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June 5, 2006

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SENT VIA MESSENGER AND EMAIL

Ontario Securities Commission
Suite 1800
20 Queen Street West
P.O. Box 55
Toronto, ON M5H 3S8

Attention: The Secretary to the Commission

Dear Sirs:

Offer of SHLD Acquisition Corp. ("SHLD"), a wholly-owned subsidiary of Sears Holdings Corporation ("Sears Holdings"), to purchase all of the outstanding common shares (the "Offer") of Sears Canada Inc. ("Sears Canada")

Application under sections 104 and 127 of the *Securities Act* (Ontario)

We are the solicitors for Sears Holdings and SHLD (collectively, the "Applicants").

The Applicants hereby apply for relief under sections 104 and 127 of the *Securities Act* (Ontario) (the "Act") in respect of the conduct of Pershing Square Capital Management, L.P. ("Pershing") and its joint actors, including, but not limited to, Knott Partners Management LLC ("Knott Partners") and Hawkeye Capital Management, LLC ("Hawkeye") in connection with the Offer. In particular, the Applicants seek the following relief from the Commission:

1. an order that Pershing and its joint actors be reprimanded;

2. an order requiring that Pershing and its joint actors comply with Part XX and the regulations related to Part XX by selling into the market by July 31, 2006, the common shares of Sears Canada each of them purchased during the period in which they were required to disclose their position as joint actors under Part XX of the Act and failed to do so;

3. an order requiring that Pershing and its joint actors be prohibited from acquiring any further common shares of Sears Canada;

4. in the alternative, an order directing that the votes attached to any common shares of Sears Canada owned or controlled by Pershing and its joint actors be excluded in determining whether minority approval of any subsequent acquisition

transaction in connection with the Offer has been obtained pursuant to Rule 61-501; and

5. such further and other order as the Commission deems appropriate and in the public interest.

Overview of Applicants' Position

1. It is the Applicants' position that Pershing and its joint actors, including, but not limited to, Knott Partners and Hawkeye, have violated sections 101 and/or 102, 126.1 and 126.2 of the Act and have engaged in abusive minority tactics contrary to the public interest. In particular,

   (a) Pershing and its joint actors acquired beneficial ownership of common shares of Sears Canada during the Offer period and failed to comply with the early warning disclosure requirements under sections 101 and/or 102 of the Act;

   (b) Pershing issued a news release with respect to its acquisition of common shares of Sears Canada during the Offer period that failed to comply with the requirements of section 198 of the Regulations and contained material misrepresentations contrary to section 126.2 of the Act;

   (c) Pershing and its joint actors have engaged in a course of conduct that they knew, or reasonably ought to have known, would result in an artificial price for the common shares of Sears Canada contrary to section 126.1 of the Act by secretly acquiring shares during the Offer period and by orchestrating carefully calculated and unattributed press coverage for the purpose of maintaining the price of Sears Canada common shares above the Offer price; and

   (d) Pershing and its joint actors have engaged in abusive minority tactics by, among other things, seeking to "park" 6.9 million common shares of Sears Canada that are the subject of total return swaps with Sun Trust Capital Markets ("Sun Trust") (the "Pershing/Sun Trust Swaps") with the understanding that:

      (i) the Pershing/Sun Trust Swaps could be unwound and the 6.9 million shares returned to Pershing; and

      (ii) the votes attached to the 6.9 million common shares would be voted as directed by Pershing or would not be voted at all.

2. The Applicants state that, having entered into the Pershing/Sun Trust Swaps with the understanding that the shares subject to the swaps remained under their direction or control, Pershing, together with its joint actors, engaged in abusive minority tactics, including the violations of Ontario securities laws described above, by secretly acquiring shares in an attempt to thwart the Offer and any subsequent acquisition transaction. The conduct of Pershing and its joint actors warrants the granting of the relief sought in this application under sections 104 and 127 of the Act.

The Parties

3. Sears Holdings is the United States' third largest broadline retailer, with approximately $55 billion in annual revenues. Sears Holdings is the leading home appliance retailer as well as a leader in tools, lawn and garden, home electronics and automotive repair and maintenance. Prior to the announcement of the Offer, Sears Holdings held 57,732,517 common shares of Sears Canada, representing approximately 53.8% of the outstanding common shares.

4. SHLD is a wholly-owned subsidiary of Sears Holdings. SHLD was incorporated for the sole purpose of making the Offer.

5. Pershing is a New York-based hedge fund. From Pershing's public disclosure, it appears that Pershing currently holds 5,601,400 common shares of Sears Canada, acquired during the Offer period, representing approximately 5.2% of the outstanding shares. Pershing has also publicly disclosed that it is entitled to the economic benefit of an additional 6.9 million common shares of Sears Canada pursuant to the Pershing/Sun Trust Swaps.

6. Hawkeye and Knott Partners are also New York-based hedge funds. From their public disclosure, it appears that Hawkeye holds 1,525,872 common shares of Sears Canada (representing approximately 1.4% of the outstanding shares) and Knott Partners holds 1,114,300 common shares of Sears Canada (representing 1.0% of the outstanding common shares), all of which were acquired during the Offer period.

7. Pershing, Hawkeye and Knott Partners collectively own or control approximately 7.7% of the outstanding common shares.

Chronology

8. On November 17, 2004, Sears, Roebuck and Co. ("Sears Roebuck") and Kmart Holding Corporation ("Kmart") announced that they had entered into a merger agreement.[1] The day prior to that announcement, the closing price of the common shares of Sears Canada was $17.43 per share. The merger was completed on March 24, 2005.

9. In their public disclosure, Pershing has stated that it commenced acquiring shares of Sears Canada in early-2005.

10. On June 13, 2005, Sears Canada announced that it would consider strategic alternatives for its credit and financial services business (the "Credit Card Business")[2] and shortly thereafter began a process to sell the Credit Card Business. Sears Holdings was a strong supporter of the sale of the Credit Card Business over the initial resistance of certain of the independent directors of Sears Canada, as well as supporting the distribution of most of the cash proceeds of the sale to Sears Canada shareholders, again over the initial resistance of certain of the independent directors.

11. On August 31, 2005, Sears Canada announced that it had entered into an agreement to sell the Credit Card Business for net proceeds of $2.2 billion[3] and, on September 14, 2005, announced that it proposed to distribute approximately $2 billion of the proceeds to its shareholders.[4] After the announcement of the distribution, the trading price of the Sears Canada shares increased to over $30 per share.

12. Following the announcement of the distribution of the proceeds of the sale of the Credit Card Business, Pershing entered into the Pershing/Sun Trust Swaps with respect to 6.9 million common shares of Sears Canada (representing approximately 6.4% of the outstanding shares) in order to not be subject to Canadian withholding tax on the distribution. It is evident from the public

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[1] A copy of the Sears Roebuck press release dated November 17, 2004 is attached as Tab "A" to this Application.

[2] A copy of the Sears Canada press release dated June 13, 2005 is attached as Tab "B" to this Application.

[3] A copy of the Sears Canada press release dated August 31, 2005 is attached as Tab "C" to this Application.

[4] A copy of the Sears Canada press release dated September 14, 2005 is attached as Tab "D" to this Application.

statements of Mr. William Ackman, the managing partner of Pershing, that Pershing understood that:

(i) the Pershing/Sun Trust Swaps could be unwound and the 6.9 million shares returned to Pershing; and

(ii) the votes attached to the 6.9 million common shares would be voted as directed by Pershing or would not be voted at all.

13. On December 2, 2005, Sears Canada declared a share distribution comprised of $18.64 per share, consisting of a return of capital of $4.38 per share and an extraordinary cash dividend of $14.26 per share.[5]

14. On December 5, 2005, Sears Holdings issued a press release announcing its intention to make the Offer at a price of $16.86 per share, an 8.7% premium over the most recent closing price and a 22.2% premium over the average closing price since August 31, 2005.[6] The Offer price of $16.86 per share was established after the declaration of the distribution of $18.64 per share arising from the sale of the Credit Card Business (i.e. shareholders who received the Offer price and the $18.64 distribution would effectively receive $35.50 per share). The effective price of $35.50 represented an increase of approximately 100% from the price of the shares at the time of the announcement of the Sears Roebuck /Kmart merger.

15. In the same press release, Sears Holdings also announced that it had entered into a lock-up agreement with Natcan Investment Management Inc. ("Natcan"), Sears Canada's largest minority shareholder. Natcan, a sophisticated investor, agreed to tender all 9,699,862 common shares that it owned or controlled to the Offer, representing approximately 9.06% of the outstanding common shares of Sears Canada.

16. On February 9, 2006, SHLD mailed the Offer to shareholders of Sears Canada.[7] The Offer was scheduled to expire on March 17, 2006. In the Offer, Sears Holdings stated its intention to pursue a subsequent acquisition transaction to

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[5] A copy of the Sears Canada press release dated December 2, 2005 is attached as Tab "E" to this Application.

[6] A copy of the Sears Holdings press release dated December 5, 2005 is attached as Tab "F" to this Application.

[7] A copy of the Sears Holdings press release dated February 9, 2006 announcing that it had mailed the Offer is attached as Tab "G" to this Application.

acquire all of the remaining minority shares not tendered to the Offer at the same price offered under the Offer (the "Subsequent Acquisition Transaction").

17. On February 28, 2006, in an article in the *Daily Deal*, Mr. Scott Stuart reported that "Pershing Square Management LP, whose head, Bill Ackman is a seasoned real estate investor, now owns 4.9%" of the common shares of Sears Canada".[8] Pershing's ownership of 4.9% of the common shares was repeated by Mr. Stuart in an article in the *Daily Deal* dated March 16, 2006.[9] Similarly, in the March 17, 2006 edition of *The Globe and Mail*, Ms. Marina Strauss reported that Pershing held 5.3 million common shares of Sears Canada (representing approximately 4.9% of the outstanding common shares).[10]

18. However, according to the letter from Davies Ward Phillips & Vineberg LLP ("DWPV"), the solicitors for Pershing, Hawkeye and Knott Partners, to the Commission dated May 25, 2006, Pershing did not commence acquiring shares of Sears Canada until March 16, 2006.[11] Accordingly, either these news reports were mistaken or Pershing began acquiring common shares of Sears Canada prior to March 16, 2006, contrary to its representations to the Commission. In the event that the news reports were incorrect, Pershing was the likely source of the information, either directly or indirectly.

19. In the event that Pershing did commence acquiring Sears Canada on March 16, 2006, the timing of the purchases (on the day before the Offer was initially scheduled to expire) strongly suggests that the purpose of Pershing in acquiring the shares was to ensure that the price of Sears Canada shares did not fall below the Offer price. Maintaining the price in the market above the Offer price would create a disincentive to other Sears Canada shareholders from tendering into the Offer. In addition, following its acquisition of Sears Canada shares, Pershing did not issue a press release pursuant to section 102 of the Act, notwithstanding that it understood that it had "parked" the votes attached to the 6.9 million shares subject to the Pershing/Sun Trust Swaps (which, together with any shares acquired by Pershing on March 16, 2006, would represent more than 5% of the outstanding shares of Sears Canada).

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[8] A copy of the February 28, 2006 article in the *Daily Deal* is attached as Tab "H" to this Application.

[9] A copy of the March 16, 2006 article in the *Daily Deal* is attached as Tab "I" to this Application.

[10] A copy of the March 17, 2006 article in the *Globe and Mail* is attached as Tab "J" to this Application.

[11] A copy of the letter from DWPV dated May 25, 2006 is attached as Tab "K" to this Application.

20. On the same date that Pershing states that it commenced acquiring shares of Sears Canada, in an article in the *National Post*, Mr. Ronald Mayers, head of alternative strategies at Desjardins Securities is quoted as stating that: "These guys [Sears Holdings] are just not going to get it this time around... They just aren't. *We have done an informal enough count*".[12] (Emphasis added.) As described in greater detail below, the Applicants state that Pershing supported and reinforced its efforts to maintain an artificial price for the shares by making selective and unattributed disclosure of "information" to analysts and reporters, either directly or through Mr. Mayers, for the purpose of obtaining press coverage, based on misleading and/or incomplete information supplied by Pershing, suggesting to Sears Canada shareholders that a higher offer price was inevitable and to discourage shareholders from tendering their shares to the Offer.

21. On March 20, 2006, Sears Holdings announced that SHLD had taken up 10,161,968 common shares pursuant to the Offer and that it had extended the Offer to March 31, 2006.[13]

22. On April 3, 2006, Sears Holdings announced that SHLD had increased the price under the Offer to $18.00 per share and that SHLD had entered into a deposit agreement with Vornado Realty L.P. ("Vornado") pursuant to which Vornado agreed to tender all 7,500,000 common shares it owned or controlled to the Offer.[14] Sears Holdings further announced that SHLD had extended the Offer to April 18, 2006 and that it continued to discuss entering into support agreements at the revised price of $18.00 per share with certain shareholders of Sears Canada who together owned sufficient shares to assure Sears Holdings that it would obtain a majority of the minority shares in the Subsequent Acquisition Transaction. The press release stated that Sears Holdings believed that agreements at the revised offer price would be reached and announced during the extension period.

23. The following day, in an article by Ms. Strauss in the April 4, 2006 edition of *The Globe and Mail*, Mr. Mayers is reported to have stated, based on his consultations with other shareholders of Sears Canada, that "It is really close... Despite all of the hissing and spitting that's going on, I think this transaction gets done at

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[12] A copy of the March 16, 2006 article in the *National Post* is attached as Tab "L" to this Application.

[13] A copy of the Sears Holdings press release dated March 20, 2006 is attached as Tab "M" to this Application.

[14] A copy of the Sears Holdings press release dated April 3, 2006 is attached as Tab "N" to this Application.

$19.50." [15] Mr. Mayers also referred to "nasty stuff going on behind the scenes". The same article states that a spokesman for Pershing had confirmed to Ms. Strauss that it would be "holding out for more". The Applicants note that it was also Ms. Strauss who reported on March 17, 2006, that Pershing held approximately 4.9% of the common shares. Her April 4, 2006 article makes it clear that she was in contact with Pershing.

24. Then, in the April 5, 2006 edition of *The Globe and Mail*, Mr. Mayers is reported to have made the following statements:[16]

> *Investors owning 22 million shares say they won't accept the bid of $18.00 a share, or $899 million, Ron Mayers, head of alternative strategies at Desjardins said yesterday...*The results indicate Sears Holdings may have to raise the price a second time, Mr. Mayers said. (Emphasis added.)

The Globe and Mail article did not state how Mr. Mayers came to have the knowledge of the position of the holders of the 22 million shares in respect of the Offer.

25. On April 6, 2006, Sears Holdings announced that SHLD had entered into support agreements with shareholders of Sears Canada who had committed to vote an aggregate of 7,611,000 common shares in favour of the Subsequent Acquisition Transaction expected to close in December 2006 at the Offer price of C$18.00 per share.[17] The press release also stated that:

> Giving effect to the 10,209,246 common shares purchased previously in the offer, the 7,500,000 common shares committed and tendered by Vornado Realty, L.P., and the support commitments for 7,611,000 common shares announced today, Sears Holdings and its affiliates have acquired in the offer or obtained commitments for an aggregate of 25,320,246 common shares, representing over 50% of the common shares (including Deferred Shares Units and unexercised options) that were not owned by Sears Holdings and its affiliates at the commencement of the offer. *Accordingly, Sears Holdings and its affiliates will own or have support commitments for sufficient shares to assure the necessary shareholder approval of a going private transaction of Sears Canada at the offer price of C$18.00 per share.* (Emphasis added.)

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[15] A copy of the April 4, 2006 article in *The Globe and Mail* is attached as Tab "O" to this Application.

[16] A copy of the April 5, 2006 article in *The Globe and Mail* is attached as Tab "P" to this Application.

[17] A copy of the Sears Holdings press release dated April 6, 2006 is attached as Tab "Q" to this Application.

The press release also announced that the Offer had been extended until August 31, 2006.

26. According to the letter from DWPV to the Commission dated May 25, 2006, on April 6, 2006, after Sears Holdings' announcement, Pershing acquired further shares of Sears Canada in the market. Again, the Applicants believe that the purpose of Pershing acquiring the shares was to ensure that the price of Sears Canada shares would not fall below the Offer price (which would otherwise be the expected result of Sears Holdings' announcement that it had received commitments from Sears Canada shareholders which, when aggregated with shares acquired or agreed to be tendered to the Offer, were sufficient for Sears Holdings to obtain approval of the Subsequent Acquisition Transaction).

27. On April 7, 2006, Pershing issued a press release which disclosed that Pershing held 5,601,400 common shares of Sears Canada, representing approximately 5.2% of the issued and outstanding common shares.[18] This was the first time that Pershing publicly and formally disclosed its holdings in Sears Canada, notwithstanding that it had been secretly acquiring shares, by its own admission, since March 16, 2006. The press release also disclosed, again for the first time, that Pershing was entitled to the "economic benefit of an additional 6,900,000 (approximately 6.4% of the outstanding) common shares of Sears Canada under cash-settled derivative transactions that terminate in December 2006, with a resulting economic interest equal to 11.6% of the outstanding common shares of Sears Canada". The press release issued by Pershing was deficient and misleading because it did not state the purpose of Pershing in acquiring the additional shares. As stated above, the Applicants believe that the purpose of Pershing in acquiring the shares was to manipulate the price of Sears Canada shares and ensure that it did not fall below the Offer price.

28. In addition, Pershing did not disclose in its April 7, 2006 press release whether it intended to make future purchases of common shares of Sears Canada; however, in the April 12, 2006 edition of the *Wall Street Journal*, which included direct quotes from Mr. Ackman, it was reported that Mr. Ackman had "scrambled to unwind his swap agreement in order to recapture the voting rights" attached to the 6.9 million common shares.[19] If Pershing, in fact, had disposed of legal and beneficial ownership of the shares subject to the Pershing/Sun Trust Swaps, any attempt to unwind the swaps on or after April 7, 2006 clearly demonstrated an

[18] A copy of the Pershing press release dated April 7, 2006 is attached as Tab "R" to this Application.

[19] A copy of the April 12, 2006 article in the *Wall Street Journal* is attached as Tab "S" to this Application.

intention on the part of Pershing to acquire the 6.9 million common shares subject to the swaps. However, Pershing was unable to unwind the Pershing/Sun Trust swaps.

29. The same *Wall Street Journal* article quoted Mr. Ackman's statement of his clear understanding that the shares subject to the Pershing/Sun Trust Swaps would not be voted in the Subsequent Acquisition Transaction:

> It is the convention in the swap market for a swap dealer to abstain from voting for corporate actions of any kind.

Pershing therefore clearly understood that, as a result of entering into the Pershing/Sun Trust Swaps, it had "parked" 6.9 million common shares of Sears Canada, and removed the shares from the pool of minority shares that would be tendered to the Sears Holdings offer or voted in favour of the Subsequent Acquisition Transaction, thereby making it much more difficult for Sears Holdings to achieve minority approval.

30. On April 17, 2006, during the Good Friday/Passover holiday, Pershing, Hawkeye and Knott Partners jointly announced that they had formed a group that intended "to take all appropriate legal action to halt" Sears Holdings' acquisition of the remaining minority shares.[20] The April 17 press release discloses that Pershing, Hawkeye and Knott collectively owned 8,241,572 Common Shares or approximately 7.7% of the outstanding Common Shares.

31. The Applicants believe that Pershing, Hawkeye and Knott Partners were acting jointly or in concert with respect to the Offer prior to April 17, 2006, together with other shareholders of Sears Canada. The Applicants believe that Mr. Mayers obtained his information with respect to the position of the holders of the 22 million shares (as reported in the April 5, 2006 edition of *The Globe and Mail*) from communications with Pershing, Hawkeye and/or Knott Partners. It appears clear from subsequent articles in the press that Pershing was communicating its intentions with respect to the Offer to Mr. Mayers and using him to disseminate that information to the market through the media. For example, in the April 7, 2006 edition of *The Globe and Mail*, Mr. Mayers is reported to have stated, prior to Pershing issuing its press release on April 7, 2006 stating that it intended to exercise all of its legal rights with respect to the shares, that:[21]

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[20] A copy of the Pershing, Hawkeye and Knott Partners' press release dated April 17, 2006 is attached as Tab "**T**" to this Application.

[21] A copy of the April 7, 2006 article in *The Globe and Mail* is attached as Tab "U" to this Application.

> 'I think there's another shoe yet to drop', said Ron Mayers at Desjardins Securities Inc. and a shareholder of Sears Canada. He said shareholders could launch an oppression lawsuit, or invoke dissenters' rights, to force a change.

The identity of the other shareholders in the "22 million share group" is unknown to the Applicants because such knowledge resides with Pershing and its joint actors and Mr. Mayers.

32. As described in more detail below, it is the Applicants' position that the conduct of Pershing and its joint actors, including, but not limited to, Knott Partners and Hawkeye, has violated sections 101 and/or 102, 126.1 and 126.2 of the Act and constitutes abusive minority tactics contrary to the public interest.

Violations of Section 101 and/or 102 of the Act

Sections 101 and 102 of the Act

33. Section 101 of the Act provides that:

> **101.** (1) Every offeror that acquires beneficial ownership of, or the power to exercise control or direction over, or securities convertible into, voting or equity securities of any class of a reporting issuer that, together with such offeror's securities of that class, would constitute 10 per cent or more of the outstanding securities of that class,
>
> (a) shall issue and file forthwith a news release containing the information prescribed by the regulations; and
>
> (b) within two business days, shall file a report containing the same information as is contained in the news release issued under clause (a).
>
> (2) Where an offeror is required to file a report under subsection (1) or a further report under this subsection and the offeror or any person or company acting jointly or in concert with the offeror acquires beneficial ownership of, or the power to exercise control or direction over, or securities convertible into, an additional 2 per cent or more of the outstanding securities of the class or there is a change in any other material fact in such a report, the offeror,
>
> (a) shall issue and file forthwith a news release containing the information prescribed by the regulations; and
>
> (b) within two business days, shall file a report containing the same information as is contained in the news release issued under clause (a)

> (3) During the period commencing on the occurrence of an event in respect of which a report or further report is required to be filed under this section and terminating on the expiry of one business day from the date that the report or further report is filed, neither the offeror nor any person or company acting jointly or in concert with the offeror shall acquire or offer to acquire beneficial ownership of any securities of the class in respect of which the report or further report is required to be filed or any securities convertible into securities of that class.
>
> (4) Subsection (3) does not apply to an offeror that is the beneficial owner of, or has the power to exercise control or direction over, securities that, together with such offeror's securities of that class, constitute 20 per cent or more of the outstanding securities of that class.

34. Section 102 of the Act provides that:

> **102.** (1) Where, after a formal bid has been made for voting or equity securities of an offeree issuer that is a reporting issuer and before the expiry of the bid, an offeror, other than the person or company making the bid, acquires beneficial ownership of, or the power to exercise control or direction over, securities of the class subject to the bid which, when added to such offeror's securities of that class, constitute 5 per cent or more of the outstanding securities of that class, the offeror shall, not later than the opening of trading on the next business day, issue a news release containing the information prescribed by the regulations and, forthwith, the offeror shall file a copy of the news release.

The Shares Subject to the Pershing/Sun Trust Swaps

35. Pershing entered into the Pershing/Sun Trust Swaps with respect to 6.9 million common shares of Sears Canada in December 2005. It is clear from Mr. Ackman's statements reported in the April 12, 2006 edition of the *Wall Street Journal* that Pershing understood that:

(i) the Pershing/Sun Trust Swaps could be unwound and the 6.9 million shares returned to Pershing; and

(ii) in any Subsequent Acquisition Transaction, the votes attached to the 6.9 million common shares would be voted as directed by Pershing or would not be voted at all.

36. Based on the clear understanding of Pershing that it retained the power to exercise control or direction over the 6.9 million shares, Pershing was required to comply with the early warning disclosure requirements of section 102 of the Act once it acquired any shares of Sears Canada during the Offer period (as any purchase of Sears Canada shares would, together with the 6.9 million common shares subject

to the Pershing/Sun Trust swaps, exceed 5% of the outstanding common shares of Sears Canada).

37. Pershing did not make any such disclosure notwithstanding that, by its own representations to the Commission, it commenced purchasing common shares of Sears Canada during the Offer period as early as March 16, 2006.

38. In addition, given that Pershing purchased an additional 5,601,400 shares of Sears Canada during the Offer period, which, taken together with the 6.9 million shares subject to the Pershing/Sun Trust Swaps, represented more than 10% of the outstanding common shares of Sears Canada, Pershing was also required to comply with the disclosure requirements set out in section 101 of the Act. Pursuant to section 101(3) of the Act, Pershing was prohibited from acquiring any further common shares of Sears Canada once it exceeded the 10% threshold prescribed in section 101 until it had made the required disclosure. No such disclosure was made and Pershing continued to acquire shares of Sears Canada in the market until it reached the level of its current holdings, in violation of section 101(3).

39. Further, prior to entering into the Pershing/Sun Trust Swaps in order not to be subject to Canadian withholding tax, Pershing held 6.9 million shares, representing approximately 6.4% of the outstanding Sears Canada shares. The Applicants believe Pershing was acting jointly or in concert with other shareholders prior to entering into the Pershing/Sun Trust Swaps and held, together with such joint actors, more than 10% of the outstanding Sears Canada shares, for which no disclosure under section 101 of the Act was made.

40. The relief sought of requiring Pershing and its joint actors to dispose of their shares acquired in violation of sections 101 and/or 102 of the Act is justified. For example, in December 1998, in connection with the take-over bid by Torstar Corporation for Sun Media Corporation ("Sun Media"), Quebecor Inc. ("Quebecor") issued a press release announcing that it was reversing certain purchases of Sun Media made during the offer period to reduce its holdings of Sun Media to below 5%. Although not stated in the press release, the reason for the reversal of the trades was that Quebecor had failed to comply with the early warning disclosure requirements contained in section 102 in respect of its purchases.[22] Similarly, in December 2000, Trilogy Retail Enterprises L.P. ("Trilogy"), which had made an unsolicited bid for Chapters Inc. ("Chapters"), announced that it had cancelled trades in shares of Chapters which it had acquired in violation of section 101(3) of the Act.

[22] *Securities Law and Practice*, 3rd ed. at §20.16.1 (p. 20-171)

The April 7th Press Release Violates Section 198 of the Regulations

41. The April 7, 2006 press release of Pershing announcing that it had acquired more than 5% of the shares of Sears Canada was deficient in that it did not disclose either the purpose of Pershing in acquiring the common shares during the Offer period or its intention to acquire further common shares of Sears Canada.

42. Section 198 of the Regulations sets out what is required to be included in any press release issued under section 102 of the Act:

> **198.** A press release required under section 102 of the Act shall be authorized by a senior officer of the offeror and shall include in respect to the class of securities subject to the bid and each class of securities into which the securities of the class are subject to the bid are convertible,
>
> (a) the name of the offeror issuing the release;
>
> (b) the number of securities acquired by or over which the offeror and every person acting jointly or in concert with the offeror has acquired control or direction since the commencement of the bid;
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> (c) the number of securities held by or over which the offeror and every person acting jointly or in concert with the offeror exercised control or direction after the transaction or occurrence giving rise to the press release;
>
> (d) the market where the transaction or occurrence took place; and
>
> (e) the purpose of the offeror and any person acting jointly or in concert with the offeror in effecting the transaction, including any future intention to increase the beneficial ownership, control or direction of the offeror and any person acting jointly or in concert with the offeror over securities of the offeree issuer.

43. The April 7, 2006 press release issued by Pershing is completely silent on the purpose of Pershing in acquiring shares during the Offer period, stating only that:

> Pershing Square and its affiliates intend to exercise all of their legal rights, including appraisal rights to ensure that their reasonable expectations are not frustrated and to ensure that they receive fair value for their investments in Sears Canada.

44. It is obvious that the purpose of Pershing in acquiring the shares was not simply to exercise the legal rights attached to the shares. Rather, the Applicants believe that, given that Pershing acquired the shares *after* Sears Holdings announced that majority of the minority approval of the Subsequent Acquisition Transaction was assured, the true purpose of Pershing in acquiring the shares was to maintain the

price of Sears Canada shares above the Offer price. That purpose was not disclosed in Pershing's April 7, 2006 press release. Pershing therefore did not comply with section 102 of the Act and section 198 of the Regulations.

45. Further, the April 7, 2006 press release did not disclose the future intention of Pershing to acquire common shares of Sears Canada. However, as described in the April 12, 2006 edition of the *Wall Street Journal*, Pershing sought to unwind the Pershing/Sun Trust Swaps in order to again acquire legal and beneficial ownership of the 6.9 million shares subject to the swaps. The actions of Pershing in seeking to unwind the swaps establishes an undisclosed intention to acquire further common shares of Sears Canada. For this reason, the April 7, 2006 press release did not comply with section 102 of the Act and section 198 of the Regulations.

46. These violations of the Act are serious, particularly as the purpose of Pershing acquiring shares appears to have been to thwart the Offer and the Subsequent Acquisition Transaction. The purpose of Pershing's acquisitions and its future intentions is critical information for Sears Holdings, Sears Canada shareholders and the market generally that is required to be disclosed by section 198 of the Regulations, and its absence from an otherwise very carefully worded press release is very difficult to explain.

The April 17th Press Release

47. The April 17, 2006 press release disclosed that Pershing, together with its joint actors, Knott Partners and Hawkeye, had "formed a group to oppose" the Offer, including "tak[ing] all appropriate legal action to halt the transaction...". However, the Applicants believe that Pershing was acting jointly with Knott Partners and Hawkeye and other shareholders of Sears Canada prior to April 17, 2006.

48. This is supported by public statements made by Mr. Ron Mayers during the Offer period. The Applicants believe that Mr. Mayers obtained his information with respect to the intentions of the holders of the 22 million shares from communications with Pershing, Hawkeye and/or Knott Partners. As described above, it also appears clear from subsequent articles in the press that Pershing was communicating its intentions with respect to the Offer to Mr. Mayers.

49. The question whether persons are acting jointly or in concert is a question of fact. The purpose of section 91 is to ensure that all persons or companies who are effectively engaged in a common investment or purchase program, whether in support of, or opposition to, a take-over bid, abide by the rules that govern

securities transactions prior to, during and subsequent to the bid.[23] Subsection 91(1) of the Act provides as follows:

> **91(1)** For the purposes of this Part, it is a question of fact as to whether a person or company is acting jointly or in concert with an offeror and, without limiting the generality of the foregoing, the following shall be presumed to be acting jointly or in concert with an offeror:
>
> 1. Every person or company who, as a result of any agreement, commitment or understanding, whether formal or informal, with the offeror or with any other person or company acting jointly or in concert with the offeror, acquires or offers to acquire securities of the issuer of the same class as those subject to acquire.
>
> 2. Every person or company who, as a result of any agreement, commitment or understanding, whether formal or informal, with the offeror or with any other person or company acting jointly or in concert with the offeror, intends to exercise jointly or in concert with the offeror or with any other person or company acting jointly or in concert with the offeror any voting rights attaching to any securities of the offeree issuer.
>
> 3. Every associate or affiliate of the offeror.

50. For the purposes of section 91, the term "offeror" includes a person who has made an "offer to acquire", which is defined in section 89(1) of the Act as follows:

> "offer to acquire" includes,
>
> (a) an offer to purchase, or a solicitation of an offer to sell, securities,
>
> (b) an acceptance of an offer to sell securities, whether or not such offer to sell has been solicited,
>
> or any combination thereof, and the person or company accepting an offer to sell shall be deemed to be making an offer to acquire to the person or company that made the offer to sell;

51. Therefore, to the extent that Pershing, together with Hawkeye, Knott Partners or any other shareholder of Sears Canada, purchased shares of Sears Canada based on any agreement, commitment or understanding, whether formal or informal, concerning the acquisition of the shares or the voting of such shares, such persons would be acting jointly or in concert.

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[23] *Report of the Committee to Review the Provisions of the Securities Act (Ontario) Relating to Take-Over Bids and Issuer Bids* (September 23, 1983)

52. As held by the Ontario Securities Commission in *243978 Alberta Ltd. et al. (Re),* (1982), 4 OSCB 566C at 569C while "a formal agreement" between the parties would unquestionably be helpful from an evidentiary point of view, "a formal agreement" is not a prerequisite. This pragmatic approach recognizes that when parties make agreements to breach securities laws, they tend to act secretly and informally, not leaving "smoking guns" in plain view.

53. In *Re Capital Reserve Inc.* (1988), Weekly Summary, Edition 88:98, the evidence indicated that one of the respondents had put together a group of people to purchase shares in Capital Reserve. The British Columbia Securities Commission held that the respondent and the other purchasers were acting jointly and in concert and that the acquisition of the pooled shares was a take-over bid.

54. A similar finding was made by the Ontario Securities Commission in *Re 243978, supra.* In that case, one of the named respondents and his associates entered into an agreement, commitment or understanding to purchase shares in the target company. The Commission held that the respondent and his associates set out to make a secret take-over bid of the target company with the intention of obtaining sufficient shares to force or influence management of the target to merge with the respondent's company. In the words of the Commission, this constituted an "illegal and secret acquisition of effective control of a public company jointly or in concert and with the assistance of their 'friends' and 'employees'".

55. In the event that Pershing was acting jointly or in concert with Hawkeye, Knott Partners and/or other shareholders of Sears Canada without disclosing that fact, Pershing, together with its joint actors, violated sections 101 and/or 102 of the Act, depending on the holdings of its joint actors.

Violations of Section 126.1 and 126.2 of the Act

56. Section 126.1 of the Act provides that:

> **126.1** A person or company shall not, directly or indirectly, engage or participate in any act, practice or course of conduct relating to securities or derivatives of securities that the person or company knows or reasonably ought to know,
>
> (a) results in or contributes to a misleading appearance of trading activity in, or an artificial price for, a security or derivative of a security; or
>
> (b) perpetrates a fraud on any person or company.

57. In *Re Podorieszach* (2004 WL 728599), the Alberta Securities Commission was required to consider what is meant by "artificial price" for a security under section

93(b) of the *Securities Act* (Alberta), the equivalent of section 126.1 of the Act. The Commission stated the following:

> An individual's trading activity may have the intended effect of raising or lowering the price of a security to a level different than it would be under normal market conditions. *Alternatively, the trading activity may maintain a price when it would otherwise have risen or fallen. In our view, both situations create an artificial price because the price is not reflective of the market's unimpeded judgment of the value of the security being traded. Such conduct that is designed to affect artificially the prices on the market is contrary to the public interest because it misleads other buyers and sellers...* [emphasis added.]

58. In addition, the Commission found that the mere fact that the transaction involved the transfer of ownership of the securities from a real seller for consideration does not preclude a finding that the price was artificial:

> The Respondents also argued that each of the impugned purchases involved a real purchaser paying a real price to a real seller, and hence there was no "artificial price". In effect, the argument seems to have been that a completed transaction involving the payment of real consideration to an arm's length seller precludes a finding that the price was artificial.
>
> Again, we disagree. That argument suggests that no transaction in which economic interests change and ownership genuinely passes from seller to buyer, acting in a market, could contravene subsection 93(b) of the Act. That in turn only implies that only a sham transaction – for example, a "wash trade" – could contravene subsection 93(b). That is not correct While sham transactions can manipulate the markets and contravene the provision, it does not follow that those are [the] only types of transactions that can do so.

59. From the limited disclosure provided by Pershing to date with respect to its trading activities, the Applicants believe that Pershing was timing its purchases of Sears Canada shares to maintain the price of Sears Canada shares; in particular, to ensure that the price of the shares did not fall below the current Offer price. In that regard, the timing of its purchases on March 16, 2006 (the day before the day on which the Offer was originally scheduled to expire) and April 6, 2006 (the same day that Sears Holdings announced that it had entered into support agreements in respect of a sufficient number of shares to ensure minority approval of the Subsequent Acquisition Transaction) clearly support the inference that the purchases were made for the purpose of maintaining the price of Sears Canada shares. The Applicants state that Pershing supported and reinforced its efforts to maintain an artificial price for the shares by making selective and unattributed disclosure of "information" to analysts and reporters, either directly or through

Mr. Mayers, for the purpose of obtaining press coverage, based on misleading and/or incomplete information supplied by Pershing, suggesting to Sears Canada shareholders that a higher offer price was inevitable and to discourage shareholders from tendering their shares to the Offer.

60. The Applicants state that the conduct of Pershing and its joint actors violates section 126.1 of the Act as Pershing and its joint actors knew or reasonably ought to have known that their conduct would result in an artificial price for the common shares of Sears Canada contrary to section 126.1.

61. In addition, the Applicants state that Pershing has violated section 126.2 of the Act. Section 126.2 provides that:

> **126.2** (1) A person or company shall not make a statement that the person or company knows or reasonably ought to know,
>
> (a) in a material respect and at the time and in the light of the circumstances under which it is made, is misleading or untrue or does not state a fact that is required to be stated or that is necessary to make the statement not misleading; and
>
> (b) would reasonably be expected to have a significant effect on the market price or value of a security.

62. In particular, the April 7, 2006 press release of Pershing failed to disclose that the purpose of Pershing in acquiring shares was to maintain the market price of Sears Canada shares above the Offer price and failed to disclose the future intentions of Pershing with respect to the acquisition of Sears Canada shares. In addition, it failed to disclose that Pershing was acting jointly or in concert with other shareholders of Sears Canada, including, but not limited to, Knott Partners and Hawkeye in an attempt to thwart the Offer. It was left to Mr. Mayers to communicate this information in more general terms. The omission of those material facts made the press release misleading and their omission would reasonably be expected to have a significant effect on the market price or value of Sears Canada shares.

Abusive Minority Tactics Contrary to the Public Interest

63. As described above, Pershing understood that the 6.9 million shares that were the subject of the Pershing/Sun Trust Swaps would either be returned to Pershing or not be voted in the Subsequent Acquisition Transaction. Pershing therefore understood that it had "parked" the 6.9 million shares by removing the shares from the pool of shares that would be voted in the minority approval of the Subsequent Acquisition Transaction.

64. Based on this understanding, Pershing secretly acquired shares of Sears Canada in the market during the Offer period, without disclosing to the public the fact that Pershing understood that it had "parked", and had control or direction over the votes attached to, the 6.9 million common shares or the fact that it was acting jointly or in concert with other shareholders of Sears Canada, including, but not limited to, Hawkeye and Knott Partners

65. In addition, as described above, even when Pershing made limited disclosure of its holdings in Sears Canada, that disclosure was deficient in that it did not disclose that the purpose of Pershing's acquisition of shares of Sears Canada was to maintain the price of the Sears Canada shares above the Offer price and provide a disincentive to Sears Canada shareholders to tender to the Offer.

66. The Applicants state that, even if the above conduct does not amount to breaches of sections 101 and/or 102, 126.1 and 126.2 of the Act, it constitutes abusive minority tactics contrary to the public interest. In particular, the Companion Policy to Rule 61-501 states that following with respect to abusive minority tactics:

> **3.3 Special Circumstances** - As the purpose of the Rule is to ensure fair treatment of minority security holders, *abusive minority tactics in a situation involving a minimal minority position may cause the Director to grant an exemption from the requirement to obtain minority approval.* Where an issuer has more than one class of equity securities, exemptive relief may also be appropriate if the Rule's requirement of separate minority approval for each class could result in unfairness to security holders who are not interested parties, or if the policy objectives of the Rule would be accomplished by the exclusion of an interested party's votes in one or more, but not all, of the separate class votes.

67. As the decision of the Commission in *Re Financial Models Co.* (2005), 28 OSCB 2184 establishes (citing its earlier decision in *Re British Columbia Forest Products Limited* (1981), 1 OSCB 116C), it is clear that in exercising its public interest jurisdiction, the Commission is also concerned with protecting the interests of majority shareholders from abuse:

> [55] In *Re British Columbia Forest Products Limited* (1981), 1 OSCB 116C at page 120C, the Commission shed light on the protection due to majority shareholders:
>
> > However, the Commission's responsibility and duty is not only to the minority security holders but to the capital markets as a whole and to all participants therein whether majority or minority security holders. Accordingly, just as the Commission must be vigilant to protect minority security holders so too it must be vigilant not to abuse the rights of majority security holders ... There must be confidence in the marketplace for holders of large blocks of securities as well as holders of small blocks of securities.

68. Sears Canada does not seek exemptive relief from the requirement to obtain minority approval as that would prejudice other minority shareholders of Sears Canada whose conduct is not in question; however, the Applicants state that the Commission should exercise its broad public interest jurisdiction and either require Pershing and its joint actors to dispose of their common shares of Sears Canada or exclude the votes attached to any common shares of Sears Canada owned or controlled by Pershing and its joints actors, including Knott Partners and Hawkeye, from the determination of the majority of the minority in the Subject Acquisition Transaction.

Conclusion

Having entered into the Pershing/Sun Trust Swaps with the understanding that, by convention, the swaps could easily be unwound and the 6.9 million common shares returned or, in the alternative, that the shares would be voted as directed by Pershing or not voted at all, Pershing, together with its joint actors, have engaged in abusive minority tactics, including violating Ontario securities laws described above, in attempting to thwart the Offer. By secretly acquiring shares in the market without disclosing the "parking" of the 6.9 million shares, Pershing and its joint actors were effectively trying to "rig the game" to thwart the Offer and any Subsequent Acquisition Transaction. Their actions must be contrary to the public interest and cannot be condoned. Therefore, the Applicants submit that the conduct of Pershing and its joint actors warrants the granting of the relief sought in this application under sections 104 and 127 of the Act.

We enclose our firm cheque in the amount of $7,500 in respect of the filing fee for the application.

Please contact me or my partner Don Ross at (416) 862-4288 with any questions you may have concerning the foregoing.

Yours very truly,

Joseph M. Steiner
JMS:adc
Enclosures

c. Naizam Kanji/Michael Brown/Kelley McKinnon - (OSC Staff)
Kent Thomson/Luis Sarabia/Patricia Olasker - (Davies)
Kathleen Keller-Hobson/John Laskin/Andrew Gray - (Torys)
Paul Steep/Tom Sutton - (McCarthys)
Don Ross - (Osler)
Allan D. Coleman - (Osler)