavit of W. Judson Martin sworn November 29, 2012 (the "**Martin November 29 Affidavit**"), para. 124, Motion Record of the Appellants, Tab 3(N), p. 322.

assets from the myriad of litigation that had been commenced against SFC, its directors and officers and the third party defendants, all of whom claimed indemnity from SFC and its subsidiaries.[4]

14. Throughout the proceedings the Ad Hoc Committee supported SFC in its efforts to develop a restructuring transaction that would be supported by SFC's creditors, including by participating in a mediation that took place among SFC, the class action plaintiffs, the third party defendants, the Monitor and the Ad Hoc Committee on September 4, 2012 and September 5, 2012 pursuant to the Mediation Order granted by the CCAA Court on July 25, 2012.[5] While no settlement was reached at the mediation, settlement discussions continued after the mediation and the E&Y settlement was reached on November 29, 2012.[6]

15. In the days that followed, the Plan was amended to include Article 11, which set out the Framework for Future Releases. The Plan, with Article 11, was considered and approved by the creditors on December 3, 2012 and by the CCAA Court on December 10, 2012.

16. As consideration for the inclusion of Article 11 into the Plan, Ernst & Young agreed with SFC that it would, among other things, waive all claims against SFC, not receive any consideration of any kind under the Plan, waive all rights to appeal and support and vote for the Plan. The other former auditor, BDO Limited, and each of the underwriters also agreed to

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[4] Martin November 29 Affidavit, paras. 66-72, Motion Record of the Appellants, Tab 3(N), pp.306-307.

[5] Martin January 11 Affidavit, para. 14, Motion Record of Sino-Forest Corporation, Tab 1(B), p. 38.

[6] Martin November 29 Affidavit, para. 86, Motion Record of the Appellants, Tab 3(N), p. 311; Martin January 11 Affidavit, para. 16, Motion Record of Sino-Forest Corporation, Tab 1(B), p. 38; Thirteenth Report of the Monitor dated November 22, 2012 at para. 31, Ernst & Young Record, Tab 18.

support the Plan, with Article 11.. On this basis, the Plan was presented to the CCAA Court for approval at the sanction hearing with the support of all parties, except the Moving Parties.

17. The E&Y settlement and the development and inclusion of Article 11 of the Plan and its Framework for Future Releases was a significant and positive development in SFC's restructuring that provided tangible benefits to SFC, its stakeholders and the CCAA proceedings, including that:

(a) Ernst & Young and the other third party defendants agreed to support the Plan;

(b) Ernst & Young and the other third party defendants agreed to release all of their claims against SFC and its subsidiaries thereby eliminating the time and expense needed to litigate those claims and the potential dilution of the recovery by creditors if any of those claims against SFC were ultimately determined to be valid claims under the Plan;[7]

(c) Ernst & Young and the other third party defendants agreed not to seek leave to appeal to the Supreme Court of Canada in respect of this Court's dismissal of their appeal of the "Equity Claims Decision";

(d) Ernst & Young and the other third party defendants agreed not to receive any distributions of any kind under the Plan, thereby materially decreasing the unresolved claims reserve that would otherwise have had to be created under the Plan in respect of these contested claims; and

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[7] Subsections 7.1(m) (n) and (o) of the Plan, Motion Record of the Appellants, Tab 4(A).

(e) the E&Y settlement – if approved – provides a recovery to the equity holders of SFC who otherwise do not receive any distributions under the Plan.[8]

18. The E&Y settlement, Article 11 of the Plan, its Framework for Future Releases and the corresponding support of Ernst & Young and the other third party defendants for the Plan all contributed to the overall timeliness of the approval of the Plan and the ultimate implementation of the Plan, each of which needed to occur as soon as possible under the circumstances of this restructuring.[9]

19. Pursuant to the Framework for Future Releases, on February 4, 2013, the Honourable Justice Morawetz heard a separate, specific motion seeking approval of the E&Y settlement. The Moving Parties opposed the motion, arguing that the E&Y settlement was not fair and reasonable. Any issues relating to the E&Y settlement were considered at that hearing pursuant to a hearing schedule that was accepted by the Moving Parties for purposes of that separate hearing. The Honourable Justice Morawetz has reserved his decision on approval of the E&Y settlement.

III. LAW AND ARGUMENT

A. Leave to Appeal

20. Leave to appeal an order made in a CCAA proceeding can only be granted where:

(a) the point on appeal is of significance to the practice;

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[8] Martin January 11 Affidavit, para. 19, Motion Record of Sino-Forest Corporation, Tab 1(B), pp. 39-40.

9 Martin January 11 Affidavit, para. 21, Motion Record of Sino-Forest Corporation, Tab 1(B), p. 40; Martin November 29 Affidavit, para. 165, Motion Record of the Appellants, Tab 3(N); Thirteenth Report of the Monitor dated November 22, 2012 at paras. 20, 22 and 110, Ernst & Young Record, Tab 18.

(b) the point on appeal is of significance to the underlying parties;

(c) the appeal is *prima facie* meritorious and not frivolous; and

(d) the appeal will not hinder the progress of the action.[10]

21. The four part test for granting leave to appeal requires that all four elements be satisfied; the failure to establish any one of the requirements will result in a dismissal of the application.[11]

22. The moving parties carry a heavy burden in order to obtain leave in a CCAA proceeding, and courts have emphasized that such an application will only be granted sparingly because of, among other things, the "real time" dynamic of CCAA proceedings and the discretionary nature of orders made by supervising CCAA judges. [12]

23. For the reasons set forth below, the Ad Hoc Committee respectfully submits that the Moving Parties have not satisfied the test for granting leave to appeal.

(a) Point on appeal is not of significance to the practice

24. The point on appeal is not of significance to the practice. In the particular circumstances of this restructuring, it was proper for the Plan to contain – and for the CCAA Court to approve a Plan that contained – a Framework for Future Releases. As discussed above, the Framework for Future Releases under Article 11 of the Plan is merely a mechanic or procedure that sets out how potential settlements and related releases might be approved in the future. Whether or not any

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[10] *Stelco Inc. (Re)* (2005), 75 O.R. (3d) 5 (C.A.) at para. 24, Brief of Authorities of Sino-Forest Corporation, Tab 2; *Timminco Ltd. (Re)*, 2012 ONCA 552 at para. 2, Brief of Authorities of Sino-Forest Corporation, Tab 3.

[11] *Statoil Canada Ltd. (Arrangement relatif a),* 2012 QCCA 665 at paras. 4 & 7, Brief of Authorities of Sino-Forest Corporation, Tab 4.

[12] *Statoil Canada Ltd. (Arrangement relatif a), supra* at para. 4, Brief of Authorities of Sino-Forest Corporation, Tab 4; *Timminco Ltd. (Re), supra* at para. 2, Brief of Authorities of Sino-Forest Corporation, Tab 3; *Stelco Inc.,* [2005] O.J. No. 4883 (C.A.) at paras 15 & 18, Brief of Authorities of Sino-Forest Corporation, Tab 5; *Pacific National Lease Holding Corp. (Re)* (1992), 19 B.C.A.C. 134 at paras. 28-30, Brief of Authorities of Sino-Forest Corporation, Tab 6.

such settlement should be approved or not is a question for another hearing and another order – but not the Sanction Order, which merely established the process.

25. It is of no significance to the practice that the Plan sets out this process for potential future approvals. In issuing the Sanction Order, the Honourable Justice Morawetz correctly found that the Moving Parties' objections with respect to Article 11 of the Plan were premature and would more appropriately be considered at the future hearing to consider whether or not the E&Y settlement (or any other settlement) should actually be approved:

> [22] Having reviewed these documents [the relevant provisions of the Plan], it is apparent that approval of the E&Y Settlement is not before the court on this motion and no release is being provide to E&Y as a result of this motion. In the event all of the pre-conditions are satisfied and if all of the required court approvals and orders are issued, the position of the Funds [the Moving Parties] could be affected. However, the Funds will have the opportunity to make argument on such hearings.
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> [23] I have also reviewed the form of Sanction Order being requested specifically paragraph 40. This provision provides that the E&Y Settlement and the release of the E&Y Claims pursuant to section 11.1 of the Plan shall become effective upon the satisfaction of certain conditions precedent, including court approval of the terms of the E&Y Settlement, the terms and scope of the E&Y Release and the Settlement Trust Order and the granting of the Settlement Trust Order.
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> [24] Paragraph 41 of the draft Sanction Order also provides that any Named Third Party Defendant Settlement, Named Third Party Defendant Settlement Order and Named Third Party Defendant Release, the terms and scope of which remain in each case subject to further court approval in accordance with the Plan, shall only become effective after the Plan Implementation Date and upon the satisfaction of the conditions precedent, set forth in section 11.2 of the Plan.
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> [25] The requested Sanction Order confirms my view that the arguments put forth by counsel on behalf of the Funds are

premature and can be addressed on the return of the motion to approve the specific settlements and releases.[13]

(b) Point on appeal is not of significance to the underlying parties

26. The Moving Parties have already acceded to the provisions of Article 11 of the Plan in proceeding with the February 4th motion to consider the E&Y settlement at which, pursuant to an agreed upon schedule, they were given and had an opportunity to make all of their arguments concerning whether or not the E&Y settlement should be approved, including whether or not they should continue to have access to any statutory opt-out rights. As such, the present appeal is of no significance to the parties as the procedures in question have already been carried out on consent of the Moving Parties.

(c) Appeal is not *prima facie* meritorious

27. In order for this requirement to be satisfied, "on first impression, there must appear to be an error in principle of law or a palpable and overriding error of fact. Exercise of discretion by a supervising judge, so long as it is exercised judicially, is not a matter for interference by an appellate court, even if the appellate court were inclined to decide the matter another way."[14]

28. Courts have long recognized and reiterated the large amount of deference that must be afforded to decisions made by the supervising judge in a CCAA proceeding.[15]

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[13] Sanction Order Endorsement, December 10, 2012, Motion Record of the Appellants, Tab 5.

[14] *Resurgence Asset Management LLC v. Canadian Airlines Corp.*, 2000 ABCA 149 at para. 35, Brief of Authorities of Sino-Forest Corporation, Tab 9.

[15] *Ravelston Corp. (Re)*, 2007 ONCA 268 at *para.* 14, Brief of Authorities of Sino-Forest Corporation, Tab 10; *Resurgence Asset Management, supra* at para. 28, Brief of Authorities of Sino-Forest Corporation, Tab 9.

29. The Honourable Justice Morawetz has presided over the entirety of these CCAA proceedings and was and is uniquely situated with respect to the facts and circumstances of this case. The Honourable Justice Morawetz made no error of any kind in deciding that the Plan was fair and reasonable, and that it was proper for the Plan to include – in the context of this multi-faceted and complex restructuring – the Framework for Future Releases, which would set out the procedures by which any settlements among SFC, the Named Third Party Defendants and the class action plaintiffs might ultimately be considered for further court approval.

30. Moreover, the development and inclusion of Article 11 and the Framework for Future Releases into the Plan was an important step in allowing SFC to achieve a complex compromise solution that was overwhelmingly accepted by its creditors, supported by all of SFC's stakeholders (expect for the Moving Parties), and approved by an experienced CCAA judge familiar with all the facts and circumstances of these particular CCAA proceedings.

IV. RELIEF REQUESTED

31. For the reasons set forth above, the Ad Hoc Committee respectfully submits that the Moving Parties' motion for leave to appeal the Sanction Order should be dismissed.

ALL OF WHICH IS RESPECTFULLY SUBMITTED this 26th day of February 2013,

GOODMANS LLP

Lawyers for the Ad Hoc Committee of Noteholders of Sino-Forest Corporation

SCHEDULE "A" – AUTHORITIES CITED

1. *Stelco Inc. (Re)* (2005), 75 O.R. (3d) 5 (C.A.)
2. *Timminco Ltd. (Re)*, 2012 ONCA 552
3. *Statoil Canada Ltd. (Arrangement relatif a)*, 2012 QCCA 665
4. *Stelco Inc.* (2005), 78 O.J. No. 4883 (C.A.)
5. *Pacific National Lease Holding Corp. (Re)* (1992), 19 B.C.A.C. 134
6. *Resurgence Asset Management LLC v. Canadian Airlines Corp.*, 2000 ABCA 149
7. *Ravelston Corp. (Re)*, 2007 ONCA 268

SCHEDULE "B" – STATUTORY REFERENCES

1. *Companies' Creditors Arrangement Act*, R.S.C., 1985, c. C-36

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