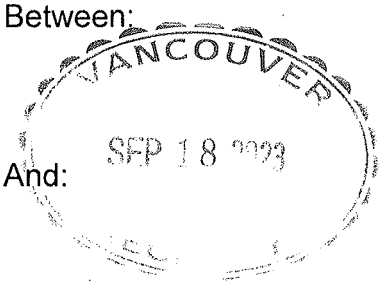
No. S236214
Vancouver Registry

In the Supreme Court of British Columbia

Between:



1392752 BC Ltd.

Petitioner

And:

Skeena Sawmills Ltd.
Skeena Bioenergy Ltd.
ROC Holdings Ltd.

Respondents

RESPONSE TO PETITION

Filed by: Delta Cedar Specialties Ltd. ("Delta Cedar" or the **"Petition Respondent")**

THIS IS A RESPONSE TO the Petition filed 8 September 2023

Part 1: ORDERS CONSENTED TO

The Petition Respondent consents to the granting of the orders set out in the paragraphs NONE of Part 1 of the Petition, subject to the comments in Part 5 of this Response to Petition.

Part 2: ORDERS OPPOSED

The Petition Respondent opposes the granting of the orders set out in paragraphs ALL of Part 1 of the Petition, subject to the comments in Part 5 of this Response to Petition.

Part 3: ORDERS ON WHICH NO POSITION IS TAKEN

The Petition Respondent takes no position on the granting of the orders set out in paragraphs NONE of Part 1 of the Petition.

Part 4: FACTUAL BASIS

Overview

1. The Petition Respondent, Delta Cedar, does not oppose the appointment of the Receiver of the Respondents, but opposes any notion that this appointment should be made on the basis that the Petitioner holds any valid security over the assets of the Respondents. In particular, the Petition Respondent wishes to challenge the validity or

enforceability of the Petitioner's security on the ground that this security constitutes a fraudulent preference and/or fraudulent conveyance. The proposed form of order states that the Receiver is to be appointed under, *inter alia*, section 243 of the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3 [*BIA*], which can only be invoked by a "secured creditor".

2. Accordingly, to the extent that the Receiver is appointed, the order should instead be made under the following conditions:

a) the appointment of the Receiver should only be made pursuant to section 39 of the *Law and Equity Act,* R.S.B.C. 1996, c. 253 [*LEA*] and Rule 10-2 of the *Supreme Court Civil Rules,* and any reference to the *BIA* should be omitted from the form of order;

b) the appointment of the Receiver should be made without prejudice to the Petition Respondent's right to challenge the Petitioner's security interests as being invalid and unenforceable as against it; and

c) other elements of the proposed receivership order should be remedied (see below).

Relationship between The Petition Respondent Delta Cedar and the Skeena Entities

3. Pursuant to a log purchase and loan agreement dated 4 October 2021 (the "**Loan Agreement**"), Skeena Sawmills Ltd. (**"Skeena Sawmills"**) owes the Petition Respondent $3,137,951.65. This debt is secured by a security agreement charging Skeena Sawmills' inventory and receivables as collateral, which security interest was perfected by registration in the Personal Property Registry on 4 October 2021. The Petition Respondent is therefore a secured creditor as against the Skeena Sawmills' inventory and receivables.

Affidavit #1 of Glen Franke, sworn 18 September 2023 ("Franke Affidavit") at paras. 2 and 3

The Financial Indebtedness of the Respondents

4. Based on their own materials, Skeena Sawmills, Skeena Bioenergy Ltd. and ROC Holdings Ltd. (the **"Skeena Entities"**) are indebted to 1392752 B.C. Ltd. (the **"Lender"**) in the amount of over $143 million. Additionally, Skeena Sawmills and Skeena Bioenergy Ltd. have over 200 other creditors combined.

Notice of Application, filed 8 September 2023 at paras. 12 and 15

5. It is apparent that the Skeena Entities have, at all material times, faced significant financial difficulties and have only continued in business with the financial assistance of the Petitioner, which made unsecured shareholder loans to the Skeena Entities of up to some $135 million. In 2023, the Skeena Entities ceased business operations, allegedly due to a lack of economic viability. In fact, the Skeena Entities never were financially viable or solvent. The Skeena Entities have exhausted their over $143 million in shareholder funding and their bank accounts are now in overdraft. Finally, the Skeena Entities are in default of some of their financial obligations, lending further credence to the impecunious financial situation of the companies.

Notice of Application at paras. 6-7 and 17-25

6. Additionally, the Petitioner/Lender admits that there are registered charges against the assets held by the Skeena Entities, including the Petition Respondent's security interest against inventory and accounts receivables.

Notice of Application at paras. 26-28

7. The Petition Respondent is currently unaware of the status of its collateral given that financial statements have not been provided to the Petition Respondent.

Franke Affidavit at para. 4

Non-Arms' Length Security Documents and Receivership Proposal

8. In its Notice of Application, the Petitioner/Lender has confirmed that it is related to the Skeena Entities. Specifically, the Petitioner/Lender and the Skeena Entities are

both controlled by Xiao Peng Cui and Shenwei Wu (the **"Shareholders"**), who are the beneficial shareholders of the Skeena Entities and the Petitioner/Lender.

Notice of Application at para. 5

9. In January 2023, the Skeena Entities and the Petitioner/Lender entered into a number of agreements, including, *inter alia,* a forbearance agreement dated 31 January 2023 (the **"Forbearance Agreement"**) and a general security agreement over all of the personal property of the Skeena Entities (the **"Unlawful Security"**), purporting to secure the following indebtedness:

a) $135,596,000 in debt owing as unsecured shareholder loans prior to the execution of the said January 2023 agreements; and

b) any future advances made thereafter by the Petitioner/Lender in order to fund the activities of the Skeena Entities.

Notice of Application at paras. 7, 10-11, and 14

10. In substance, this is a case of the left hand agreeing to give the right hand security it did not previously have as a condition for continuing to fund the operations of the Skeena Entities even though, by their own admission, the Skeena Entities had by January 2023 ceased their operations due to adverse economic conditions. The Skeena Entities only operated for a brief period of time in May and June 2023. Still, according to the Petitioner's own evidence, the Petitioner only demanded repayment of its loans on 5 September 2023, some 9 months after the Unlawful Security was granted. It is very clear from these circumstances that the Petitioner and the Skeena Entities agreed with themselves as non-arms' length related parties to give the Petitioner both security and preference/priority to which it was not entitled.

Notice of Application at paras. 17 and 34

Part 5: LEGAL BASIS

Introduction

11. There is no time at this hearing to fully argue the issues arising from the Forbearance Agreement and the Unlawful Security. This Response to Petition is intended to describe the positions that will be advanced in support of the Petition Respondent's position that the Unlawful Security is void or unenforceable as against it.

The Unlawful Security and Forbearance Agreement Constitute a Fraudulent Preference and/or a Fraudulent Conveyance

12. Sections 3 and 5 of the *Fraudulent Preference Act,* R.S.B.C. 1996, c. 164 generally provide that dispositions of property (including a grant of security) are void if the disposition is made:

a) when a person is insolvent or is unable to pay their debts in full;

b) with an intent to defeat, hinder, delay or prejudice creditors; and

c) with an intent to give the creditor preference over other creditors, such as by placing it in a better position to recover payment than it would have been if it were an unsecured creditor.

***Ocean Construction Supplies Ltd. v. Creative Prosperity Capital Corp.* (1995), 34 C.B.R. (3d.) 241**

13. Additionally, a disposition of property (including a grant of security) made to delay, hinder, or defraud creditors is void under section 1 of the *Fraudulent Conveyance Act,* R.S.B.C. 1996, c. 163.

14. In *Bossin v. Vancouver Folk Music Festival Society,* the respondent challenged the validity of a security instrument under the *Fraudulent Conveyance Act* and the *Fraudulent Preferences Act,* on the basis that the disposition was made when the respondent was insolvent and because the parties were in a close relationship. The Court found that the disposition was a fraudulent preference given that it was made at

a time when the grantor was insolvent and was made to give preference to the grantee.

***Bossin v. Vancouver Folk Music Festival Society* (1997), 74 A.C.W.S. (3d.) 506**

15. Here, the Unlawful Security furthers a fraudulent preference and/or represents a fraudulent conveyance. The grant of security of the assets of the Skeena Entities was made in circumstances where:

a) the Skeena Entities could no longer repay their debts;

b) the Petitioner/Lender was owed unsecured debt and made further advances in order to secure their debt (via the Unlawful Security) in anticipation that they would need to defeat other unsecured creditors;

c) the Unlawful Security was the product of collusion between several parties who are not at arms-length – being the Petitioner/Lender, the Skeena Entities, and the Shareholders. Given that the Shareholders controlled both companies, it was a foregone conclusion that the Shareholders would otherwise exert "pressure" on the Skeena Entities in a way that advantaged them or otherwise arrange the affairs of their various companies in a way that protected their investments; and

d) the disposition was likely made with the objective of bulwarking the Petitioner/Lender's position amongst other creditors or otherwise giving it preferential priority vis-à-vis other creditors.

16. In this case, the Skeena Entities and the Petitioner/Lender are intimately tied through the Shareholders who are the beneficial shareholders of both the Skeena Entities and the Petitioner/Lender. The Unlawful Security, under which it is now proposed to appoint the Receiver, confers an unlawful preference to a non-arms length lender.

17. In light of the foregoing, the Petition Respondent opposes the granting of receivership under the Unlawful Security or the *BIA*. Going forward, the Petition Respondent wishes to reserve its right to challenge the validity and enforceability of the Unlawful Security when the time comes for asserting priority amongst other creditors.

The Authority to Appoint a Receiver is Available in Equity

18. It is not necessary to invoke either the *BIA* (as a secured creditor) or the Unlawful Security in order to seek a court appointment of the Receiver. In these circumstances, no order should be granted that would directly or indirectly amount to a declaration of the validity of the Unlawful Security. For example, only a secured creditor can invoke section 243 of the *BIA* in order to have a receiver appointed and nothing in the order sought should somehow validate the Unlawful Security.

19. Here, given that the validity of the Unlawful Security is in dispute, the Petition Respondent does not concede that the Petitioner/Lender is a secured creditor. Until this issue has been decided, no order should be granted on the basis that the Petitioner/Lender holds a secured claim against the Skeena Entities.

20. The Receiver should instead be appointed pursuant to section 39 of the *LEA* and/or the *Supreme Court Civil Rules*, which confer a power to appoint a receiver even in circumstances where no security is in existence. Pursuant to Rule 10-2 of the *Supreme Court Civil Rules* and s. 39 of the *LEA*, a court may appoint an equitable receiver whenever it appears just and convenient to do so. Such an order may be made where ordinary attachment proceedings cannot be used.

***Clarke v. Braich*, 2021 BCSC 121 at para. 52**

21. In *Warren v. Warren,* the Court appointed an equitable receiver over the assets of a judgment debtor, notwithstanding that the plaintiff did not have any security. The court noted that the requisite circumstances existed given that the only assets held by the defendant were held by a company he controlled and that the defendant was evasive.

22. Thus, the court can appoint a receiver without any underlying security instrument when it is "just and convenient" to do so – *i.e.*, there is no requirement for the court to appoint a receiver pursuant to a security instrument. In this case, the requisite circumstances exist for the Receiver to be appointed, given that:

a) the Petition Respondent, along with the other creditors, will face significant difficulties in their ability to recoup their loans, advances, and interest given that the Skeena Entities are impecunious and there are over 200 other creditors; and

b) the appointment of a receiver will be efficient and provide cost-saving measures, in comparison to a large number of enforcement proceedings.

Objections to the Proposed Order

23. Finally, the proposed receivership order cannot be approved in the form attached to the Notice of Application. The first issue is that little or no changes have been made to the Model Order and, as a result, the proposed order contemplates the possibility that the Receiver can continue the operations of the Skeena Entities even though, according to the evidence, these operations have been shut down since the beginning of the summer of 2023. The order also contemplates an excessive amount of borrowing power without any evidence as to the "burn rate" of the operations of the Skeena Entities on a monthly basis, which should be low given that its operations have been shut down.

24. It is the Petition Respondent's submission that the receivership order should not contemplate any form of actual operation of the former business of the Skeena Entities, at least not until a first report is obtained from the Receiver as to the true financial situation of the Skeena Entities. In addition, the collateral of the Petition Respondent (the inventory and receivables of Skeena Sawmills) should be preserved and should not be used to fund operations. In addition, given that the operations of the Skeena Entities have been shut down, there should not be any obligation on the

part of any supplier (including the Petition Respondent) to continue to supply product to the Skeena Entities.

25. It follows that the following changes should be made (including some changes that are form rather than substance):

a) the order uses the word "Lands" without any definition of that word;

b) the words "Pursuant to Section 243(1) of the BIA" should be removed from paragraph 2;

c) the order should specifically state that it is made without prejudice to the right of any creditor to challenge the validity and enforceability of the Unlawful Security and that any such challenge may be brought by notice of application in this proceeding;

d) paragraphs 3(c), 3(e) and 11 of the proposed order should be removed as they contemplate that the Receiver would have the power to operate the business of the Skeena Entities;

e) a paragraph should be inserted specifically stating that the Receiver shall have no power to operate the business of the Skeena Entities and that its role will be to sell the assets and undertakings of the Skeena Entities as is, where is, without any continuation of its operations;

f) paragraph 3(i) should only be granted if the following is added thereto: ", if necessary for the effective marketing of the assets and undertakings of the Debtors";

g) paragraph 3(p) should only be granted if the following is added thereto: ", if necessary for the effective marketing of the assets and undertakings of the Debtors";

h) paragraph 12 should be modified to remove the supply of goods from the scope of that paragraph;

i) paragraph 14 should be modified to only allow for the current skeleton staff to remain employed, "as necessary for the effective marketing of the assets and undertakings of the Debtors"; and

j) paragraph 24 of the proposed order should be modified such that there is a limitation on the borrowing powers of the Receiver of $100,000, which should be sufficient to prepare a report and seek further borrowing authority, if need be.

Part 6: MATERIAL TO BE RELIED ON

26. Affidavit #1 of Glen Franke, sworn on 18 September 2023.

27. Affidavit #1 of Xiao Peng Cui, filed on 8 September 2023.

The Petition Respondent estimates that the hearing of the Petition will take one hour.

Date: 18 September 2023

Signature of lawyer for Petition Respondent
Francis Lamer

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