IN THE SUPREME COURT OF BRITISH COLUMBIA

Citation: ***Ehattesaht Holdings Ltd. v. Coulson Forest Products et al.,*** 2006 BCSC 1810

Date: 20061207
DocketS061816
Registry: Vancouver

Between:

Ehattesaht Holdings Ltd.

Petitioner

And

Coulson Forest Products Ltd., Hecate Logging Ltd., Maquinna Aircrane 2000 Ltd., Maquinna Forest Products Ltd.

Respondents

Before: The Honourable Mr. Justice Pitfield

Reasons for Judgment

Counsel for the Petitioner:	William E.J. Skelly, James P. Tate
Counsel for the Respondent, Coulson Forest Products Ltd.:	Frank G. Potts
Counsel for the Respondent, Hecate Logging Ltd., The Receiver, Ernst & Young Inc.:	Mary I.A. Buttery
Date and Place of Hearing:	December 1, 2006 Vancouver, B.C.

[1] Ernst & Young Inc., appointed receiver and liquidator of Hecate Logging Ltd. by court order made April 28, 2006, applies for an order approving the sale of Hecate's forest licence to Ehattesaht Holdings Ltd. ("EHL") free and clear of encumbrances, including replacement logging contracts.

[2] At the conclusion of the hearing, I dismissed the application, granted liberty to reapply, and advised counsel that I would provide written reasons for my decision.

[3] The background to the application is as follows. EHL and Coulson Forest Products Ltd. ("CFPL") are equal shareholders of Hecate which holds a forest licence conferring cutting rights in an area of Vancouver Island. Maquinna Forest Products Ltd. ("MFPL") and Maquinna Aircrane 2000 Ltd. ("MAL") are wholly owned subsidiaries

of Hecate. For many years, MFPL has carried on conventional logging operations under the licence, while MAL has carried on heli-logging operations. Each of MFPL and MAL has used a variety of contractors to conduct the logging operations. Some of those contractors were affiliated with CFPL. Others were strangers to EHL, CFPL and Hecate.

[4] For reasons which were not fully explained in the affidavit material, the working relationship between CFPL and EHL in relation to Hecate broke down. EHL gave notice under a shareholders' agreement that Hecate should be wound up. EHL says that CFPL refused to consent to the winding-up, contrary to the shareholders' agreement. On March 17, 2006, EHL commenced this action by petition. It sought an order pursuant to s. 324 of the *Business Corporations Act*, S.B.C. 2002, c. 57 ("*BCA*"), that Hecate be liquidated and dissolved, an order that a liquidator be appointed, an order that the liquidator be directed to sell Hecate's forest licence with each shareholder being afforded the opportunity to exercise a right of first refusal in respect of offers to purchase the licence, and other consequential relief.

[5] On April 28, 2006, the court ordered the liquidation of Hecate. The material terms of the order for present purposes are the following:

> THIS COURT ORDERS THAT:
>
> 1. On July 31, 2006, Hecate Logging Ltd. ("Hecate") shall commence proceedings to liquidate and dissolve Hecate;
>
> 2. Subject to the terms and conditions of this Order, pursuant to s. 324(3)(b) and 227(3) of the *Business Corporations Act*, S.B.C. 2002, c. 52, Ernst & Young Inc. is appointed receiver for Hecate (the "Receiver"), without security, of all of Hecate's current and future assets, undertakings and properties of every nature and kind whatsoever and wherever situate including all proceeds thereof (the "Property");
>
> 3. Prior to July 31, 2006, the Receiver may only:
>
> i) Identify assets and propose sales mechanisms;
>
> ii) Prepare and deliver to the parties a report on whether the debt in the amount of $445,250.00 allegedly owing from EHL to Hecate is properly a debt owing from EHL to Hecate;
>
> iii) Prepare and deliver to the parties a report on the value, if any, of the agreement with Western Forest Products dated December 15, 1997; and
>
> iv) Take such other steps as CFP and EHL may agree or as this Court may order.
>
> 4. After July 31, 2006, the Receiver is expressly empowered and authorized to take into its custody or control the Property and to comply with such other duties as the parties may agree or as this Court may order. Without limiting the generality of the foregoing, the Receiver shall:
>
> i) Prepare and deliver to the parties the reports described in paragraphs 3(ii) and 3(iii) above, if it has not already done so;
>
> ii) Conduct the sale of forest licence A19326 (the "Forest Licence") in accordance with articles 5(d), 5(e) and 5(f) of the Shareholders Agreement entered into between Maquinna Development Corporation, CFP, Maquinna Log Marketing Ltd., and Hecate and dated for reference November 16, 1987; and
>
> iii) Realize upon the assets of Hecate and distribute the proceeds therefrom and from the sale of the Forest Licence among the creditors and shareholders of Hecate, such assets to include without limitation any tax losses.

[6] The order was made pursuant to s. 324 of the *BCA* which provides as follows:

> (1) On an application made in respect of a company by the company, a shareholder of the company, a beneficial owner of a share of the company, a director of the company or any other person, including a creditor of the company, whom the court considers to be an appropriate person to make the application, the court may order that the company be

liquidated and dissolved if

(a) an event occurs on the occurrence of which the memorandum or the articles of the company provide that the company is to be liquidated and dissolved, or

(b) the court otherwise considers it just and equitable to do so.

(2) Nothing in subsection (1) prevents the court from requiring that security for costs be provided by a person bringing an application under that subsection.

(3) If the court considers that an applicant for an order referred to in subsection (1)(b) is a person who is entitled to relief either by liquidating and dissolving the company or under section 227, the court may do one of the following:

(a) make an order that the company be liquidated and dissolved;

(b) make any order under section 227(3) it considers appropriate.

(4) If the court orders under this *Act* that a company be liquidated and dissolved, the court must, in its order, appoint one or more liquidators.

(5) An appointment of a liquidator under subsection (4) takes effect on the commencement of the liquidation.

[7] As I construe the order, its effect was two-fold. Ernst & Young was appointed the receiver of Hecate's business in the period from April 28, 2006 to July 31, 2006. After July 31, 2006, Ernst & Young was to proceed, as liquidator, to liquidate Hecate. This liquidation arises out of a shareholders' dispute. This is not a proceeding under the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36 ("*CCAA*"), or the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3 (*"BIA*"). None of the parties is insolvent. The liquidation must proceed in accordance with the provisions of Division 4 of the *BCA*.

[8] The difficulty, if I may describe it as that, encountered by the liquidator is that it has been met with claims by CFPL that one or more persons, including CFPL, its affiliates, and various third parties, hold replacement logging contracts within the meaning of the *Timber Harvesting Contract and Subcontract Regulation*, B.C. Reg. 22/96 (the "Regulation"). If MFPL and MAL are parties to a contract with Hecate, or if MFPL and MAL are parties to subcontracts with third parties within the meaning of the Regulation, generally described as replaceable contracts or replaceable subcontracts to which a right of replacement attaches, then s. 33.8 of the Regulation is of concern. That section provides as follows:

33.8 A replaceable contract must provide that if the licence that the contract pertains to is transferred, the licence-holder must require, as a condition of such transfer, that the transferee either

(a) assume the licence-holder's obligation under the contract, or

(b) offer a new, replaceable contract to the contractor on substantially the same terms and conditions as the original replaceable contract.

[9] Faced with the assertion that one or more parties possesses a replaceable contract in relation to the Hecate licence, the liquidator seeks to expunge or abrogate such as might exist. The liquidator says it should be permitted to obtain the order it requests because it is empowered, as receiver or liquidator, to disclaim such rights. It says that the proceeds from the sale of the licence will be increased if it is sold free and clear of replaceable contract rights.

[10] The liquidator also says that by expunging or abrogating any replacement contract rights and replaceable subcontract rights, the relationship between EHL and CFPL will be fully and finally dissolved, that being one of the objectives in the circumstances. The liquidator says that if MFPL or MAL holds a replaceable contract and CFPL or one of its affiliates holds replaceable subcontracts, and if the burden of those contracts must pass with the licence, the relationship between EHL and CFPL will not be terminated when the licence is sold to EHL.

[11] While I understand the liquidator's objective, I am of the opinion that it does not have the right to disclaim a contract in the circumstances that surround this action.

[12] The liquidator must act in accordance with provisions of the *BCA*. Among its duties under the *BCA* are those conferred by ss. 330(d) and (l) which provide as follows:

> 330 A liquidator must
>
> ...
>
> (d) subject to this Part, use the liquidator's own discretion in realizing the assets of the company or distributing those assets among the creditors and shareholders of the company;
>
> ...
>
> (l) dispose of the assets of the company, other than assets that are to be distributed in kind to the company's shareholders, and pay or make provision for all of the company's liabilities, ...

[13] It is settled law that a receiver may disclaim a contract in proceedings under the *CCAA*: see *Clear Creek Contracting Ltd. v. Skeena Cellulose Inc.* (2003), 13 B.C.L.R. (4th) 236, 2003 BCCA 344. The purpose of the *CCAA* is to permit a company in financial difficulty to be restructured with a view to survival. Courts have grafted large amounts of flesh on to the skeleton provided by the *CCAA*. One of the rights conferred upon the monitor in such cases, is the right to disclaim contracts. Disclaimer has the effect of converting rights under an executory contract to a right to sue for damages flowing from breach of contract. The result is that the holder of rights under an executory contract is relegated to the status of unsecured creditor to share with other unsecured creditors in the financial misfortunes of the insolvent company.

[14] A similar right has been conferred upon trustees in bankruptcy acting under the *BIA*: see Houlden & Morawetz, *Bankruptcy and Insolvency Law of Canada*, 3rd ed. looseleaf (Toronto: Carswell, 2005) at 3-130.17.

[15] There is ample justification for the existence of a right to disclaim in proceedings governed by the *CCAA* or *BIA*. In both instances, the survival of a company is at stake. If survival cannot be assured, the leftovers will be divided among claimants as the company's affairs are finalized, its assets realized, and the resulting proceeds divided among claimants. It is not appropriate to suggest that a holder of contractual rights in those circumstances should be less at risk than others with claims against the company. The right of disclaimer places all unsecured claims against the company on the same footing.

[16] Counsel did not identify an instance in which a receiver/liquidator acting other than in conformity with the provisions of the *CCAA* or the *BIA* had been granted such power, subject only to the overriding discretionary control of the court. The submission of counsel is that the fact the liquidator in this case is not bound by the *CCAA* or the *BIA* is a distinction without a substantive difference and the same rule should apply. With respect, I do not agree.

[17] In the circumstances that surround this application, there is no suggestion of insolvency or financial difficulty. There is no suggestion that the claims of creditors will not be fully paid. Rather, the situation is that two shareholders of equal status cannot agree among themselves upon the manner in which the company will be operated. They are deadlocked and want the assets sold in order that they can realize upon their investment and go their separate ways. In such circumstances, I cannot see any policy reason for granting the liquidator a right of disclaimer to the prejudice of holders of contractual rights. I cannot conclude that the *BCA* was intended to require those who dealt *bona fide* with the company to assume a burden or loss because of a dispute between shareholders rather than financial difficulty by which all who deal with the company will be affected.

[18] If the liquidator wishes to sell the Hecate forest licence without the accompanying obligation to respect any replaceable contract rights, some means other than disclaimer must be found. I suggest there are alternatives.

[19] The liquidator may take steps to confirm, by application to the court under s. 325(3)(h) of the *BCA* which provides that a court may make an order determining the validity of any claims made against the company, that no replaceable contract or subcontract rights exist. If it is determined that there are no such rights, there should be no need for the kind of order sought by the liquidator on this application.

[20] If it is determined that MFPL or MAL is party to a replaceable logging contract with Hecate, then the liquidator may apply for a determination of the question of whether any subcontractor to either of those companies

holds replaceable logging subcontract rights.

[21] If it is determined that MFPL or MAL holds replaceable logging contract rights conferred by contract with Hecate, the liquidator should be in a position to terminate contracts between Hecate, MFPL, and MAL by mutual consent. Under the court order, the liquidator controls the assets of Hecate, including the shares of MFPL and MAL, ownership of which entitles him to control the conduct of MFPL and MAL. Termination of any replaceable contract between Hecate and MFPL or MAL would conform to the overall objective which is to sever the relationship between CFPL and EHL.

[22] If a replaceable logging contract exists between Hecate and MFPL or MAL, and it is determined that there are replaceable logging subcontracts with strangers to MFPL or MAL, the liquidator should be obliged to pursue the termination of those rights by negotiation, or to sell the Hecate forest licence to a purchaser who is prepared to assume the contractual obligations. There is no reason why CFPL and EHL should be in a better position with respect to replacement logging contracts or subcontracts entered into by any of Hecate, MFPL or MAL because of the dispute between CFPL and EHL than they would have been without it.

[23] The alternatives I have suggested are not meant to be exhaustive. Rather, they are intended to demonstrate that the liquidator's inability to disclaim in the present circumstances is not fatal to the overall objective, which is to terminate the business relationship between CFPL and EFL.

[24] As I indicated at the close of the hearing, the parties are at liberty to apply for the expeditious determination of the question of whether any of Hecate, MFPL or MAL is bound by any replaceable logging contract or subcontract. The liquidator is at liberty to apply for such orders as it considers necessary or appropriate under s. 325 of the *BCA.*

"I.H. Pitfield, J."
The Honourable Mr. Justice I.H. Pitfield