

# The role of third parties and stakeholders in a Plan of Arrangement

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In *Re iAnthus Capital Holdings Inc.*, the British Columbia Court of Appeal affirmed a lower court's decision approving a revised plan of arrangement. This capped a series of decisions in respect of the proposed transaction, which together provide valuable insight into the role of third parties and stakeholders in the plan of arrangement process.

In the initial decision, Justice Gomery of the Supreme Court of British Columbia (SCBC) rejected an application by iAnthus Capital Holdings, Inc. (iAnthus) for approval of a restructuring plan of arrangement, on the basis of overly broad release and injunction clauses. The SCBC did not dismiss the application outright but provided an opportunity for the parties to revise the plan and in particular the release and injunction clauses in question. On a further application, the SCBC approved the revised plan.

Below we provide: (1) a brief overview of the plan of arrangement structure and (2) a summary of the most significant aspects of the case.

## Plan of Arrangement - Overview

For parties seeking to acquire a target company, or a company seeking to restructure its debt obligations, a plan of arrangement (the Plan of Arrangement or Arrangement) is a viable option to be considered. The Plan of Arrangement, a statutory, court-supervised process, normally involves a negotiated deal between the potential acquiror (the Offeror) and the target company, or, in the case of a restructuring, the company and its creditors. (In both cases, the applicable company is referred to herein as the Company).

## Plan of Arrangement - Process

Once the parties have negotiated and agreed to a definitive agreement setting out the terms of the transaction in detail, the Company will apply to court for an interim order (the Interim Order) with respect primarily to the manner in which the Company's securityholder meeting should be convened. Once the court has granted an Interim Order, a securityholder meeting for the Company will be set in order to consider and if thought appropriate, approve the Arrangement.

In connection with the holding of the Company's securityholder meeting, an information circular will be circulated to securityholders of the Company, which describes and recommends approval of the transaction. Once the shareholder meeting has been held and if an affirmative vote in favor of the Arrangement has been obtained, the Company will return to court to apply for a final order.

At the hearing for the final order, the court will review the transaction to determine whether it is "fair and reasonable"<sup>1</sup>, paying close attention to the percentage of securityholders who voted and exercised their votes in favour of the

transaction. The court is typically deferential to the business judgment of the board where it has obtained a fairness opinion from a reputable financial advisor, although such fairness opinions have recently become subject to greater judicial scrutiny.

## Case background and analysis

As noted, the BC Court of Appeal (BCCA) affirmed Justice Gomery's order approving a revised Plan of Arrangement under the *Business Corporations Act* (British Columbia) (the BCA), a week following its initial rejection due to the overly broad scope of release of claims and permanent injunction clauses contained in the initial plan.

iAnthus was incorporated under the BCA but carried on business in the United States in the cannabis industry. In total, iAnthus owed approximately CA\$97.5 million in principal in secured notes and CA\$60 million in principal to a group of unsecured creditors, in addition to ordinary trade creditors. iAnthus encountered financial difficulties and was unable to make interest payments on its secured notes in March 2020.<sup>2</sup> This default constituted a cross-default on its unsecured notes. As a result, iAnthus began negotiations with its creditors and in July 2020 entered into a restructuring agreement (the Restructuring Agreement) which, among other terms, reduced the secured notes by \$13.5 million, extinguished the unsecured notes, and provided each of the secured and unsecured creditors groups with shares in the capital of iAnthus representing 48.625% of iAnthus' total outstanding shares (i.e. 97.25% of outstanding shares in total). The Restructuring Agreement was to be implemented by way of a Plan of Arrangement under the BCA (the Initial Plan).

The Initial Plan also included a release and an injunction. The release had the following terms:

- it was for the benefit of iAnthus, its current and former directors, officers, employees, shareholders, auditors, financial advisors, legal counsel and agents and for the creditors and "persons associated with them" (each a Released Party);
- it excluded liabilities or claims attributable to any Released Party's gross negligence, fraud or wilful misconduct as determined by the final, non-appealable judgment of a court of competent jurisdiction;
- the claims subject to the release were all those arising on or prior to the effective date of the release in connection with various matters such as the secured notes, including the affected "Equity Claims", defined by reference to a definition in s. 2(1) of the *Companies' Creditors Arrangement Act*;<sup>3</sup> and
- the subject claims were further extended to "any other actions or matters related directly or indirectly to the foregoing".<sup>4</sup>

In addition, the injunction provided that:

"All Persons are permanently and forever barred, estopped, stayed and enjoined, on and after the Effective Date, with respect to any and all Released Claims, from (a) commencing, conducting or continuing in any manner, directly or indirectly, any action, suits, demands or other proceedings of any nature or kind whatsoever against the Released Parties, as applicable; (b) enforcing, levying, attaching, collecting or otherwise recovering or enforcing by any manner or means, directly or indirectly, any judgment, award, decree or order against the Released Parties; (c) creating, perfecting, asserting or otherwise enforcing, directly or indirectly, any lien or encumbrance of any kind against the Released Parties or their property; or (d) taking any actions to interfere with the implementation or consummation of this Plan; provided, however, that the foregoing shall not apply to the enforcement of any obligations under this Plan."<sup>5</sup>

A group of debentureholders and one shareholder (the Appellants) opposed the Initial Plan. In analyzing the language

of the originally drafted release, Justice Gomery deemed it legally unjustifiable for a release to bar claims of third parties with no benefits to derive from the arrangement, such as historical securityholders that preceded the proposal of the plan of arrangement. To Justice Gomery, the mere presence of a clause that effectively barred claims from third parties who did not receive any benefit under a proposed plan of arrangement rendered that arrangement unfair and unreasonable.<sup>6</sup> Justice Gomery took similar issue with the permanent injunction clause, which purported to bolster the preventative effect on “all persons” from pursuing legal action and enforcing claims against iAnthus, effectively converting any unsuccessful third party challenge to the release into a contempt of the Court.<sup>7</sup>

However, Justice Gomery allowed iAnthus to amend the Initial Plan and submit a revised plan (the Revised Plan), with a narrower scope of the release pertaining to third party claims and without the inclusion of any permanent injunction.<sup>8</sup> The Court approved the amended release on the basis that it was legally justifiable under Section 291(4) of the BCA. Specifically, the amended release had the following revised terms:

- It excluded shareholders, auditors and agents from the definition of Released Party;
- It provided for the release of claims brought by anyone against any of the Released Parties in connection with the Restructuring Agreement, the Revised Plan, and the legal proceedings related to both;
- It limited the ability of the shareholders and equityholders who had an opportunity to vote on the Revised Plan and Released Parties to advance “Affected Equity Claims” against the Released Parties;
- It limited the ability of the shareholders and equityholders who had an opportunity to vote on the Revised Plan and Released Parties to advance claims against the Released Parties in connection with the notes (secured and unsecured) and other enumerated matters; and
- It limited claims for contribution or indemnity against a Released Party that could only be brought, as a practical matter, by a Released Party following a successful defence of a Released Claim.<sup>9</sup>

Overall, Justice Gomery found the Revised Plan to be fair and reasonable, finding that:

“The Revised Plan offers substantial benefits to shareholders and was approved by a significant majority of shareholders. Its purpose is to effect a capital restructuring that will allow iAnthus to move forward towards profitability. The release is an ancillary order for the accomplishment of that purpose. Its effects are targeted and attenuated by the carve-out of claims for gross negligence, fraud, or wilful misconduct. The persons who are most likely to suffer adverse effects from the release also receive benefits under the Revised Plan, or the benefit of the release, or both.” (para 44).

The Appellants appealed Justice Gomery’s decision. However, the BCCA affirmed Justice Gomery’s decision approving the Revised Plan in addition to dismissing the Appellants’ arguments. Specifically, the Appellants argued that the lower court judge had erred on two points: (i) basing his decision on the misrepresentation by iAnthus that all material financial information had been disclosed, and (ii) that the plan was fair and reasonable despite it not considering their interests. In dismissing the appeal, the BCCA also found the following: (i) the Appellants’ other claim against a director had only been affected to a limited extent by the release because they could still sue for grounds not covered by it, (ii) that iAnthus was not required to deal with all classes of securityholders under either the BCA or the Revised Plan, and (iii) the Appellants’ claim for admission of fresh evidence could not be accepted because the evidence they sought to introduce had already been disclosed to them and would not have changed the outcome of Justice Gomery’s decision.

## Takeways

Although not examined in isolation, releases barring claims of third parties who receive no benefit from a proposed plan of arrangement, which they may not even be aware of, are unfair and unreasonable. This characterization on its own will render the proposed arrangement unfair and unreasonable and thus, unacceptable, notwithstanding that the balance of the plan of arrangement is considered fair and reasonable.

In the context of a plan of arrangement that is to effect a capital restructuring intended to drive the Company towards profitability, releases of third party claims are ancillary orders for the accomplishment of that purpose.<sup>10</sup>

Substantive amendments to a plan of arrangement that had been previously sanctioned by the parties with a direct concern (i.e., the securityholders or the equityholders) do not necessarily trigger the need for a new securityholder approval where the suggested changes are not detrimental to the securityholders or the equityholders.<sup>11</sup>

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1. *BCE Inc. v. 1976 Debentureholders*, 2008 SCC 69.↩

2. 2021 BCCA 48. ↩

3. Section 2(1), *Companies' Creditors Arrangement Act*, RSC 1985, c C-36 defines an *Equity Claim* as a claim in respect of an equity interest, including a claim for, among others, a dividend or similar payment; a return of capital; a redemption or retraction obligation; a monetary loss resulting from the ownership, purchase or sale of an equity interest or from the rescission, or, in Quebec, the annulment, of a purchase or sale of an equity interest, or; contribution or indemnity in respect of a claim referred to in any of these categories.↩

4. 2020 BCSC 1442. ↩

5. 2020 BCSC 1442. ↩

6. 2020 BCSC 1442. ↩

7. 2020 BCSC 1442. ↩

8. 2020 BCSC 1484. ↩

9. 2020 BCSC 1484. ↩

10. 2020 BCSC 1484. ↩

11. 2020 BCSC 1484. ↩

## Your Key Contacts



**Bennett Wong**

Partner, Calgary

D +1 403 268 7057

[bennett.wong@dentons.com](mailto:bennett.wong@dentons.com)



**Gregory Brown**

Associate, Vancouver

D +1 604 648 6519

[gregory.brown@dentons.com](mailto:gregory.brown@dentons.com)



**Dan Cerchia**

Associate, Calgary

D +1 403 268 7176

[dan.cerchia@dentons.com](mailto:dan.cerchia@dentons.com)