No. S236214
Vancouver Registry

IN THE SUPREME COURT OF BRITISH COLUMBIA

BETWEEN:

1392752 B.C. LTD.

PETITIONER

AND:

SKEENA SAWMILLS LTD.
SKEENA BIOENERGY LTD.
ROC HOLDINGS LTD.

RESPONDENTS

NOTICE OF APPLICATION

NAME OF APPLICANT: 1392752 B.C. Ltd. (the "**Applicant**")

TO: All Parties of Record

TAKE NOTICE that an application will be made by the Applicant to the presiding judge, Justice Basran, at the courthouse at **800 Smithe Street, Vancouver, B.C.** on January 25 and 26 at **9:45 a.m.**, for the orders set out in Part 1 below.

PART 1: ORDERS SOUGHT

1. A Declaration that the Grid Promissory Notes dated January 31, 2023 and May 1, 2023 (collectively, the "**Promissory Notes**") are valid and enforceable agreements in favour of the Applicant as against the Respondent, Skeena Sawmills Ltd. ("**Sawmills**"), and the amount owing by Sawmills to the Applicant pursuant to the Promissory Notes is the aggregate sum of $7,614,137.72 (the "**2023 Shareholder Loans**"), plus interest as follows:

   (a) 5% per annum, compounded monthly, on the sum of $1,432,031.72, pursuant to the Grid Promissory Note dated January 31, 2023; and

   (b) 8% per annum, compounded monthly, on the sum of $6,182,106.06, pursuant to the Grid Promissory Note dated May 1, 2023.

2. A Declaration that a joint and several guarantee dated January 31, 2023 (the "**Guarantee**") granted by the Respondents Sawmills, Skeena Bioenergy Ltd. ("**Bioenergy**") and ROC Holdings Ltd. ("**ROC**" and together with Bioenergy and Sawmills, the "**Skeena Entities**") in favour of the Applicant is a valid and enforceable guarantee by the Skeena Entities with respect to the 2023 Shareholder Loans.

3. A Declaration that the following security agreements charging the real and present and after acquired personal property (collectively, the "**Property**") of the Respondents:

   (a) an all-indebtedness Mortgage and Assignment of Rents dated January 31, 2023, granted in favour of the Applicant by ROC;

   (b) a General Assignment of Leases and Rents dated January 31, 2023 granted in favour of the Applicant by ROC; and

   (c) General Security Agreements, each dated January 31, 2023 granted in favour of the Applicant by the Skeena Entities, and registered in the British Columbia Personal Property Registry on January 10, 2023, under base registration numbers 294186P, 294187P and 294189P;

   (collectively, the "**Security**");

   are valid and enforceable agreements in favour of the Applicant to secure the 2023 Shareholder Loans.

4. A Declaration that the 2023 Shareholder Loans, including interest, are secured by the Security.

5. A Declaration that the Security ranks in priority to the interests in the Property of all persons having an interest in the Property, including the Respondents and all persons claiming by, through and under them, other than in relation to inventory, accounts receivable and any statutory claims that may have priority pursuant to one or more statutes.

6. The Applicant shall be at liberty to apply for such further Declarations that the Guarantee and the Security are valid and enforceable agreements in relation to pre-2023 advances, in whole or in part, to the Skeena Entities by the Applicant, as assignee, and that such advances are debts guaranteed by the Guarantee and/or secured by the Security.

7. Such further and other relief as counsel may advise and this Honourable Court may deem just.

PART 2: FACTUAL BASIS

The Parties

8. The Respondents, Sawmills, Bioenergy and ROC are related parties. Sawmills and Bioenergy respectively operated a sawmill and pellet plant in Terrace, British Columbia. ROC is the owner of the real property on which Sawmills and Bioenergy operated.

9. The Applicant is related to the Skeena Entities. Specifically, the Applicant and the Skeena Entities are controlled by Xiao Peng Cui and Shenwei Wu (the "**Shareholders**") who acquired the Skeena Entities approximately 12 years ago.

Cui #2, para. 2.

10. Since the Shareholders' acquisition, the Skeena Entities have suffered perennial financial losses, which were historically funded by unsecured loans provided by the Shareholders (the "**Shareholder Loans**").

Cui #2,para. 5;
T. Huang #1.

11. Ultimately, the Shareholders assigned the Shareholder Loans to the Applicant in January 2023 as part of an effort to try to rescue the Skeena Entities and put them on a sustainable financial footing. This plan included an agreement to provide further advances to Bioenergy and Sawmills.

Cui #2, paras. 6 to 9.

12. As part of this plan, in March 2023 the Skeena Entities sought advice from and engaged Alvarez & Marsal Canada Inc. ("**A&M**") to provide financial and restructuring advice.

Hu #2, paras. 3 to 4. Ex. A.

The Indebtedness owing to the Applicant

13. As set out in a Forbearance Agreement dated January 31, 2023 (the "**Forbearance Agreement**"), the Skeena Entities were indebted to the Applicant pursuant to the Shareholder Loans in the amount of $135,596,000 (the "**Indebtedness**"), payable on demand.

The January 2023 Demands

14. As a result of concerns over the Skeena Entities' debt load, ongoing operating losses and cash flow deficits, the Applicant determined that it was not in a position to maintain the status quo and, through its solicitors, issued formal demand for payment of the Indebtedness on the Skeena Entities on January 26, 2023 (the "**January 2023 Demands**").

Cui #1, Ex. A;
Cui #2, para. 5.

The Forbearance Agreement and the 2023 Shareholder Loans

15. Notwithstanding the January 2023 Demands, the Skeena Entities requested further advances from the Applicant for working capital needs. As a result of the Skeena Entities' perennial financial losses, the Applicant was not willing to provide further unsecured advances, but rather, agreed to provide the 2023 Shareholder Loans in the form of secured loans.

Cui #2, paras. 8 and 11.

16. As part of the plan to try to save the Skeena Entities, the Applicant and the Skeena Entities entered into the Forbearance Agreement, whereby the Applicant agreed to forbear from taking steps to recover the Indebtedness and agreed to advance the 2023 Shareholder Loans to cover working capital needs on the condition that the Skeena Entities provide security for the Indebtedness and the 2023 Shareholder Loans.

Cui #2, paras. 9 and 10.

17. In reliance on the Forbearance Agreement, the Applicant advanced the 2023 Shareholder Loans to Sawmills, pursuant to the Promissory Notes. As security for the 2023 Shareholder Loans, the Skeena Entities granted the Security in favour of the Applicant.

Cui #2, para. 11.

18. After consultations with A&M, Sawmills and Bioenergy seriously contemplated initiating restructuring proceedings, including a possible plan of arrangement to be proposed to its creditors under the *Companies' Creditors Arrangement Act.* However, in or around April 2023, it was ultimately decided that Sawmills and Bioenergy would pursue direct negotiations and payment and/or forbearance arrangements with key creditors.

Hu #2, paras. 5 to 7, Exs. B to C.

19. As a result of high operating costs, lack of consistent funding, weak lumber markets and an inability to access economically viable fibre, Sawmills initially closed its log scale in January 2023 and ceased operations in February 2023. Sawmills briefly re-commenced its operations in May 2023 as part of the efforts to put it on a more viable financial footing. However, it ceased operations again in or around the end of June 2023.

Hu #2, para. 4 and 8.

20. Similarly, as a result of high manufacturing costs during the winter, Bioenergy initially ceased operations in January 2023. It re-commenced operations in June 2023 as part of the efforts to put it on a more viable financial footing. However, due to the lack of fibre supplies available resulting from Sawmill's May 2023 closure, Bioenergy again ceased operations in or around the end of July 2023.

Hu #2, paras. 4 and 9.

21. All of the funds advance by or on behalf of the Applicant to Sawmills and Bioenergy were used by those entities to fund the operating expenses of Sawmills and Bioenergy, including payments to key vendors, payroll and statutory remittances. To the extent possible, Sawmills and Bioenergy always kept payments to employees as up to date and current as possible, even while juggling or delaying other financial obligations. The 2023 Shareholder Loans were not used for any other purpose beyond the business of the Skeena Entities.

Hu #2, paras. 13 to 15, Ex. E.

22. In the end, the effort to save the Skeena Entities did not succeed and the Skeena Entities defaulted on their obligations to the Applicant under the Security and the Forbearance Agreement. In particular, and in spite of the ongoing advances of the 2023 Shareholder Loans, the Skeena Entities, among other things:

    (a) failed to pay property taxes to the City of Terrace, British Columbia;

    (b) allowed various contractor liens and charges to be registered against Sawmills and Bioenergy; and

    (c) allowed creditors of the Skeena Entities to commence enforcement actions, including a garnishing order obtained by Timber Baron Contracting Ltd. and a Notice of Civil Claim filed by Canzus Consulting Ltd.

The Receivership Proceedings

23. As a result of the foregoing, the Applicant filed its petition in these proceedings on September 8, 2023, seeking to appoint A&M as receiver and manager (the "**Receiver**") over all of the property of the Skeena Entities.

24. By order pronounced September 21, 2023, this Honourable Court appointed the Receiver over all of the assets, property and undertakings of the Skeena Entities.

PART 3: LEGAL BASIS

25. On the facts set out in Part 2, above, namely that:

    (a) the Security is a valid and enforceable agreement charging the Property;

    (b) the Promissory Notes and the Guarantee are valid and enforceable agreements; and

    (c) Sawmills is indebted to the Applicant for the 2023 Shareholder Loans, with such indebtedness being evidenced by the Promissory Notes and validly secured by the Security in priority to the interest of all persons, including each of the Respondents, other than in relation to inventory, accounts receivable and any statutory claims that may have priority pursuant to one or more statutes;

    and pursuant to the terms of the Security, the Applicant is entitled to the declarations enumerated in Part 1, above.

The 2023 Shareholder Loans Are Debt and not Equity

26. The legal characterization of an advance of funds by a shareholder is a question of fact to be determined by reference to all of the surrounding circumstances. This includes circumstances beyond only the date of the advances.

Broer v. Multiguide GmbH, 2023 BCCA 134 ["_Boer_"], paras 18, 22, 25, 40, and 44 to 47.

27. Surrounding circumstances are not limited to only those circumstances at the time of the advance. Subsequent circumstances and conduct are also relevant. The court should focus on the substance of the transaction over its form and consider not just the expressed intentions of the parties as reflected in the transaction documentation, but also the manner in which the transaction was implemented and the economic reality of the surrounding circumstances.

Broer, paras 43-46

28. Key factors can include:

    (a) that shareholders advances had always been recorded in the financial statements as shareholder loans;

Broer, para 62.

(b) the absence of any ambiguity in the parties dealings over time respecting the characterization of the subject advances as loans, given the lack of any written agreement that formalized the matter; and

***Broer*, paras 53-55.**

(c) whether the parties, by way of their subsequent conduct, re-characterized the advances, or simply clarified them.

***Broer*, para 58.**

29. In analyzing the surrounding circumstances respecting both the original Shareholder Loans and, in particular, the 2023 Shareholder Loans, the Applicant submits that the court should consider that:

(a) at all material times, the parties understood that the original Shareholder Loans were shareholder loans advanced to keep the Skeena Entities operational in difficult economic circumstances;

Cui #2, paras. 7 to 10.

(b) the fact of the Shareholder Loans were always recorded in the financial consolidated statements as "loans due to the shareholder";

Hu #2, Exs. M to S.

(c) the Forbearance Agreement and Promissory Notes are written agreements that formalize a consistent understanding regarding the original Shareholder Loans as shareholder loans and, further, expressly identify the 2023 Shareholder Loans as loans, not equity investments; and

Cui #1, Exs. B to C.

(d) the 2023 Shareholder Loans were used only to fund the operations of the Skeena Entities, including payments to some of the currently objecting creditors. Beyond this and the Skeena Entities' efforts to save their business, there was no benefit to the Shareholders in making the 2023 Shareholder Loans.

Hu #2, paras 13 to 15. Ex. E.

30. The Forbearance Agreement did not re-characterize the original Shareholder Loans as something they were not prior to that. In addition, it expressly identified the 2023 Shareholder Loans as loans at the outset of those advances.

31. As a result of:

(a) the 2023 Shareholder Loans being advanced for the same reasons as the original Shareholder Loans, i.e. to keep the Skeena Entities in business; and

(b) the documents governing the 2023 Shareholder Loans (the Forbearance Agreement and Promissory Notes) being unambiguous and reflecting a typical transaction between a lender and a debtor;

the 2023 Shareholder Loans were always characterized and treated as loans, and not equity investments.

32. As set out above, the original Shareholder Loans were advanced to fund the Skeena Entities' losses and, in essence, help keep the Skeena Entities in business. As required by the Forbearance Agreement, the Applicant made the 2023 Shareholder Loans in order to cover the Skeena Entities' working capital needs and assist in keeping these companies operational in light of their difficult economic and environmental circumstances. The advances were used to pay existing and ongoing liabilities of the Skeena Entities.

33. While ultimately unsuccessful, the parties agreed to this arrangement in an effort to put Sawmills and Bioenergy on a sustainable financial footing to continue in business. Using the 2023 Shareholder Loans, both Sawmills and Bioenergy tried to recommence operations after initially shutting down. These efforts also included investigations into a CCAA process as an avenue of salvation.

Hu #2, paras. 5 to 6.

Fraudulent Preference Act

34. The *Fraudulent Preference Act*, RSBC 1996, c 164 (the "**FPA**") has no application in the present circumstances. The relevant portions of the FPA provide:

> 6(1) Nothing in sections 3, 4 and 5 applies, if the money paid, or the property disposed of bears a fair and reasonable relative value to the consideration, to a sale in good faith, to a payment made in the ordinary course of business to innocent persons, to a payment to a creditor, or to a disposition in good faith of property of any kind made in any of the following circumstances:

> (a) in consideration of a present actual payment in good faith in money;
>
> (b) by way of security for a present actual advance of money in good faith;
>
> (c) in consideration of a present actual disposition in good faith of any property.
>
> . . .
>
> (5) Nothing in this section invalidates a security given to a creditor for an existing debt if, because of the giving of the security, an advance in money is made to the debtor by the creditor in the belief in good faith that the advance will enable the debtor to continue the debtor's business and to pay the debtor's debts in full.

35. Section 6(a) of the FPA shields a transfer where it is made to a creditor: (1) in good faith, and (2) for a present actual payment. The effect of s. 6 is similar to that of s. 2 of the *Fraudulent Conveyance Act* in that it has the effect of protecting good faith dispositions for good consideration.

_Wu v. Gu_, 2020 BCSC 396, para. 98.

36. The advances under the 2023 Shareholder Loans began within days of the execution of the Forbearance Agreement and the provision of the Security. In total, the 2023 Shareholder Loans amounted to more than $7.6 million and constitute good consideration.

37. The Security is immune from attack under the FPA as a fraudulent preference because the Security was a disposition of property by the Skeena Entities in consideration of a present actual payment in good faith in money by the Applicant.

Fraudulent Conveyance Act

38. The *Fraudulent Conveyance Act*, RSBC 1996, c 163 (the "**FCA**") provides:

> 1. If made to delay, hinder or defraud creditors and others of their just and lawful remedies
>
> (a) a disposition of property, by writing or otherwise,
>
> (b) a bond,
>
> (c) a proceeding, or
>
> (d) an order

> is void and of no effect against a person or the person's assignee or personal representative whose rights and obligations are or might be disturbed, hindered, delayed or defrauded, despite a pretence or other matter to the contrary.

39. There is no need to prove "dishonest intent" in challenging a disposition as a fraudulent conveyance. The intent required to render a transfer void is only the intent to "put one's assets out of the reach of one's creditors".

***Abakhan & Associates Inc. v. Braydon Investments Ltd.*, 2009 BCCA 521, para. 65 and 73;**
***Mawdsley v. Meshen*, 2012 BCCA 91, para. 7.**

40. It must be established that there was an intent to delay, hinder or defraud creditors. An intent to defraud creditors can be established even where there may be other legitimate business purposes for the transaction.

***Mawdsley*, para. 7;**
***Braydon Investments*, paras. 85.**

41. Absent direct evidence, intent is generally inferred. Establishing intent is required as a matter of evidence because the fact that a transaction had the effect of delaying, hindering, or defrauding creditors is not, on its own, sufficient to render it a fraudulent conveyance.

***Mawdsley*, para. 7,**
***Braydon Investments*, paras. 80 and 85.**

42. Section 2 of the FCA shields transactions where the "disposition of property" was made "for good consideration and in good faith" and was "lawfully transferred to a person who, at the time of the transfer, had "no notice or knowledge of collusion or fraud."

***Fraudulent Conveyance Act*, R.S.B.C. 1996, c.163, section 2.**

43. The "collusion and fraud" that must be shared is the intent that must be proven to establish a fraudulent conveyance under section 1 of the FCA. Given the related nature of the Skeena Entities and the Applicant, it can be inferred that the Applicant was aware of the intent of the Skeena Entities given their common ownership. However, it must still be shown that the Skeena Entities had the intent required under the FCA to establish a fraudulent conveyance.

Forbearance is Good Consideration for the Security

44. Courts accept that forbearance by a creditor alone, even by implication, can be good consideration for security given for existing and future debts. This includes circumstances where the security is granted to a non-arm's length party. However, the forbearance must be real, in the sense that the creditor actually had an intention to enforce, agreed to refrain from doing so and allowed the debtor additional time to pay its existing debt. Further, the advance of additional monies under that security can underscore the *bona fides* of the transaction.

***Forjay Management Ltd. v. 0981478 B.C. Ltd.*, 2023 BCSC 1368, paras 159 -160;**
***Montor Business Corporation v. Goldfinger,* 2016 ONCA 406, para 56.**

45. On the issue of the inadequacy of consideration, the test has variously been expressed as "so palpable that it must be taken to have been a fraudulent contrivance" and "gross inadequacy". Good consideration is "valuable consideration" or more than nominal consideration.

***Chan v. Stanwood*, 2002 BCCA 474, para. 19 and 20.**

46. The forbearance provided by the Applicant, as set out in the Forbearance Agreement, was real and is good consideration for the Security, notwithstanding that the Applicant and the Skeena Entities are non-arm's length parties.

47. Further, the Applicant made new advances totally over $7.6 million by way of the 2023 Shareholder Loans in reliance on the Security.

48. As a result of the forbearance, the Skeena Entities were given time to try to get their business on a viable and sustainable financial footing. They sough the assistance of A&M to do so. They entered good faith negotiations and signed some forbearance agreements with various creditors as part of this effort.

Hu #2, paras. 5 to 7.

49. Among other things, the 2023 Shareholder Loans also allowed both Sawmills and Bioenergy to restart operations for a few months after both had shut down in early 2023. They also allowed the payment of current creditors, including a number now objecting to the Security as a preference.

Hu #2, paras. 8 to 9 and 13 to 14. Ex. E.

50. Further, as evidenced by the ultimate commencement of these receivership proceedings, the Applicant clearly had an intention to pursue its debt and agreed to refrain from doing so in January 2023 to allow the Skeena Entities additional time to address their financial difficulties and the viability of the businesses.

Intent and Severability of Security for future Advances

51. The Applicant advanced in excess of $7.6 million to the Skeena Entities after being provided the Security. This is "good consideration" within section 2 of the FCA as that amount cannot be described as "grossly inadequate" or "so palpable as to be a fraudulent contrivance". It is "more than nominal consideration". For this reason, the Security cannot be a fraudulent conveyance because the consideration flowing back to the Skeena Entities, the $7.6 million, had clear and adequate value.

52. If the Applicant were seeking to prove the validity, enforceability and priority of the Security for the Shareholder Loans advanced before 2023, then the issue of the intent of the Skeena Entities in providing security for those past advances would be relevant to the present application.

53. However, that is not the question on the present application because the Applicant only seeks declaratory relief with respect to the 2023 Shareholder Loans. These advances were all made after January 2023 and pursuant to the Forbearance Agreement, the Promissory Notes and the Security.

54. When assessing whether the security granted for subsequent advances is a preference, the courts treat the nature of that security differently, and severable, when considering the issue of a possible fraudulent preference or conveyance. This is consistent with the purposes of the FPA and the FCA to protect good faith dispositions for valuable consideration, even among related entities.

55. Where a present advance is made on the eve of insolvency, it cannot be attacked as a preference, even where the person making the advance is already a creditor. Security obtained for a present advance will not be treated as a preference.

***In re British Columbia Bond Corporation Limited and Lang*, (1931) 12 C.B.R. 213 (B.C.S.C.), para. 4**
***Re Goldstein*, (1922) 3 C.B.R. 404 (On. S.C.), para. 7-8;**
***Candie Maid Ltd., Re*, 1975 CarswellOnt 82 (Ont. S.C.), para. 9.**

56. In cases where security for past debts is challenged as a preference, the secured creditor is nonetheless entitled to priority for advances made after the date of the security was given where those advances were used by the debtor to pay existing financial obligations.

***Anglin v. Rosen*, [1957] SCR 755, at 763 and 767.**

57. The existence of other legitimate reasons for a transaction, and the exchange of good consideration, can vitiate the inference of intent to put property out of the reach of creditors.

***Balfour v. Tarasenko*, 2019 BCSC 2212, para. 64.**

58. In the present circumstances, the 2023 Shareholder Loans were advances in good faith by the Applicant in compliance with its obligations under the Forbearance Agreement and in reliance on the Security. At the time the advances were made, there was a plan by the Skeena Entities to try to get themselves onto a viable financial footing. The 2023 Shareholder Loan advances were used to try to re-start the operations of Skeena and Bioenergy. The advances were also used to pay other existing creditors to allow for continued operation.

59. The fact that this plan ultimately failed, leading to this receivership, does not detract from fact of the underlying intent in granting the Security in January 2023, certainly with respect to the 2023 Shareholder Loans which are the only debts in issue on this application.

60. The intent of the Skeena Entities in granting the Security in exchange for the advances made as the 2023 Shareholder Loans was not "an intent to delay, hinder or defraud creditors" The granting of the Security does not run afoul of the FCA as a fraudulent conveyance, certainly with respect to the 2023 Shareholder Loans.

61. There was no other business objective of the Skeena Entities beyond trying to save their businesses that points to an intent to defraud its other creditors or favour the Applicant above them.

62. For all these reasons, the Security represents valid and enforceable agreements that secure and give priority to the 2023 Shareholder Loans. The declarations sought by the Applicant ought to be granted.

PART 4: MATERIAL TO BE RELIED ON

63. Receivership Order pronounced September 21, 2023

64. First Report of the Receiver dated October 25, 2023.

65. Second Report of the Receiver dated December 13, 2023.

66. Affidavit #1 of Xiao Peng Cui, made September 8, 2023.

67. Affidavit #2 of Xiao Peng Cui, made January 3, 2024.

68. Affidavit #1 T. Huang, made December 20, 2023.

69. Affidavit #1 of J. Hu, made September 19, 2023.

70. Affidavit #2 of J. Hu, made January 5, 2024.

71. Affidavit #1 of C. Conto, made January 3, 2024.

The applicant estimates that the application will take **two (2) days.**

☐ This matter is within the jurisdiction of a Master.

☒ This matter is not within the jurisdiction of a Master as it involves inherent jurisdiction

TO THE PERSONS RECEIVING THIS NOTICE OF APPLICATION: If you wish to respond to this Notice of Application, you must, within 5 business days after service of this Notice of Application or, if this application is brought under Rule 9-7, within 8 business days after service of this Notice of Application:

(a) file an Application Response in Form 33,

(b) file the original of every affidavit, and every other document, that

(i) you intend to refer to at the hearing of this application, and

(ii) has not already been filed in the proceeding, and

(c) serve on the applicant 2 copies of the following, and on every other party of record one copy of the following:

(i) a copy of the filed Application Response;

(ii) a copy of each of the filed affidavits and other documents that you intend to refer to at the hearing of this application and that has not already been served on that person;

(d) if this application is brought under Rule 9-7, any notice that you are required to give under Rule 9-7(9).

Dated at the City of Vancouver, in the Province of British Columbia, this 5th day of January 2024.

Lawson Lundell LLP
Solicitors for the Applicant

This Notice of Application is filed by the law firm of Lawson Lundell LLP, whose place of business and address for delivery is 1600 – 925 West Georgia Street, Vancouver, British Columbia, V6C 3L2.

To be completed by the court only:

Order made

☐ in the terms requested in paragraphs _____ of Part 1 of this Notice of Application

☐ with the following variations and additional terms:

_____

_____

Date: _____

Signature of ☐ Judge ☐ Master