Ontario Securities Commission
Commission des valeurs mobilières de l'Ontario
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IN THE MATTER OF THE *SECURITIES ACT*
R.S.O. 1990, c. S.5, AS AMENDED

- and -

IN THE MATTER OF MI DEVELOPMENTS INC.

REASONS AND DECISION

Hearing:	September 9 and 10, 2009	
Panel:	James E. A. Turner	- Vice-Chair
	Paulette L. Kennedy	- Commissioner
Counsel:	Thomas G. Heintzman René R. Sorell Andrew B. Matheson (McCarthy Tétrault LLP)	- For Greenlight Capital, Inc.
	Michael E. Barrack Jessica S. Bookman (ThorntonGroutFinnigan LLP) Shane Priemer (Voorheis & Co. LLP)	- For Farallon Capital Management, L.L.C., Hotchkis and Wiley Capital Management, LLC, Donald Smith & Co. Inc., Owl Creek Asset Management, L.P., North Run Capital, LP, Pzena Investment Management, LLC
	Kent E. Thomson Andrea L. Burke James W. E. Doris Vincent A. Mercier Derek D. Ricci (Davies Ward Phillips & Vineberg LLP)	- For MI Developments Inc.

Laura K. Fric Emmanuel Z. Pressman Craig T. Lockwood (Osler, Hoskin & Harcourt LLP)	-	For Magna Entertainment Corp.
Sean F. Dunphy Edward J. Waitzer Amanda Linett Ellen Snow (Stikeman Elliott LLP)	-	For Fair Enterprise Limited
James Sasha Angus Michelle Vaillancourt Usman Sheikh Naizam Kanji Shannon O'Hearn Jason Koskela	-	For Staff of the Ontario Securities Commission

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REASONS AND DECISION

I. OVERVIEW

[1] This matter involved the hearing by the Ontario Securities Commission (the "**Commission**") of two applications (i) an application dated July 10, 2009 by Farallon Capital Management, L.L.C., Hotchkis and Wiley Capital Management, LLC, Donald Smith & Co. Inc., Owl Creek Asset Management, L.P., North Run Capital, LP and Pzena Investment Management, LLC, on behalf of themselves and funds and entities under their management (collectively, the "**Shareholders**"), and (ii) an application dated March 30, 2009 (as amended and restated on April 9, 2009 and July 13, 2009) by Greenlight Capital, Inc. ("**Greenlight**"), (the Shareholders and Greenlight are collectively referred to in these reasons as the "**Applicants**" and the two applications are collectively referred to as the "**Applications**").

[2] The Applications are made pursuant to sections 104 and 127 of the *Securities Act*, R.S.O. 1990, c. S.5, as amended (the "**Act**") and relate to compliance by MI Developments Inc. ("**MID**") with Multilateral Instrument 61-101 – *Protection of Minority Security Holders in Special Transactions* ("**MI 61-101**") in connection with two groups of transactions (i) a new loan in the amount of US$125 million made by MID to Magna Entertainment Corp. ("**MEC**") (the "**November Loan**"), extensions by MID in favour of MEC of existing loans in the amount of US$312 million (the "**Loan Extension**") and a proposed corporate reorganization of MID described in paragraph 36 of these reasons (the "**November Reorganization Proposal**"), all publicly announced on November 26, 2008, and (ii) two transactions between MID and MEC related to the voluntary filings made by MEC under Chapter 11 of the United States Bankruptcy Code (the "**Bankruptcy Filings**"), being the debtor-in-possession financing by MID of MEC of up to US$62.5 million (the "**DIP Financing**") and a so-called "stalking horse" offer in the amount of US$195 million made by MID to acquire certain assets from MEC (the "**Stalking Horse Bid**"), both publicly announced on March 5, 2009.

[3] The November Loan, the Loan Extension and the November Reorganization Proposal are collectively referred to in these reasons as the "**November Transactions**". The DIP Financing and the Stalking Horse Bid are collectively referred to as the "**March Transactions**".

[4] The Applicants sought a determination that the November Transactions and the March Transactions violated MI 61-101 because minority shareholder approval ("**Minority Approval**") of those transactions was required and not obtained and because a formal valuation was required and not provided. The Applicants also sought an order or orders from the Commission that would, in effect, prohibit MID from relying on any exemption from the requirement to obtain Minority Approval under MI 61-101 in connection with any future related party transactions between MID and MEC.

[5] On August 11, 2009, the Commission issued a Notice of Hearing pursuant to subsection 104(1) and section 127 of the Act, scheduling a hearing for September 9 and 10, 2009 to consider the Applications.

[6] On August 20, 2009, following a motions hearing, the Commission issued an order granting MEC limited intervener status to make oral and written submissions with respect to the appropriateness and scope of any Commission order in disposing of the Applications. The Commission also granted Fair Enterprise Limited ("**Fair Enterprise**") limited intervenor status to adduce oral and written evidence regarding its involvement in the transactions and agreements to which it is a party and that are at issue in this matter. On August 21, 2009, the Commission issued a protective order related to the confidentiality of non-public documents produced by the parties.

[7] On September 3, 2009, the Commission heard motions made by the Applicants for production of documents. The motions resulted in orders for certain pre-hearing production.

[8] The hearing of the Applications on the merits was held on September 9 and 10, 2009. As noted above, the Applicants alleged that the November Transactions and the March Transactions were related party transactions between MID and MEC, and that MID failed to comply with the requirement to obtain Minority Approval and to prepare a formal valuation under MI 61-101 in connection with those transactions. The Applicants alleged that MID's conduct raises significant public interest and public policy issues that required intervention by the Commission. The Applicants submitted that MID disregarded the legitimate interests of its shareholders in entering into a series of related party transactions that resulted in substantial value destruction for shareholders and that the Commission should exercise its discretion to ensure that the legitimate objectives of securities regulation are met in connection with those transactions.

[9] MID denied that it failed to comply with MI 61-101. MID submitted that the November Transactions (assuming the Loan Extension was, in fact, a related party transaction) were all "downstream transactions" for purposes of MI 61-101 and therefore Minority Approval and a formal valuation were not required. MID submitted, in the alternative, that the related party transactions (again, assuming the Loan Extension was a related party transaction) were exempt from Minority Approval and the valuation requirement under the 25% market capitalization exemption in MI 61-101.

[10] MID submitted that the Loan Extension was not a related party transaction within the meaning of MI 61-101 because it did not constitute a material amendment to the existing loans to which it related.

[11] MID also submitted that the Commission does not have the authority to grant the requested relief under either section 104 or section 127 of the Act, and that, even if we concluded that we could grant such relief, we should not do so in the circumstances.

[12] MID submitted further that the granting of the requested relief would seriously undermine MID's investment in MEC represented by its outstanding secured loans to MEC. MID submitted that the November Loan, the Loan Extension and the March Transactions were intended by MID primarily to protect and preserve the value of that investment.

[13] MEC submitted that if the order sought by the Applicants were granted, it would be punitive and would have a devastating financial impact on MEC. We were told that, if the order

were granted, MEC would run out of funds before a MID minority shareholder vote could be held and that would lead to a fire sale of MEC's assets. MEC also submitted that if such an order were granted, MEC's ability to maximize value in the ongoing auction of its assets would be severely prejudiced because MID would not be permitted to fully participate.

[14] On September 14, 2009, we issued an order dismissing the Applications and releasing MID from its undertaking provided to Staff of the Commission ("**Staff**") on May 11, 2009 that it would not enter into certain transactions with MEC, pending the outcome of this matter, that could not be unwound. These are our reasons for dismissing the Applications.

II. THE PARTICIPANTS

A. The Applicants

1. Farallon Capital Management, L.L.C. et al.

[15] The Shareholders are a group of U.S.-based investment management firms including hedge fund sponsors and mutual fund managers catering to a variety of institutional and retail clients.

[16] As of July 10, 2009, the Shareholders collectively owned or controlled approximately 37% of the outstanding Class A subordinate voting shares of MID ("**MID Class A Shares**").

2. Greenlight Capital, Inc.

[17] Greenlight is a New York-based investment management firm founded in 1996. Together with its affiliates, Greenlight manages approximately US$5 billion in assets.

[18] Greenlight has had a significant investment in MID since MID was spun out from Magna International Inc. ("**Magna**") in 2003. Greenlight, together with its affiliates, owns 5.6 million MID Class A Shares, representing approximately 12% of the outstanding MID Class A Shares. Greenlight also holds US$1,000,000 principal amount of MEC 8.55% convertible subordinated notes due June 15, 2010.

B. MI Developments Inc.

[19] MID is a company incorporated under the laws of Ontario. In August 2003, Magna spun-off MID as a public company and the owner of Magna's real estate assets. MID is a real estate operating company engaged principally in the ownership, management, leasing, development and acquisition of industrial and commercial real estate properties. Its head office is located in Aurora, Ontario.

[20] As part of the spin-off, Magna transferred to MID all of its shares in MEC. As of September 1, 2009, MID held a 54% equity interest and a 96% voting interest in MEC through the ownership of 218,116 MEC Class A subordinate voting shares ("**MEC Class A Shares**") and 2,928,447 MEC Class B shares ("**MEC Class B Shares**").

[21] The authorized capital of MID consists of an unlimited number of MID Class A Shares, 706,170 MID Class B shares ("**MID Class B Shares**"), and an unlimited number of preference shares issuable in series. As of September 3, 2009, MID had 46,160,564 MID Class A Shares, 547,413 MID Class B Shares, and no preference shares outstanding. Each MID Class A Share carries one vote and each MID Class B Share carries 500 votes.

[22] The MID Class A Shares are listed on the Toronto Stock Exchange (the "**TSX**") and the New York Stock Exchange. The MID Class B Shares are listed on the TSX.

[23] MID is controlled by a group of persons consisting of Mr. Frank Stronach, the Stronach Trust, 445327 Ontario Limited ("**445327**") and Fair Enterprise. Those persons are collectively referred to in these reasons as the "**Stronach Group**".

[24] Mr. Stronach is a director and the Chairman and founder of each of MID and MEC. Until April 7, 2009, Mr. Stronach was also the Chief Executive Officer of MEC. Mr. Stronach and three other members of his family are trustees of the Stronach Trust and Mr. Stronach is also a potential beneficiary; 445327 is wholly-owned by the Stronach Trust.

[25] MID is controlled by the Stronach Group and is a control person with respect to MEC within the meaning of MI 61-101.

C. The Intervenors

1. Magna Entertainment Corp.

[26] MEC is a public company incorporated under the laws of the State of Delaware with a registered office in Wilmington, Delaware and its principal executive office in Aurora, Ontario. MEC is the owner and operator of horse racetracks in North America and one of the world's leading suppliers of live horse racing content to the inter-track, off-track and account wagering markets. MEC was created in 1999 as part of a reorganization of the non-automotive businesses of Magna, under which Magna transferred certain horse racing and real estate assets to MEC. Magna spun off a minority interest in MEC to Magna shareholders in March, 2000 when MEC became a public company.

[27] The authorized capital of MEC consists of 310,000,000 Class A subordinate voting shares ("**MEC Class A Shares**") and 90,000,000 Class B shares ("**MEC Class B Shares**"). Each MEC Class A Share carries one vote and each MEC Class B Share carries 20 votes. Prior to March 2009, the MEC Class A Shares were listed on the TSX and the NASDAQ National Market ("**NASDAQ**"). The shares were de-listed from the TSX effective April 1, 2009 and from the NASDAQ effective March 16, 2009, as a result of the bankruptcy of MEC.

[28] MEC is controlled by the Stronach Group through MID. MID beneficially owns 218,116 MEC Class A Shares and 2,928,447 MEC Class B Shares, representing in aggregate 54% of MEC's outstanding equity securities and 96% of the votes attached to MEC's outstanding voting securities.

[29] In March 2009, MEC initiated voluntary bankruptcy proceedings by making the Bankruptcy Filings in the United States Bankruptcy Court for the District of Delaware (the "**U.S. Bankruptcy Court**") and by commencing a parallel proceeding in Canada under the *Companies' Creditors Arrangement Act*.

2. Fair Enterprise Limited

[30] Fair Enterprise is a company incorporated under the laws of the Island of Jersey, Channel Islands. It is an estate planning vehicle for the Stronach family. The members of the Stronach family are indirect beneficiaries. All of the shares of Fair Enterprise are held by Bergenie Anstalt, a Lichtenstein anstalt. The directors of Fair Enterprise are EFG Corporate Services Limited and EFG Trust Company Limited and are not otherwise related to Mr. Stronach or any other member of the Stronach Group.

[31] Prior to November 25, 2008, Fair Enterprise owned 628,570 MEC Class A Shares (the "**Fair Enterprise MEC Shares**") representing approximately 21.5% of the outstanding MEC Class A Shares and less than 1% of the votes attached to MEC's outstanding voting securities.

[32] As noted above, Fair Enterprise is part of the Stronach Group and there is no dispute that Fair Enterprise is a related party of MID within the meaning of MI 61-101.

[33] Mr. Stronach is not a director or shareholder of Fair Enterprise. According to Fair Enterprise, Mr. Stronach shared control and direction over the Fair Enterprise MEC Shares until November 25, 2008.

III. THE RELEVANT TRANSACTIONS

[34] The focus of the Applications are the November Transactions and the March Transactions. The Applicants allege that these transactions violated MI 61-101 for the following reasons:

(i) In each case, the relevant transactions were "related party transactions" between MID and MEC within the meaning of MI 61-101;

(ii) Minority Approval of the related party transactions and a formal valuation were required under MI 61-101 and were not obtained and no exemption was available;

(iii) The downstream transaction exception contained in paragraph (g) of section 5.1 of MI 61-101 (the "**Downstream Exception**") was not available to MID in respect of the November Transactions or the March Transactions because, at the relevant time, Fair Enterprise beneficially owned or exercised control or direction over more than 5% of a class of equity or voting securities of MEC through its interest in the Fair Enterprise MEC Shares. The Downstream Exception was not, or should not be, available to MID because:

a. The Azalea Trust Transaction (described further under "The Azalea Trust Transaction," below) under which Fair Enterprise purported to dispose of the Fair Enterprise MEC Shares was not completed at the time that the November Transactions were agreed to by MID and MEC;

b. MID failed to make reasonable inquiry that no related party of MID beneficially owned or exercised control or direction over more than 5% of a class of equity or voting securities of MEC;

c. The Azalea Trust Transaction was an artificial transaction and a sham and did not effect a disposition by Fair Enterprise of the beneficial ownership of the Fair Enterprise MEC Shares;

d. The Azalea Trust Transaction was carried out on the basis of improperly acquired information about the pending November Reorganization Proposal and in violation of insider tipping and trading prohibitions, and trading blackout requirements, and such violations should prevent MID from relying on the Downstream Exception in the circumstances; and

(iv) The 25% market capitalization exemption contained in paragraph (a) of section 5.5 of MI 61-101 (the "**Market Cap Exemption**") was not available to MID in respect of the November Transactions or the March Transactions because each group of transactions was part of a series of "connected transactions", the fair market value of which, when aggregated, exceeded 25% of the market capitalization of MID at the relevant time (determined in accordance with MI 61-101).

A. The November Transactions

[35] The November Transactions involved a multi-stage transaction that included MID providing a new loan to MEC of up to US$125 million (i.e., the November Loan) and MID extending the maturity and repayment dates of amounts due under MID's existing US$312 million secured loans to MEC (i.e., the Loan Extension), which amounts would otherwise have become due on December 1, 2008.

[36] The November Transactions also included the November Reorganization Proposal which was to be implemented following MID shareholder approval, including Minority Approval by the holders of MID Class A Shares, and which included:

(i) A substantial issuer bid by MID;

(ii) The purchase by MID from MEC of selected real estate assets at fair market value;

(iii) The purchase by the Stronach Group from MID of MEC shares; and

(iv) MID acquiring up to a 60% voting interest in MEC.

If completed, the November Reorganization Proposal would have spun out MID's interest in MEC to the MID shareholders.

[37] MID represented that the purpose of the November Loan was two-fold. First, it was meant to provide immediate funding so that MEC could continue its operations until MID shareholders had an opportunity to consider and vote on the November Reorganization Proposal. Second, US$28.5 million was made available for the limited purpose of funding an application by MEC in connection with a lottery licence. That application was ultimately unsuccessful and US$27.5 million was repaid to MID. The November Loan was advanced under an agreement dated December 1, 2008.

[38] The Loan Extension extended the maturity dates of existing secured loans from MID to MEC in the aggregate amount of US$312 million. The extension was for a period of four months, from December 1, 2008 to March 31, 2009. The Loan Extension was a unilateral extension by MID as permitted under terms of the loans that expressly provide that MID may unilaterally extend the maturity and repayment dates of the loans.

[39] If the November Reorganization Proposal did not receive the requisite MID shareholder approval, or was abandoned or withdrawn, the maturity dates and repayment dates under the November Loan and the Loan Extension would be accelerated to a date 30 days after the abandonment or withdrawal of the November Reorganization Proposal.

[40] On February 18, 2009, MID publicly announced that it was not proceeding with the November Reorganization Proposal. As a result, the maturity dates and repayment dates of the November Loan and the Loan Extension were accelerated to March 20, 2009.

[41] In the early hours of November 26, 2008, before the special committee of disinterested directors of MID and the MID board of directors met to approve the November Transactions, counsel for MID sent an e-mail to counsel for Fair Enterprise which stated that:

> In order to rely on the downstream transaction [*sic*], MID needs to make reasonable enquiry that no related party owns more than 5% of any class of MEC shares. Would you confirm that Frank Stronach and related entities no longer beneficially own or exercise control or direction over, other than through their interest in MID, any shares of MEC (or at a minimum no more than 5% of any class of MEC shares).

At approximately 6:15 a.m. on November 26, counsel for Fair Enterprise replied that "I did ask the question previously and was advised that neither Frank [Stronach] nor any other related entity to Frank [Stronach] owned or exercised control or direction over any MEC Shares (other than indirectly though MID)". A few minutes later, counsel for Azalea Trust confirmed that this was his understanding as well.

B. The Azalea Trust Transaction

[42] On November 25, 2008, Fair Enterprise purported to sell the Fair Enterprise MEC Shares to the Azalea 2008 Trust (the "**Azalea Trust**"). That sale transaction is referred to in these reasons as the "**Azalea Trust Transaction**". The news release relating to the Azalea Trust Transaction provided as follows:

> THE AZALEA 2008 TRUST ACQUIRES SHARES OF MAGNA ENTERTAINMENT CORP.
>
> November 25, 2008 – The Azalea 2008 Trust has acquired, by private agreement, ownership and control over 628,570 shares of Class A Subordinate Voting Stock (the "Class A Shares") of Magna Entertainment Corp. ("MEC"), representing approximately 21.6% of the outstanding Class A Shares of MEC. The Trust intends to sell the Class A Shares of MEC as soon as practicable and in an orderly fashion when permitted to do so under applicable securities laws, and intends on donating any net gains (after expenses) resulting from the sale of such shares to one or more registered Canadian charities designated by the trustee of the Trust.
>
> For further information, please contact:
> Timothy Jones
> c/o 40 King Street West
> Suite 5800
> Toronto, Ontario
> M5H 3S1

[43] The November Transactions were publicly announced the next day, November 26, 2008.

[44] The Azalea Trust was established on November 25, 2008 by Mr. Timothy Jones as settlor. Mr. Jones also served as the sole director and officer of the numbered company incorporated on the same day to act as trustee of the Azalea Trust. Mr. Jones is a former mayor of Aurora, Ontario and is a paid consultant to Neighbourhood Network, a community initiative founded by Belinda Stronach, Executive Vice-Chairman and a director of Magna.

[45] The purpose of Azalea Trust, as set out in its organizing trust deed, is to benefit one or more Canadian registered charities. The beneficiaries of Azalea Trust are such Canadian registered charities as are appointed by the trustee, and if no such charities are appointed, then the beneficiary is the Reena Foundation, a charity for people with developmental disabilities. The sole trustee of Azalea Trust is 2191273 Ontario Inc. ("**2191273**"), a corporation wholly-owned by Mr. Jones. Mr. Jones is the sole director and officer of 2191273. Under section 8.3 of the trust deed for the Azalea Trust, 2191273 is entitled to trustee fees equal to 10% of the net proceeds of sale of the Azalea Trust's MEC shares to a maximum of $100,000.

[46] The purchase price of the Fair Enterprise MEC Shares was US$886,284.00, which we are told represented the fair market value of the shares determined at the time of the Azalea Trust

Transaction. Azalea Trust satisfied the purchase price by issuing to Fair Enterprise a non-interest bearing promissory note due December 31, 2010 (the "**Promissory Note**"). Recourse against Azalea Trust under the Promissory Note was limited to "the enforcement and realization by the Holder of its legal and equitable rights and remedies against the MEC Shares and the proceeds realized from the sale of the MEC Shares." These terms of the Azalea Trust Transaction were not disclosed in the news release issued by Fair Enterprise on November 25, 2008 (referred to in paragraph 42 of these reasons).

[47] It was represented to us that Mr. Stronach caused the sale of the Fair Enterprise MEC Shares for two reasons. First, Mr. Stronach wanted to address allegations from certain MID shareholders that his economic interests were not aligned with MID and its shareholders because he had a direct interest in MEC through the ownership by Fair Enterprise of the Fair Enterprise MEC Shares. Second, Mr. Stronach was generally aware that if Fair Enterprise disposed of those shares, an exemption from the related party transaction requirements of MI 61-101 would be available to MID (i.e., the Downstream Exception would be available).

[48] At the closing of the Azalea Trust Transaction, the share certificates for the Fair Enterprise MEC Shares were not endorsed and delivered to the Azalea Trust. Rather, a transfer form was signed and delivered. The Fair Enterprise MEC Shares were not registered in the name of the Azalea Trust until April 13, 2009, and the certificates for those shares were not delivered to the Azalea Trust until April 17, 2009.

[49] Pursuant to a covenant in the purchase agreement related to the Azalea Trust Transaction, the Azalea Trust agreed to "sell the MEC Class A Shares that it purchased as soon as practicable after November 25, 2008 and in an orderly fashion when permitted to do so under applicable securities laws" (the "**Disposition Covenant**") and was to apply the net proceeds of sale to the repayment of the Promissory Note. Any excess of the net proceeds over the amounts due under the Promissory Note was to be donated to charity.

[50] The legal counsel who acted for Azalea Trust in connection with the Azalea Trust Transaction testified that Azalea Trust had technical difficulties in attempting to sell the Fair Enterprise MEC Shares and to comply with the Disposition Covenant. These difficulties included the following:

(i) Mr. Jones originally understood that a hold period applied to the Fair Enterprise MEC Shares and, accordingly, did not take steps to immediately sell those shares;

(ii) approximately 71% of the Fair Enterprise MEC Shares were represented by a share certificate containing a legend restricting trading under applicable U.S. securities law and requiring the Azalea Trust to obtain a legal opinion that any proposed sale was in fact exempt from, or not subject to, registration requirements under U.S. securities law;

(iii) the MEC Class A Shares were delisted from NASDAQ on March 16, 2009;

(iv) the trading of MEC Class A Shares on the TSX was suspended on March 6, 2009 and the MEC Class A Shares were delisted on April 1, 2009;

(v) there were problems obtaining MEC's consent to effecting the legal transfer of the Fair Enterprise MEC Shares to the Azalea Trust due to complications that arose from MEC's bankruptcy; and

(vi) there was some confusion surrounding transferring the Fair Enterprise MEC Shares through MEC's transfer agent relating to how the relevant guarantee medallion program was to be complied with.

The last of these difficulties was not finally resolved until May 1, 2009.

[51] The Applicants alleged that Azalea Trust was in breach of the Disposition Covenant by the time of the March Transactions.

[52] The Azalea Trust filed a Schedule 13D with the United States Securities and Exchange Commission (the "**13D**") on December 5, 2008. The 13D disclosed that the Azalea Trust owned the Fair Enterprise MEC Shares and that the trustee of the Azalea Trust and Mr. Jones, as sole director and officer of the trustee, may be deemed beneficial owners of those shares for U.S. securities law purposes.

[53] On March 27, 2009, Fair Enterprise released the Azalea Trust from its obligations under the Promissory Note, and each of Fair Enterprise and the Azalea Trust mutually released each other from all claims arising in connection with the Azalea Trust Transaction.

[54] On June 29, 2009, the Azalea Trust sold the Fair Enterprise MEC Shares for an aggregate price of $7,500 to 2210456 Ontario Inc., a company that was owned and controlled by a third party.

[55] MID represented that it was not directly involved in negotiating, documenting, structuring or implementing the Azalea Trust Transaction. MID says that it had no specific knowledge of the terms of that transaction other than as a result of the inquiries described in paragraph 157 of these reasons.

C. The DIP Financing and Stalking Horse Bid

[56] On March 5, 2009, MEC and certain of its subsidiaries made the Bankruptcy Filings and on the same day were granted recognition by the Ontario Superior Court of Justice of the U.S. bankruptcy proceedings under the *Companies' Creditors Arrangement Act*.

[57] The DIP Financing and Stalking Horse Bid were publicly announced on March 5, 2009. MID agreed to lend MEC an amount of up to US$62.5 million under the DIP Financing. The aggregate purchase price offered by MID for the purchase from MEC of assets under the Stalking Horse Bid was US$195 million. That purchase price was to be satisfied (i) as to US$136 million, through a credit for MID's existing loans to MEC, (ii) as to US$44 million, by payment

in cash, and (iii) as to US$15 million, through the assumption of a capital lease. The Stalking Horse Bid represented the minimum offer or "floor price" for the MEC assets. Third parties were encouraged to make higher competing offers.

[58] On April 20, 2009, MID publicly announced that it had agreed with MEC to terminate the Stalking Horse Bid in response to objections raised by a number of parties in the MEC bankruptcy proceeding. As a result, no assets were purchased by MID under the Stalking Horse Bid.

[59] On April 20, 2009, MID also publicly announced that the terms of the DIP Financing had been amended to, among other things, extend the maturity date from September 6, 2009 to November 6, 2009 and to reduce the principal amount from US$62.5 million to US$38.4 million.

D. The Amended DIP Financing

[60] On August 26, 2009, MID publicly announced that the terms of the DIP Financing had been conditionally amended to, among other things, increase the principal amount of the loan by US$28 million to up to US$66.4 million, and to extend the maturity date to April 30, 2010 (the "**Amended DIP Financing**"). The Amended DIP Financing is conditional upon the Commission rendering a decision in favour of MID in connection with the Applications and upon the U.S. Bankruptcy Court approving the amendment.

[61] Under the Amended DIP Financing, MEC must use its best efforts to sell all its assets by seeking "stalking horse" bidders and conducting auctions of its assets. Any sales are subject to approval by the U.S. Bankruptcy Court. MID has indicated that it does not intend to bid on certain of MEC's assets; it has also indicated that it is continuing to evaluate whether to make offers to purchase one or more of the other assets of MEC, in the event that MEC receives no other bids acceptable to MEC.

[62] No advances under the Amended DIP Financing were to be made prior to October 1, 2009.

IV. THE HEARING

[63] The hearing on the merits to consider the Applications was held on September 9 and 10, 2009. Two witnesses were called to testify: they were Mr. Richard J. Crofts, Executive Vice-President, Corporate Development, General Counsel and Secretary of MID, and Mr. John M. Campbell, a lawyer with Miller Thomson and the legal counsel who acted for the Stronach Group, Fair Enterprise and the Azalea Trust in connection with the Azalea Trust Transaction.

V. THE ISSUES

A. The Questions for Determination

[64] The Applications raised the following questions for determination:

(i) Can the Commission make the order requested by the Applicants under section 104 of the Act?

(ii) Can the Applicants bring the Applications under section 127 of the Act?

(iii) If so, can the Commission make the order requested by the Applicants under section 127 of the Act?

(iv) Was an exemption from the requirement for Minority Approval and the requirement to prepare a formal valuation available to MID in respect of the November Transactions, the March Transactions and the Amended DIP Financing?

(v) Were there insider trading violations in connection with the Azalea Trust Transaction, and if so, did such violations prevent MID from relying on exemptions under MI 61-101?

B. Can the Commission Make the Order Requested under Section 104 of the Act?

1. Submissions

The Applicants

[65] The Applicants submitted that section 104 of the Act applies by its terms to a requirement of Part XX of the Act or to "the regulations related to" that Part. Under subsection 1(1) of the Act "'regulations' means the regulations made under this Act and, unless the context otherwise indicates, includes the rules". The Applicants submitted that MID has not complied with MI 61-101, which is a rule of the Commission.

[66] The Applicants say that MI 61-101 deals with issuer bids, insider bids, business combinations and related party transactions. They submitted that take-over bids and issuer bids are regulated under Part XX of the Act. They also say that related party transactions are included in MI 61-101 because they raise similar regulatory concerns as issuer bids and insider bids.

[67] Accordingly, the Applicants submitted that the Commission has the authority under section 104 of the Act to make an order on the terms requested by the Applicants.

MID

[68] MID submitted that the Applicants cannot bring an application under section 104 of the Act in the circumstances because Part XX of the Act relates to take-over bids and issuer bids, and does not apply to related party transactions.

[69] In support of its position, MID pointed out that the terms "take-over bid" and "issuer bid" are referred to in a number of the possible orders that can be issued under subsection 104(1) of the Act. MID also notes that the exemptive relief power available under subsection 104(2)(a) of the Act relates specifically to take-over bids and issuer bids by reason of the reference to section

97.1 of the Act. MID pointed out that Part XX of the Act is entitled “Take-over Bids and Issuer Bids”. MID also says that according to the National Numbering System adopted by the Canadian Securities Administrators, rules related exclusively to take-over bids are prefaced with “6.2”, whereas “6.1” (as in MI 61-101) relates to “special transactions” (*CSA Staff Notice 11-312 – National Numbering System* (2009), 32 O.S.C.B. 1211 at 1213).

[70] MID submitted that the Commission's *Rules of Procedure* (*The Rules of Procedure of the Ontario Securities Commission* (2009), 32 O.S.C.B. 1991 (the “***Rules of Procedure***”)), which came into force April 1, 2009, confirm that applications brought pursuant to section 104 are confined to applications brought “in connection with take-over bids, issuer bids and mergers and acquisitions transactions” and not related party transactions. The *Rules of Procedure* provide, in part, as follows:

> “*1.1 Interpretation* -- In these Rules:
>
> [. . .]
>
> 'application' includes an application:
>
> […]
>
> (f) pursuant to section 104 and/or section 127 of the Act *in connection with take-over bids, issuer bids and mergers and acquisitions transactions*;
>
> [. . .]
>
> *2.4 Application pursuant to Section 104 and/or Section 127 of the Act* -- (1) An application made pursuant to section 104 of the Act in connection with *a take-over bid or an issuer bid* by an interested person as defined in subsection 89(1) of the Act, or an application pursuant to section 127 of the Act in connection with *a take-over bid or an issuer bid*, shall be made in accordance with Rule 16, with any modifications as the circumstances require.
>
> [. . .]
>
> *Rule 16 -- Application pursuant to Section 104 and/or Section 127 of the Act*
> *16.1 Application -- (1)* An application made pursuant to section 104 of the Act *in connection with a take-over bid or an issuer bid* by an interested person as defined in subsection 89(1) of the Act, or an application made pursuant to section 127 of the Act *in connection with a take-over bid or an issuer bid*, shall be made by serving it on every other party and *on the Manager of Take-Over Bids, Issuer Bids and Mergers and Acquisitions Transactions* and filing it" [emphasis added].

Staff

[71] Staff submitted that the Commission should apply a contextual approach to the interpretation of the Act. Staff submitted that the ordinary meaning of the words "related to" implies a broad association, and therefore the connection between Part XX and MI 61-101 should be interpreted as broad rather than narrow.

[72] Staff submitted that both Part XX of the Act and MI 61-101 overlap and regulate the same types of transactions. MI 61-101 was designed, in part, to afford additional protections for minority shareholders in connection with insider bids (a type of take-over bid) and issuer bids, the very types of transactions also regulated under Part XX of the Act. Accordingly, Staff submitted that MI 61-101 is related to Part XX and that, as a result, section 104 applies to related party transactions because such transactions are subject to MI 61-101.

[73] Staff further submitted that the Commission has recognised that the additional protections under MI 61-101 for minority shareholders in connection with insider bids and issuer bids are also necessary in respect of business combinations and related party transactions. In this way, the types of transactions regulated by Part XX and MI 61-101 – insider bids, issuer bids, business combinations and related party transactions – are a related category of transactions that raise common policy concerns. Indeed, it is for this reason that MI 61-101 was enacted.

[74] Staff submitted that the predecessor to MI 61-101 (Commission Policy 3-37) was initially limited to regulating the disclosure requirements related only to issuer bids, but the policy was gradually and iteratively expanded over time to regulate and encompass additional types of transactions that raise similar policy concerns. First, it was extended to encompass insider bids and business combinations, and finally, to regulate related party transactions.

[75] Staff submitted that the relationship between Part XX and MI 61-101 is reflected in the rule-making provisions of the Act. Paragraph 28 of subsection 143(1) groups related party transactions in the same provision as take-over bids, issuer bids and insider bids for purposes of the Commission's rule-making authority. Further, the particular subparagraph under which MI 61-101 was enacted (subparagraph 143(1)28(vii)), specifically authorizes the Commission to prescribe requirements in respect of issuer bids, insider bids, going private transactions and related party transactions for "disclosure, valuations, review by independent committees of boards of directors and approval by minority security holders," presumably as a result of the Commission's historical concerns arising from these types of transactions.

2. Analysis and Conclusion

[76] Section 104 of the Act provides, in part, as follows:

> **104. (1) Application to the Commission**—On application by an interested person, if the Commission considers that a person or company has not complied with, or is not complying with, a requirement under this Part *or the regulations related to this Part*, the Commission may make an order… [emphasis added].

[77] The question we must determine is whether section 104 of the Act applies to related party transactions. It will apply to related party transactions if the provisions of MI 61-101 applicable to related party transactions are regulations "related to" Part XX of the Act. We agree with Staff that we should apply a purposive approach to the interpretation of the Act and, in doing so, we should consider the regulatory objectives of the Act. As stated in *Bell ExpressVu*, the proper approach to interpretation is as follows:

> In Elmer Driedger's definitive formulation, found at p. 87 of his *Construction of Statutes* (2nd ed. 1983):
>
> > Today there is only one principle or approach, namely, the words of an Act are to be read in their entire context and in their grammatical and ordinary sense harmoniously with the scheme of the Act, the object of the Act, and the intention of Parliament.
>
> Driedger's modern approach has been repeatedly cited by this Court as the preferred approach to statutory interpretation across a wide range of interpretive settings: [citations omitted] …
>
> *Bell ExpressVu Limited Partnership v. Rex*, [2002] S.C.J. No. 43 ("***Bell Express Vu***") at para. 26.

[78] We note that the question we must address is not whether the Commission has authority to implement rules related to related party transactions. The Commission clearly has that authority and has exercised it in implementing the provisions of MI 61-101 as they relate to related party transactions. Nor, in our view, is the question whether related party transactions raise some of the same or similar regulatory concerns as those raised by insider bids and issuer bids. They clearly do raise similar concerns and that is why related party transactions are included in MI 61-101. We note, however, that MI 61-101 imposes the requirement for Minority Approval only in connection with related party transactions and business combinations and not insider bids or issuer bids.

[79] We do not think that references in the Commission's rule-making authority, the Rules of Procedure or the numbering system for regulatory instruments are particularly helpful in determining the application of a power such as that contained in section 104 which is conferred by the Act.

[80] Section 104 grants very broad statutory authority to the Commission to intervene in and regulate transactions that are subject to it. Among other powers under that section, the Commission may order persons to comply with a requirement of Part XX or to restrain them from breaching a requirement of Part XX. The Commission does not have similar general authority to make compliance or restraining orders under any other provision of the Act.

[81] Part XX of the Act relates to take-over bids and issuer bids, including the early warning requirements. Nowhere does Part XX refer to or regulate related party transactions. Section 104 gives the Commission authority to intervene pursuant to regulations "related to" Part XX. There

is no question that portions of MI 61-101 relate to take-over bids and issuer bids. We also agree that the words "related to" should be given a broad interpretation, but the relevant subject matter of MI 61-101 must nonetheless have a sufficient nexus to Part XX of the Act.

[82] In our view, the Commission cannot expand its jurisdiction and authority under section 104 of the Act by including provisions regulating other types of transactions in a rule that also applies to take-over bids and issuer bids. There is nothing wrong, of course, in addressing different types of transactions in one rule, but in our view, doing so cannot expand the application of section 104.

[83] Section 104 provides extraordinary authority to the Commission to intervene in and regulate take-over bids and issuer bids and the other matters governed by Part XX of the Act. If it was intended that this authority also apply to other types of transactions, such as related party transactions, the Act would have done so expressly.

[84] In our view, the provisions of MI 61-101 applicable to related party transactions are not related to Part XX of the Act. This proceeding does not relate to a take-over bid or an issuer bid, but rather to a series of related party transactions. Accordingly, in our view, the Commission does not have authority to make an order under section 104 of the Act restraining MID from entering into future related party transactions.

[85] Accordingly, we dismissed the Applications to the extent that they were brought under section 104 of the Act.

[86] We would add that there is no doubt that our public interest jurisdiction under section 127 of the Act applies to related party transactions and the other types of transactions that are subject to MI 61-101.

C. Can the Applicants bring the Applications under Section 127 of the Act?

1. Submissions

The Applicants

[87] The Applicants submitted that they can properly bring the Applications under section 127 of the Act. The Applicants say that section 127 does not limit by its terms the right of private parties to bring an application under section 127. Accordingly, in their view, the Commission should not limit the availability of section 127.

[88] The Applicants submitted that the *Rules of Procedure* contemplate that an application may be brought under sections 104 and 127 of the Act by an applicant other than Staff. Rule 1.1 defines an "application" as follows: "'application' includes an application: (a) by Staff pursuant to section 127 of the Act; … (f) pursuant to section 104 and/or section 127 of the Act in connection with take-over bids, issuer bids and mergers and acquisitions transactions…"

[89] The Applicants submitted that there are other rules that contemplate the jurisdiction of a private party to bring an application, including sections 2.4 and 16.1(1) of the *Rules of Procedure*, which specify the manner in which certain applications pursuant to sections 104 and 127 of the Act are to be initiated by persons other than Staff.

[90] The Applicants further submitted that subsection 127(4) of the Act provides that "[n]o order shall be made under this section without a hearing, subject to section 4 of the *Statutory Powers Procedure Act*". The exceptions under the *Statutory Powers Procedures Act* ("**SPPA**") to when a hearing is required are dealt with in section 4.5 and section 4.6 of the SPPA. Each of these provisions requires that notice be given of an intention to deny the right to a hearing. In particular, section 4.5 of the SPPA deals with technical defects in the documents relating to the commencement of a proceeding, and subsection 4.5(2) of the SPPA requires notice to be given to the "party who commences a proceeding" if the tribunal or administrative staff intend to invoke that provision. Section 4.6 of the SPPA deals with the dismissal of a proceeding without a hearing on the basis that it is frivolous, vexatious, is commenced in bad faith, there is a lack of jurisdiction, or it is considered that some aspect of the statutory requirements for bringing a hearing have not been met. If the Commission (not Staff) intends to dismiss an application based on section 4.6 of the SPPA, there is a requirement under subsection 4.6(2) to give notice to the party who commences the proceeding and, under subsection 4.6(3), to provide an opportunity for such party to make written submissions in response.

[91] The Applicants submitted that these provisions of the SPPA therefore suggest that a person other than Staff may apply for relief under section 127. The Applicants also submitted that this interpretation is consistent with the purposes of the Act set out in section 1.1 to (a) provide protection to investors from unfair, improper or fraudulent practices, and (b) foster fair and efficient capital markets and confidence in the capital markets.

[92] The Applicants also submitted that there have been cases where private parties have brought applications under section 127 of the Act such as in connection with applications to cease trade a poison pill. Those applications are usually also brought simultaneously under section 104 of the Act.

MID

[93] MID submitted that private parties cannot bring an application under section 127 in a case such as this, which does not involve a take-over bid or issuer bid. MID concedes that applications can be brought under section 104 by private parties in connection with take-over bids or issuer bids, but the Applications do not relate to take-over bids or issuer bids.

[94] MID submitted that public policy is against allowing private parties to use section 127 of the Act for private purposes. The authority granted under section 127 is in the nature of an enforcement power that should be available only in proceedings initiated by Staff.

Staff

[95] Staff submitted that, while rare, there may be limited circumstances that would warrant permitting a private party to make an application under section 127. Staff submitted that, in order for a private party to be entitled to initiate a section 127 proceeding (i) the matter at issue must be in relation to an imminent or unfolding transaction that falls within the policy framework of securities regulation, (ii) the applicant must be a proper party with a direct interest in the outcome of the matter, and (iii) the Commission must conclude that it is a proper forum in which to both hear the application and to grant a remedy. Staff submitted that section 127 proceedings brought in those circumstances are not enforcement proceedings.

[96] Staff also submitted that the circumstances where a private party should be able to bring an application under section 127 of the Act were properly articulated in *Cablecasting*, where the Commission stated that:

> [t]he Commission acknowledged that it has jurisdiction to exercise its section 144 authority [the predecessor to section 127] on application by a minority shareholder, but stressed that its willingness to hear this specific application was premised on the statement alluded to above, made by Mr. Salter as Director of the Commission, that the application was of urgency and had sufficient merit to justify consideration by the Commission. This is, in the view of the Commission, the appropriate procedure by which matters and requests such as this should come before it.
>
> *Re Cablecasting Ltd.* (1978), O.S.C.B. 37 ("***Cablecasting***") at page 40.

[97] In Staff's submission, matters of "urgency" would suggest that a "live" or unfolding transaction is required. If a matter involves past conduct alone, Staff submitted that it would be difficult to imagine a situation where the remedy sought would be urgent. Allowing private parties unfettered access to the Commission under section 127 would, in Staff's submission, be tantamount to permitting private enforcement of the Act. Staff submitted that there must be some compelling reason why the Commission should grant access to a private party under section 127 and, in Staff's submission, that requires an unfolding transaction that raises issues of public interest or alleged breach of the Act or regulations.

[98] Staff submitted that the only imminent or unfolding transaction raised in the Applications that may invoke the public interest mandate of the Commission under section 127 is the Amended DIP Financing.

2. Analysis and Conclusion

[99] Section 127 of the Act sets forth the types of public interest orders that may be made by the Commission. That public interest power is most often applied to regulatory and enforcement matters and applications for that purpose are usually brought by Staff.

[100] Unlike section 104 of the Act, section 127 does not expressly provide that an application can be brought by an "interested person". Rule 2.1 of the *Rules of Procedure* contemplates that applications under section 127 are to be commenced by Staff by issuing a statement of allegations.

[101] At the same time, applications by persons other than Staff have been permitted by the Commission under section 127, in some circumstances, where the applicants wished to obtain one of the types of orders available under that section, usually a cease trade order or an order to remove exemptions in respect of a particular transaction. That has been the case, for example, in poison pill hearings held by the Commission. Rule 2.4 of the Rules of Procedure contemplates that an application pursuant to section 127 may be made by a person other than Staff *in connection with a take-over bid or issuer bid*. That suggests that persons other than Staff can bring an application under section 127 in those circumstances.

[102] It is not completely clear to us what the reference in subsection 127(4) of the Act to section 4 of the SPPA is intended to import. The Applicants submitted that reference is to sections 4.5 and 4.6 of the SPPA which thus suggests that third parties may bring an application under section 127. One can argue, however, that at least certain paragraphs of sections 4.5 and 4.6 apply equally to an application brought by Staff under section 127, such as where there is a technical defect in the commencement of the proceeding, the proceeding is outside the jurisdiction of the Commission or some other statutory requirement has not been met. The general reference to section 4 of the SPPA also includes section 4.1 of the SPPA which provides that parties may consent to a decision of a tribunal without a hearing, a circumstance that may arise in a proceeding brought by Staff.

[103] Accordingly, in our view, the provisions of the SPPA do not assist us in coming to a conclusion whether persons other than Staff can bring an application under subsection 127 as a matter of right.

[104] The Supreme Court of Canada discussed the nature of the Commission's public interest jurisdiction under section 127 of the Act in *Committee for the Equal Treatment of Asbestos Minority Shareholders v. Ontario (Securities Commission)*, [2001] 2 S.C.R. 132 ("***Asbestos***"). We will not repeat all of that discussion. In summary, the Court indicated that the Commission's public interest jurisdiction provides a broad regulatory authority but one that is not unlimited. Its exercise must be animated by the purposes of the Act. The purpose of the public interest jurisdiction is neither remedial nor punitive. Rather, its purpose is to restrain future conduct that is likely to be prejudicial to investors or the public interest in fair and efficient capital markets.

[105] The Supreme Court of Canada stated in *Asbestos* that:

> In summary, pursuant to s. 127(1), the OSC has the jurisdiction and a broad discretion to intervene in Ontario capital markets if it is in the public interest to do so. However, *the discretion to act in the public interest is not unlimited*. In exercising its discretion, the OSC should consider the protection of investors and the efficiency of, and public confidence in, capital markets generally. *In addition, s. 127(1) is a regulatory provision. The sanctions under the section*

> *are preventive in nature and prospective in orientation. Therefore, s. 127 cannot be used merely to remedy Securities Act misconduct alleged to have caused harm or damages to private parties or individuals* [emphasis added].
>
> *Asbestos, supra* at para. 45.

[106] The Commission is also entitled to consider both specific and general deterrence in exercising its public interest jurisdiction. The Supreme Court of Canada confirmed in *Cartaway* that "it is reasonable to view general deterrence as an appropriate, and perhaps necessary, consideration in making orders that are both protective and preventative" (*Re Cartaway Resources Corp.*, [2004] 1 S.C.R. 672 ("***Cartaway***") at para. 60).

[107] In our view, persons other than Staff are not entitled as of right to bring an application under section 127 where the application is, at its core, for the purpose of imposing sanctions in respect of past breaches of the Act or past conduct alleged to be contrary to the public interest. In our view, those purposes are regulatory in nature and enforcement related and such applications should be able to be brought as of right only by Staff. Section 127 should not be used merely to remedy misconduct alleged to have caused harm or damage to private persons.

[108] In our view, however, the Commission has discretion to permit an application to be brought by persons other than Staff under section 127. The question then, is in what circumstances the Commission should exercise that discretion?

[109] The Applications are not, at their core, brought merely for the purpose of imposing sanctions for past breaches of the Act or past misconduct. While the past conduct of MID is a central focus of the Applications, the order sought is future looking and prophylactic and not in the nature of simply an enforcement sanction. Rather, the Applications are brought for the purpose of preventing MID from completing the Amended DIP Financing and from entering into other future related party transactions with MEC, without obtaining Minority Approval. We note in this respect that MID has indicated that it may consider entering into future related party transactions with MEC in connection with the possible purchase of assets of MEC.

[110] We believe that the Applicants should be permitted to bring the Applications under section 127 for the following reasons:

(i) the Applications involve or relate to past and possible future related party transactions between MID and MEC, transactions regulated under MI 61-101;

(ii) the Applications involve alleged breaches by MID of MI 61-101, but are not purely enforcement in nature;

(iii) the relief sought is future looking in that it is intended to prevent completion of the Amended DIP Financing and other possible future related party transactions between MID and MEC, without Minority Approval;

(iv) the Commission appears to have the authority to impose an appropriate remedy in the circumstances (subject to addressing the arguments in this matter related to the Commission's authority to issue the requested order);

(v) the Applicants, as substantial shareholders of MID, were directly affected by the past conduct of MID and will be directly affected by the Amended DIP Financing and any future related party transactions; accordingly, the Applicants have a sufficiently direct interest in the outcome of the Applications; and

(vi) we are satisfied that it is in the public interest in the circumstances to hear the Applications.

[111] Accordingly, we concluded that the Applicants should be permitted to bring the Applications under section 127 of the Act in these circumstances.

D. Can the Commission Make the Order Requested under Section 127 of the Act?

1. Submissions

The Applicants

[112] The Applicants submitted that the Commission's powers under section 127 of the Act can be exercised based on past misconduct and that there is no requirement that there be a specific current or unfolding transaction to which an order would relate.

[113] The Applicants submitted that under subsection 127(1) of the Act, the Commission is given authority to make any one of a broad range of enumerated orders if, in its opinion, it is in the public interest to do so. Section 127(1)3 provides, in part, as follows:

> The Commission may make one or more of the following orders if in its opinion it is in the public interest to make the order or orders:
>
> …
>
> 3. An order that *any exemptions in Ontario securities law* do not apply to a person or company permanently or for such period as is specified in the order [emphasis added].

[114] Subsection 127(1)3 casts a wide net and includes "any exemptions in Ontario securities law". That provision is not qualified in any respect and clearly relates to the body of Ontario securities law as a whole.

[115] The Applicants submitted that paragraph (g) of section 5.1 of MI 61-101 (relating to downstream transactions) clearly amounts to an exemption from Ontario securities law. The essence of section 5.1 is to grant exemptions from the requirements of Part 5 of MI 61-101. To suggest that section 127 is limited to only "enumerated" exemptions flies in the face of the principles underlying the Act.

MID

[116] MID submitted that the Commission's role under section 127 is to restrain future conduct that is likely to be prejudicial to the public interest. MID referred to *Asbestos* and submitted that

section 127 is a regulatory provision that should not be used merely to remedy past misconduct alleged to have caused harm to private parties.

[117] MID also referred to *Mithras* where the Commission described its public interest jurisdiction and role as follows:

> As a result, we see no basis at all upon which to make any order against any of the Respondents in respect of their modified structure. That structure may (or may not) have breached the terms of clause 14(g). But that is not the point. *Under sections 26, 123 [now section 127] and 124 of the Act, the role of this Commission is to protect the public interest by removing from the capital markets – wholly or partially, permanently or temporarily, as the circumstances may warrant - - those whose conduct in the past leads us to conclude that their conduct in the future may well be detrimental to the integrity of those capital markets. We are not here to punish past conduct; that is the role of the courts, particularly under section 118 of the Act. We are here to restrain, as best we can, future conduct that is likely to be prejudicial to the public interest in having capital markets that are both fair and efficient. In so doing we must, of necessity, look to past conduct as a guide to what we believe a person's future conduct might reasonably be expected to be; we are not prescient, after all"* [emphasis added].
>
> *Re Mithras Management (1990)*, 13 O.S.C.B. 1600 ("***Mithras***") at para. 13.

[118] MID submitted that the Applications relate primarily to alleged past breaches of MI 61-101 and that, accordingly, the Commission has no jurisdiction to issue, and should not issue, the order requested under section 127. MID also submitted that such an order can be issued only with respect to a future transaction if that transaction is abusive. MID submitted that there is no such abusive transaction before us.

MEC

[119] MEC submitted that the Commission's discretion to grant relief under section 127 of the Act ought to be exercised in a forward-looking manner, and not retrospectively based on past conduct, as asserted by the Applicants.

Staff

[120] Staff submitted that the only imminent or unfolding transaction raised in the Applications which may invoke the Commission's public interest jurisdiction is MID's intention to complete the Amended DIP Financing.

2. Analysis and Conclusion

[121] The principles reflected in *Asbestos* and *Mithras* have been endorsed in numerous Commission and court decisions. We accept *Asbestos* and *Mithras* as setting forth the correct

principles. As discussed above, we recognise that our public interest jurisdiction is not unlimited and must be exercised within our regulatory mandate under the Act. That mandate, as specified in section 1.1 of the Act, is "(a) to provide protection to investors from unfair, improper or fraudulent practices, and (b) to foster fair and efficient capital markets and confidence in capital markets".

[122] One of our principal regulatory objectives is to prevent future conduct that may be detrimental to investors or to the integrity of the capital markets. In addition, specific and general deterrence are also appropriate regulatory objectives in issuing an order under section 127 (see *Cartaway*, *supra*).

[123] In this case, the allegation is that MID contravened MI 61-101 by failing to obtain Minority Approval for the November Transactions, the March Transactions and the Amended DIP Financing. The Applicants say, as a result, that we should prevent MID from entering into future related party transactions with MEC, without Minority Approval, in reliance upon any exemption otherwise available under MI 61-101. That is to say that we should, in effect, restrain possible future related party transactions even if they could otherwise be carried out in full compliance with MI 61-101 without the need for Minority Approval.

[124] In our view, we have the legal authority to issue the order requested by the Applicants. We believe that, where there have been clear violations of MI 61-101 (or a provision of the Act), the Commission can remove exemptions that might otherwise be available to a person in respect of future transactions where it is satisfied that to do so is in the public interest. We frequently make such orders in enforcement proceedings removing exemptions or cease trading specified persons or securities. We do that to prevent those persons from causing future harm to investors by participating in our capital markets and as a matter of specific and general deterrence. While this matter is not purely an enforcement matter, in our view, similar principles apply.

[125] We have discussed above the nature of our public interest jurisdiction and our reasons for concluding that it is appropriate to permit the Applicants to bring the Applications under section 127 (see, in particular, paragraphs 104 to 106 and 110 of these reasons). In our view, that discussion and the comments we refer to from *Asbestos* apply with equal force to the question of whether we have the authority to grant the order requested under section 127.

[126] In our view, in order for us to exercise our authority under section 127 in circumstances such as these, it is not necessary for there to be a specific current and unfolding transaction. Having said that, the Amended DIP Financing is a current transaction the completion of which is conditional upon the Commission rendering a decision in favour of MID in connection with the Applications and MID has indicated that it may enter into future related party transactions with MEC with respect to the possible purchase of assets from MEC. That is sufficient, in our view, to distinguish the circumstances before us from a purely enforcement proceeding.

[127] We recognise, however, that issuing the order requested by the Applicants would be an extraordinary action and that we would do so only where there has been a clear and flagrant breach of MI 61-101. The general principle that we apply is to issue the least intrusive order that is sufficient in the circumstances to accomplish our regulatory objectives. We agree with Staff

that we should exercise extreme caution in issuing an order that could cause significant financial harm to a number of persons (including third parties) and that would have the effect of significantly restricting future transactions that are being carried out in full compliance with Ontario securities law.

[128] In conclusion, in our view, we have the authority to issue the order requested by the Applicants under section 127 of the Act.

E. The Relevant Provisions of MI 61-101

[129] This matter required us to interpret and apply the provisions of MI 61-101 to the transactions before us. In doing so, we must give effect to the language of the Instrument but we must do so in the context of the regulatory objectives of MI 61-101. We must also consider the true substance and economic effect of the transactions that are being challenged.

[130] Our approach to interpreting and applying MI 61-101 should be as articulated by the Commission in *Federal Navigation* as follows:

> In conclusion, the decision of the Commission has been based upon an interpretation of the provisions of the By-law arrived at in light of the Commission's understanding of the philosophy and the intent behind the rules established by those provisions. In restating the basic tenets or general principles discussed in the Kimber Report, the Commission wishes [forcibly] to draw to the attention of the public that, although technical interpretation is necessary, it is the expectation of the Commission that the participants in the capital markets of this province will be guided by the basic philosophy and rationale from which the securities laws of this province were developed. The sophisticated gloss of technicality must not be used to obscure the true intent and import of the basic philosophies that underlie the securities laws of the province. Technical interpretations that run contrary to these basic philosophies and principles will not be acceptable to the Commission.
>
> *Re Federal & Commerce Navigation Ltd.* (1981), 1 O.S.C.B. 20 ("***Federal Navigation***") at paras. 25-26.

[131] The purpose of MI 61-101 and its predecessors is to regulate specific transactions, such as related party transactions and business combinations, that are capable of being abusive or unfair to minority shareholders (see section 1.1 of Companion Policy 61-101 CP – to MI 61-101 (the "**Companion Policy**") and *Re Sears Canada Inc.* (2006), 22 B.L.R. (4th) 267, aff'd (2006), 21 B.L.R. (4th) 311 (Ont. Div. Ct.) ("**Sears**") at para. 256).

[132] Part 5 of MI 61-101 applies to certain related party transactions. A related party transaction includes transactions between a controlling shareholder such as MID, and an entity that it controls, such as MEC. The term "related party transaction" is defined in section 1.1 of MI 61-101, and provides in part as follows:

> "related party transaction" means, for an issuer, a transaction between the issuer and a person that is a related party of the issuer *at the time the transaction is agreed to*, whether or not there are also other parties to the transaction, as a consequence of which, either through the transaction itself or together with connected transactions, the issuer directly or indirectly
>
> (a) purchases or acquires an asset from the related party for valuable consideration,
> …
>
> (j) borrows money from or lends money to the related party, or enters into a credit facility with the related party,
> …
>
> (l) materially amends the terms of an outstanding debt or liability owed by or to the related party, or the terms of an outstanding credit facility with the related party….[emphasis added].

[133] Part 5 of MI 61-101 does not prohibit related party transactions and the Commission does not view such transactions as being inherently unfair (see section 1.1 of the Companion Policy). Rather, MI 61-101 regulates certain related party transactions by giving minority shareholders two types of procedural protections. First, section 5.4 requires that an issuer proposing to carry out a related party transaction must obtain a formal valuation in respect of the subject matter of the transaction. Second, section 5.6 provides that a related party transaction shall not be completed without Minority Approval. These regulatory protections are intended to ensure fairness to minority shareholders and to limit the potential for abuse in related party transactions.

[134] Not all related party transactions require these protections. In some circumstances, conflict of interest or fairness concerns either may not be present or may not be sufficiently acute given the relative economic significance of the particular related party transaction to the issuer. The scope of application of MI 61-101 has been carefully defined to apply where there are significant concerns that conflicts of interest may arise that may result in unfairness or abuse to minority shareholders. At the same time, it is possible for the provisions of MI 61-101 to apply by their terms to a related party transaction that, in the particular circumstances, is not unfair or abusive to minority shareholders and that does not give rise to the concerns that MI 61-101 was intended to address.

[135] The related party transactions for which minority shareholder protections are not required under MI 61-101 are determined in one of two ways. First, some related party transactions are explicitly carved out of the application of Part 5 of MI 61-101 by section 5.1. Second, related party transactions may qualify for specific exemptions from Minority Approval or the requirement to prepare a formal valuation (under sections 5.5 and 5.7 of MI 61-101).

The Downstream Transaction Exception

[136] Section 5.1(g) of MI 61-101 provides as follows:

> This part does not apply to an issuer carrying out a related party transaction if
> …
> (g) the transaction is a downstream transaction for the issuer.

[137] A "downstream transaction" is defined in MI 61-101 as follows:

> … for an issuer, a transaction between the issuer and a related party of the issuer if, *at the time the transaction is agreed to*
>
> (a) the issuer is a control person of the related party; and
>
> (b) *to the knowledge of the issuer after reasonable inquiry*, no related party of the issuer, other than a wholly-owned subsidiary entity of the issuer, *beneficially owns or exercises control or direction over*, other than through its interest in the issuer, more than five per cent of any class of voting or equity securities of the related party that is a party to the transaction [emphasis added].

[138] There are two elements to the Downstream Exception. First, the issuer must be a control person of the related party with which it is transacting (the "**Transacting Related Party**") at the time the transaction is agreed to. Second, *to the knowledge of the issuer after reasonable inquiry*, no related party of the issuer may beneficially own or exercise control or direction over more than 5% of the voting or equity securities of a class of the Transacting Related Party (other than through its interest in the issuer).

[139] The Downstream Exception is based on the assumption that when an issuer enters into a transaction with a related party that it controls, the issuer will act in its own best interests, thus also benefiting its minority shareholders. For downstream transactions, there is no need to provide minority shareholders with procedural protections because there is no element of conflict of interest present.

[140] This underlying assumption may be jeopardized, however, when a related party of an issuer holds a direct interest in the Transacting Related Party. Where such an interest exists, the related party may have an economic incentive to exercise its control or influence to cause the issuer to enter into a transaction that is unfavourable to the issuer but that is favourable to the Transacting Related Party and thus benefits the related party. This conflict of interest could lead the issuer (notwithstanding the corporate law duties and obligations of its directors and officers) to ignore its best interests (and consequently those of its shareholders) with the result that the Transacting Related Party may obtain the benefits of a transaction (that also benefits the related party) while the costs are borne by the issuer and its shareholders. The requirement for Minority Approval and the valuation requirement apply to related party transactions in these circumstances.

[141] We have referred to the Downstream Exception in these reasons as an "exception" rather than an "exemption". MID argued that if the Downstream Exception applies, then MI 61-101

simply does not apply to the relevant transactions. That is in contrast to the Market Cap Exemption that exempts a transaction from the specific requirement for Minority Approval (and the requirement to prepare a formal valuation) but leaves the transaction otherwise subject to the applicable provisions of MI 61-101. In MID's submission, the latter is properly viewed as an "exemption" while the former is a carve out or an "exception". The distinction is relevant because the Commission's power under subsection 127(1)3 of the Act is to "order that *exemptions* contained in Ontario securities law do not apply …"[emphasis added].

[142] In our view, the Downstream Exception is, in legal effect and common parlance, an exemption contained in Ontario securities law (which, as defined, includes rules of the Commission) and should be treated as such. Accordingly, we believe we have authority to remove that exemption on the terms and conditions we determine to be in the public interest. We would add that, in any event, we have a cease trade power under section 127 that we believe could be exercised to accomplish the same objective.

The Market Cap Exemption

[143] Sections 5.5(a) and 5.7(a) of MI 61-101 exempt an issuer from complying with the requirements for Minority Approval and for the preparation of a formal valuation where "at the time the transaction is agreed to, neither the fair market value of the subject matter of, nor the fair market value of the consideration for, the transaction … exceeds 25 per cent of the issuer's market capitalization…" determined in accordance with MI 61-101. "Market capitalization" of an issuer is defined in section 1.1 of MI 61-101.

[144] The Market Cap Exemption establishes the minimum size for a related party transaction for which Minority Approval and a formal valuation are required under MI 61-101. Where neither the fair market value of the subject matter of the related party transaction, nor the consideration for the transaction, exceeds 25% of the issuer's market capitalization, MI 61-101 accepts that the costs of complying with the Minority Approval and formal valuation requirements outweigh the potential benefits of obtaining that approval or such a valuation. The costs of complying with the Minority Approval requirement include the actual costs of calling and holding a shareholders' meeting, the delay required in a transaction in order to obtain that approval and the uncertainty in whether the shareholders will approve the transaction and that it will proceed. The costs of preparing a formal valuation include the fees of the independent valuer and the delay necessary for the valuer to complete its work.

[145] Accordingly, MI 61-101 reflects through the terms of the Market Cap Exemption a balancing of costs and benefits, and an issuer is required to obtain Minority Approval and a formal valuation only in respect of very substantial related party transactions.

[146] In determining whether an issuer is eligible for the Market Cap Exemption, an issuer must aggregate the fair market value of any "connected transactions" that are also related party transactions (see section 5.5(a)(iii) of MI 61-101).

[147] "Connected transactions" are defined in section 1.1 of MI 61-101 as "two or more transactions that have at least one party in common and (a) are negotiated or completed at

approximately the same time or (b) the completion of at least one of the transactions is conditional on the completion of each of the other transactions". There is no doubt that this definition is, by its terms, very broad in potential application.

Conclusions

[148] There is no dispute that MID is a control person with respect to MEC or that the November Loan, the DIP Financing and the Amended DIP Financing were related party transactions for purposes of MI 61-101. The Loan Extension was also a related party transaction if it constituted a material amendment to the existing loans to which it related. The November Reorganization Proposal included certain transactions that would have been related party transactions if they had been carried out. The Stalking Horse Bid would also have been a related party transaction if assets of MEC had been purchased by MID under that bid.

[149] Clearly, there are different rationales for the Downstream Exception and the Market Cap Exemption. Either exemption may, however, apply to a related party transaction and exempt that transaction from the requirement for Minority Approval and for a formal valuation. Accordingly, the principal question we must determine is whether, at the relevant time, either the Downstream Exception or the Market Cap Exemption was available to MID in respect of the November Transactions, the March Transactions and the Amended DIP Financing.

[150] As noted above, the Downstream Exception and the Market Cap Exemption apply to exempt a related party transaction from both the requirement to obtain Minority Approval and the requirement to prepare a formal valuation. Because the submissions made to us focused primarily on the requirement for Minority Approval, we will principally address that requirement in these reasons. If we conclude that either exemption was available to exempt MID from the requirement to obtain Minority Approval, that exemption also applies to exempt MID from the requirement to prepare a formal valuation.

F. Was the Downstream Exception Available to MID?

1. Submissions

The Applicants

[151] The Applicants submitted that, commencing with the Azalea Trust Transaction, MID relied upon multiple artificial transactions in an attempt to circumvent the Minority Approval requirement for related party transactions under MI 61-101. The purpose of those transactions was to deprive MID's minority shareholders of their right to vote on and object to the November Transactions, the March Transactions and the Amended DIP Financing and the result has been substantial destruction of MID shareholder value through MID's continued support for a now bankrupt subsidiary. Since November 25, 2008, MID has advanced or agreed to advance to MEC the November Loan of up to US$125 million, the Loan Extension relating to approximately US$312 million of existing loans, the DIP Financing of up to US$62.5 million (later reduced to US$38.4 million), and the additional DIP financing of up to US$28 million. Under the Stalking

Horse Bid, MID offered to purchase assets from MEC with a purchase price of approximately US$195 million.

[152] The Applicants submitted that the Downstream Exception was not available to MID in connection with the relevant related party transactions because the Azalea Trust Transaction was an artificial transaction and a sham that did not result in the disposition by Fair Enterprise of the Fair Enterprise MEC Shares. The Applicants say that Fair Enterprise simply "parked" the Fair Enterprise MEC Shares with the Azalea Trust. They also submitted that MID failed to make reasonable inquiry with respect to the ownership of the Fair Enterprise MEC Shares and the terms of the Azalea Trust Transaction.

[153] The Applicants submitted that notwithstanding the Azalea Trust Transaction, MID continued to beneficially own the Fair Enterprise MEC Shares. They argued that, as a result of the breach by the Azalea Trust of the Disposition Covenant, and the non-recourse nature of the Promissory Note, MID had the right to acquire the Fair Enterprise MEC Shares. Under MI 61-101 and section 90 of the Act, that right to acquire the shares is deemed to constitute beneficial ownership of the shares.

[154] The Applicants submitted that the Commission should find that the Azalea Trust Transaction was ineffective to circumvent the Minority Approval requirement of MI 61-101. In addition, based on MID's past misconduct, the Applicants submitted that the Commission should exercise its public interest authority to prevent any further abuse by MID through future related party transactions with MEC.

MID

[155] MID submitted that the Azalea Trust Transaction was not artificial, contrived or lacking in *bona fides*, nor designed to frustrate the underlying philosophy of MI 61-101 or the reasonable expectations of the shareholders of MID.

[156] MID submitted that there is nothing abusive, illegal, untoward or improper with parties structuring a transaction so as to ensure that they comply in every respect with potentially available exemptions or exclusions in MI 61-101, so long as the transactions comply with applicable law.

[157] MID submitted that, in any event, at the time of the Azalea Trust Transaction, it made reasonable inquiry as to whether any related party of MID beneficially owned or exercised control or direction over more than 5% of any class of voting or equity securities of MEC. MID says that Fair Enterprise represented to it that, as of November 26, 2008, it did not own any such interest. MID submitted that its legal counsel (i) made inquiries by telephone and by e-mail (the e-mail exchange is described in paragraph 41 of these reasons), (ii) reviewed the draft news release to be issued by Azalea Trust in connection with the Azalea Trust Transaction, and (iii) reviewed subsequent public securities filings made by members of the Stronach Group, all of which confirmed that neither Mr. Stronach nor any other member of the Stronach Group beneficially owned or exercised control or direction over more than 5% of any class of voting or equity securities of MEC. As a result of and based on those reasonable inquiries, MID submitted

that it was entitled to rely on the Downstream Exception regardless of whether Fair Enterprise continued to beneficially own or exercise control or direction over the Fair Enterprise MEC Shares.

[158] MID submitted that the November Transactions, the March Transactions and the Amended DIP Financing all qualified for the Downstream Exception and, accordingly, were not subject to the requirement for Minority Approval or for the preparation of a formal valuation.

Fair Enterprise

[159] Fair Enterprise submitted that the Downstream Exception applied to all of the relevant related party transactions between MID and MEC. Fair Enterprise did own more than 5% of the voting or equity securities of MEC through its ownership of the Fair Enterprise MEC Shares, but Fair Enterprise disposed of those shares on November 25, 2008 pursuant to the Azalea Trust Transaction. Fair Enterprise submitted that (i) the Azalea Trust Transaction was a valid and *bona fide* sale transaction under which Fair Enterprise disposed of the Fair Enterprise MEC Shares, and (ii) Fair Enterprise did not subsequently regain ownership of those shares. Accordingly, Fair Enterprise says that MID was entitled to rely on the Downstream Exception with respect to the November Transactions, the March Transactions and the Amended DIP Financing.

Staff

[160] Staff submitted that the November Transactions, the March Transactions and the Amended DIP Financing did not exploit gaps or loopholes in MI 61-101. Staff submitted that the Stronach Group's motivation for disposing of the Fair Enterprise MEC Shares is irrelevant to whether the Downstream Exception was available. MI 61-101 does not prevent issuers from organizing their affairs to create the factual basis for an exemption available under the Instrument. If the factual basis for reliance on the Downstream Exception exists, there is no need to obtain Minority Approval for the relevant related party transactions.

[161] Staff also submitted that the Azalea Trust Transaction did not undermine the reasonable expectations of MID shareholders. There is no evidence to suggest that MID shareholders had any reasonable expectation that the Stronach Group would maintain its ownership of the Fair Enterprise MEC Shares. As a result, Staff submitted that it was reasonable to expect that a sale of the Fair Enterprise MEC Shares could happen at any time, such that the Downstream Exception would be available to MID.

[162] Staff submitted that MID made reasonable inquiry at the time it entered into the November Transactions as to the ownership and control or direction of the Stronach Group over shares of MEC and therefore qualified for the Downstream Exception. Staff submitted that it is not unreasonable for an issuer to rely on confirmation from legal counsel for a related party about the facts forming the basis for the availability of the Downstream Exception, unless the circumstances suggest the need for further inquiry.

2. Analysis and Conclusion

[163] The Applicants submitted that the Azalea Trust Transaction was an artificial transaction and a sham that did not result in the disposition by Fair Enterprise of the beneficial ownership of the Fair Enterprise MEC Shares. If that is the case, the Downstream Exception was not available by its terms for the November Transactions or the March Transactions. (The Downstream Exception would have been available for the Amended DIP Financing because the Fair Enterprise MEC Shares were sold by Azalea Trust to a third party on June 29, 2009 (see paragraph 54 of these reasons)). The Applicants also say that the Fair Enterprise MEC Shares were simply "parked" with the Azalea Trust to ostensibly permit the relevant related party transactions to take place without Minority Approval.

[164] The Applicants alleged that the Azalea Trust Transaction was not entered into on normal or usual commercial terms, thus demonstrating that the transaction was a sham and that it was ineffective to transfer the beneficial ownership of the Fair Enterprise MEC Shares to the Azalea Trust. In particular, the Applicants questioned the following aspects or terms of that transaction:

(i) the purchaser was a trust established for purposes of the Azalea Trust Transaction by Mr. Timothy Jones, the former mayor of Aurora, Ontario and a paid consultant to Neighbourhood Network, a community initiative founded by Belinda Stronach;

(ii) the Promissory Note representing the purchase price did not bear interest and was repayable on a non-recourse basis only out of the net proceeds of the sale of the Fair Enterprise MEC Shares;

(iii) the Fair Enterprise MEC Shares were to be sold by the purchaser as soon as practicable after November 25, 2008 (the date of the Azalea Trust Transaction) and in an orderly fashion, when permitted by applicable securities law; and

(iv) the net proceeds of sale in excess of the amounts due under the Promissory Note were to be donated to charity.

[165] The Applicants noted that the Fair Enterprise MEC Shares were not registered in the name of Azalea Trust until April 13, 2009, and that Azalea Trust did not sell the shares until June 29, 2009.

[166] There is certainly some merit to the submissions made by the Applicants with respect to this issue. Immediately prior to the Azalea Trust Transaction, Fair Enterprise held the beneficial ownership of the Fair Enterprise MEC Shares which had a fair market value of approximately $886,000. The Fair Enterprise MEC Shares were then sold (for no cash consideration and on a non-recourse basis) to a newly constituted trust of which the settlor and the sole director and officer of the trustee was an individual with at least some connection to the Stronach family. After that transfer, Fair Enterprise continued to have a direct economic interest in the Fair Enterprise MEC Shares with a fair market value of approximately $886,000, represented by the non-recourse Promissory Note. While Fair Enterprise no longer held an interest in the upside

value of the shares, in the circumstances, that value was clearly more theoretical than real. But if the fair market value of the shares fell, Fair Enterprise directly suffered that loss.

[167] Further, the Azalea Trust Transaction was only a first step in Fair Enterprise disposing of the beneficial ownership of the Fair Enterprise MEC Shares. The Azalea Trust was obligated by the Disposition Covenant to sell the shares as soon as practical after acquiring them, a step that the Azalea Trust was at best tardy in completing. Accordingly, one could say that Fair Enterprise "parked" the Fair Enterprise MEC Shares with the Azalea Trust by disposing of the beneficial ownership of those shares in technical legal terms but, in true economic terms, little changed. Applicants also noted that, on March 27, 2009, Fair Enterprise released the Azalea Trust from its obligations under the Promissory Note and each party mutually released all claims arising in connection with the Azalea Trust Transaction. That thereby ended any interest Fair Enterprise then had in the Fair Enterprise MEC Shares.

[168] We note, however, that there is no evidence to suggest that the Azalea Trust Transaction was other than what it appeared to be or that there was any attempt to disguise the true nature of it. That transaction was documented and publicly announced and there appears to be no dispute as to what the specific terms of the transaction were (there is, of course, a dispute as to the legal effect of those terms).

[169] The Azalea Trust Transaction appears to have been a *bona fide* transaction structured as it was in order to permit Fair Enterprise to dispose of the Fair Enterprise MEC Shares and to gift any proceeds in excess of the then fair market value to charity. Those objectives substantially dictated the terms of the Azalea Trust Transaction. While the terms of that transaction may not have been normal commercial terms, that does not mean that the transaction was not *bona fide*. It did not purport to be a normal commercial transaction. The objective of the transaction was to attempt to align the interests of the Stronach Group with the interests of the other shareholders of MID by disposing of the beneficial ownership of the Fair Enterprise MEC Shares. If the Azalea Trust Transaction accomplished that purpose, the Stronach Group would have had no interest in MEC except through its ownership of shares of MID. As a result, the interests of the Stronach Group and the other shareholders of MID would have been aligned and any potential concerns under MI 61-101 would have ceased to exist.

[170] There is nothing inappropriate in a person organizing its affairs or completing a *bona fide* transaction in order to qualify for the Downstream Exception. The Stronach Group wished to dispose of the Fair Enterprise MEC Shares, at least in part, to align its interests with those of the minority shareholders of MID. It chose to do so in a transaction that has some relatively unusual features. That is irrelevant, however, if Fair Enterprise, as a legal matter and as a matter of economic substance, disposed of the beneficial ownership of the Fair Enterprise MEC Shares and no longer exercised control or direction over those shares. If the Stronach Group did so by virtue of the Azalea Trust Transaction, then it no longer held an interest that created a potential conflict of interest or prevented reliance by MID on the Downstream Exception.

[171] In our view, the Azalea Trust Transaction was not an artificial transaction or a sham. While it is a close call, on balance, we are prepared to recognise the legal effect of the Azalea Trust Transaction in accordance with its terms. That legal effect was the disposition by Fair

Enterprise of the beneficial ownership of the Fair Enterprise MEC Shares to Azalea Trust. As discussed more fully below, however, we will not ignore the economic substance of the Azalea Trust Transaction in considering the application of MI 61-101.

Deemed Beneficial Ownership of the Fair Enterprise MEC Shares

[172] In determining the beneficial ownership of securities for purposes of the Downstream Exception, section 90 of the Act applies. Section 90 provides that:

> "in determining beneficial ownership … at any given date … the person or company shall be deemed to have acquired and to be the beneficial owner of a security … if the person or company … has a right … permitting … the person or company, whether or not on conditions, to acquire beneficial ownership of the security within 60 days … ".

[173] The Applicants submitted in an alternative argument that Fair Enterprise continued to be the beneficial owner of the Fair Enterprise MEC Shares after the completion of the Azalea Trust Transaction because Fair Enterprise had the right to acquire those shares as a result of Azalea Trust's breach of the Disposition Covenant. The argument is that, at least by the time of the March Transactions, the existence of that right meant that Fair Enterprise was deemed to be the beneficial owner of the Fair Enterprise MEC Shares within the meaning of section 90 of the Act and for purposes of the Downstream Exception.

[174] It seems to us that there are several problems with that submission. First, it is not clear that Azalea Trust was in breach of the Disposition Covenant. Certainly, Fair Enterprise was the party entitled to take that position and it did not allege any such breach. There was also some evidence before us as to why Azalea Trust did not or could not immediately dispose of the shares (see paragraph 50 of these reasons). Those considerations may have constituted a valid defence to any allegation by Fair Enterprise that Azalea Trust was in breach of the Disposition Covenant.

[175] Second, if there was a breach of the Disposition Covenant, it is not clear on the evidence before us that Fair Enterprise had the right, as a result, to acquire the Fair Enterprise MEC Shares within 60 days. It may have had a legal cause of action to require the disposition of the shares and to obtain the net proceeds. That, however, is not a specific right to acquire the shares. We did not see any express right of Fair Enterprise in the relevant legal documents to foreclose on the shares (that is, to take ownership of the shares in full settlement of the debt or obligation).

[176] Further, even if Fair Enterprise is viewed as having a right to acquire the shares by reason of the alleged default by Azalea Trust, there is no certainty that Fair Enterprise could, in fact, exercise that right by taking legal action and acquire beneficial ownership of the Fair Enterprise MEC Shares within 60 days.

[177] It does not seem to us that section 90 of the Act was intended to or should apply to the type of qualified legal rights Fair Enterprise would have had under the terms of the Promissory Note and the related documents if a default had occurred under them.

[178] Accordingly, we have concluded that Fair Enterprise was not deemed to beneficially own the Fair Enterprise MEC Shares, within the meaning of section 90 of the Act, after the Azalea Trust Transaction.

Control or Direction

[179] We must also address whether Fair Enterprise continued to exercise control or direction over the Fair Enterprise MEC Shares after the Azalea Trust Transaction. We have some concern that Fair Enterprise remained the registered owner of those shares until April 13, 2009 and that the relevant share certificates were not delivered to Azalea Trust when the Azalea Trust Transaction was completed (those certificates were not delivered until April 17, 2009). As a result, one can argue that Fair Enterprise continued to have the ability to exercise control or direction over those shares as the registered holder.

[180] The legal test we must apply under the Downstream Exception is whether at the relevant time Fair Enterprise "exercised" control or direction over the Fair Enterprise MEC Shares. That is typically taken to mean the ability to exercise voting or dispositive power over shares. Fair Enterprise did not have the legal right to exercise control or direction over the Fair Enterprise MEC Shares because Azalea Trust was the beneficial owner of them and that ownership was not qualified in any way. If Fair Enterprise had purported to exercise control or direction over the Fair Enterprise MEC Shares, that exercise would have been in contravention of Azalea Trust's rights as beneficial owner of the shares. Further, there is no evidence before us that Fair Enterprise actually exercised, or purported to exercise, any control or direction over the Fair Enterprise MEC Shares after the completion of the Azalea Trust Transaction.

[181] We note that the 13D filed by Azalea Trust after the Azalea Trust Transaction also contained the following disclosure:

> The Trustee has the sole power to vote or to direct the vote, and the sole power to dispose or direct the disposition of all MECA Shares [MEC Class A Shares] owned by the Trust. Mr. Jones, as the sole director and sole officer of the Trustee, may be deemed to have the sole power to vote or to direct the vote, and the sole power to dispose or direct the disposition of, all MECA Shares [MEC Class A Shares] owned by the Trust.

That is certainly not determinative of the issue for our purposes, but it does indicate Azalea Trust's view as to who exercised control or direction over the Fair Enterprise MEC Shares after the Azalea Trust Transaction.

[182] Based on the foregoing, in our view, Fair Enterprise did not, as a legal matter, beneficially own or exercise control or direction over the Fair Enterprise MEC Shares after completion of the Azalea Trust Transaction and Fair Enterprise did not, in fact, exercise control or direction over those shares after that transaction.

Reasonable Inquiry by MID

[183] The Applicants also alleged that MID failed to make reasonable inquiry in the circumstances with respect to the direct ownership by members of the Stronach Group of securities of MEC and the terms of the Azalea Trust Transaction. Having failed to do so, the Applicants submitted that MID could not rely on the Downstream Exception.

[184] There are a number of circumstances that might have led MID to make further inquiries with respect to the Stronach Group's direct interest in MEC. Those circumstances include the fact that MID knew that Fair Enterprise owned the Fair Enterprise MEC Shares, representing a direct 21.5% interest in the outstanding MEC Class A Shares, and that Fair Enterprise had purported to sell the Fair Enterprise MEC Shares, on the eve of the November Transactions, to a newly established trust. MID also knew that transaction was being effected, at least in part, to permit MID to rely on the Downstream Exception.

[185] In the circumstances, we believe that MID should have done more than simply rely on (i) telephone conversations and the brief e-mail exchange among legal counsel confirming their "understandings" with respect to the direct share ownership by the Stronach Group in MEC (see paragraph 41 of these reasons), (ii) a draft of the news release that was to be issued by the Azalea Trust publicly announcing the Azalea Trust Transaction (see paragraph 42 of these reasons for the terms of the release that was issued), and (iii) the subsequent public filings describing the Azalea Trust Transaction. That news release failed to make full disclosure of all of the key terms of the Azalea Trust Transaction (see paragraph 46 of these reasons) and review of those subsequent filings cannot assist MID in demonstrating reasonable inquiry at the time it purported to rely on the Downstream Exception. In our view, the circumstances suggested the need for further inquiry.

[186] MID has the onus of showing for purposes of the Downstream Exception that it made reasonable inquiry with respect to the direct share ownership by the Stronach Group in MEC. We are not prepared to conclude that MID has satisfied that onus in the circumstances. We believe that MID should have made more inquiries with respect to the specific terms of the Azalea Trust Transaction and that it should have received direct representations from the relevant related parties as to their direct ownership of MEC shares and as to any other facts supporting reliance by MID on the Downstream Exception.

[187] We note that if MID had satisfied its onus, it would have been entitled to rely on the Downstream Exception regardless of the terms of the Azalea Trust Transaction and regardless of whatever share interest the Stronach Group might have held directly in MEC. From a regulatory perspective, that entitlement has significant implications for the application of the substantive provisions of MI 61-101. If an issuer wants a "free pass" for a related party transaction based on its lack of knowledge of circumstances that are known to a related party, there may be an obligation to do more than was done here. We reiterate that the onus of showing reasonable inquiry was on MID. Market participants can expect the Commission to be sceptical of submissions made as to the limited knowledge of related parties when the Commission is assessing whether that onus has been satisfied, particularly in circumstances such as these.

[188] We would add that we have come to a conclusion on this issue without all of the evidence that we would have liked with respect to the specific knowledge of the various parties and their legal counsel and with respect to all of the telephone conversations and actions that may have taken place. It is difficult in an abbreviated proceeding such as this to determine exactly who knew what and when and whether that knowledge should be attributed as a legal matter to MID. We also recognise that the obligation to make reasonable inquiry under MI 61-101 is not the same as the obligation to make a reasonable investigation to establish a due diligence defence with respect to a misrepresentation in a prospectus. The latter is clearly the more stringent requirement.

[189] If the Downstream Exception was, on the facts, available to MID, then it is irrelevant whether MID made reasonable inquiry with respect to what interests the Stronach Group may have held directly in MEC. In our view, the failure to make reasonable inquiry does not disqualify a person from relying on the Downstream Exception *if it is otherwise available on the facts*. It is the reverse that is true: if reasonable inquiry is made and a person has no knowledge to the contrary, that person is entitled to rely on the responses to the inquiry in determining the availability of the Downstream Exception, regardless of what the actual facts and circumstances known to a related party may be.

Fair Enterprise's Continuing Economic Interest in MEC

[190] The legal conclusion that Fair Enterprise no longer beneficially owned or exercised control or direction over the Fair Enterprise MEC Shares after the Azalea Trust Transaction is not, however, the end of the analysis. As noted above, after the Azalea Trust Transaction, Fair Enterprise continued to have a direct economic interest in the Fair Enterprise MEC Shares through holding the Promissory Note. The amounts due under that note were payable only out of the net proceeds of the sale of the shares. Fair Enterprise did not have any interest in the upside, if the shares increased in value, but any such increase in value, in the circumstances, was very unlikely. But if the fair market value of the shares fell, Fair Enterprise directly suffered that loss. As discussed above, in economic substance, there was little change in the interest of Fair Enterprise in the Fair Enterprise MEC Shares as a result of the Azalea Trust Transaction (see the discussion in paragraphs 166 and 167 of these reasons).

[191] As a result, one can argue that the Stronach Group continued to have a direct economic interest in shares of MEC that could give rise to the type of potential conflict of interest that the related party transaction provisions of MI 61-101 were intended to address. We have not concluded that Fair Enterprise's continuing economic interest in the Fair Enterprise MEC Shares gave rise to an actual conflict of interest in the circumstances, but we believe that the on-going interest at least raises the question whether, as a matter of substance, the Downstream Exception ought to be available in respect of the November Transactions, the March Transactions and the Amended DIP Financing.

[192] Accordingly, we will address the application of MI 61-101 to those transactions on the assumption that the Stronach Group continued to have an interest in the Fair Enterprise MEC Shares that could have disqualified MID from relying on the Downstream Exception. In doing so, we will consider the spirit and intent of the provisions of MI 61-101 and we will approach the

matter in accordance with the following principles articulated by the Commission in *Sterling Centrecorp*:

> … the Commission needs to have regard to all of the facts, all of the policy considerations at play, all of the underlying circumstances of the case, and all of the interests affected by the matter and the remedy sought. As described above, section 91 of the Act and Rule 61-501 [now MI 61-101] fundamentally must be interpreted to ensure protection of the minority. At the same time, we recognize the Commission's broad mandate as articulated in the *Re British Columbia Forest Products* case:
>
> > 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 …
>
> *Re Sterling Centrecorp. Inc.* (2007), 30 O.S.C.B. 6683 ("***Sterling Centrecorp***.") at para. 212.

G. Was the Market Cap Exemption Available to MID in respect of the November Transactions?

1. Submissions

The Applicants

[193] The Applicants submitted that the Market Cap Exemption was not available to MID for the November Loan, the Loan Extension or the November Reorganization Proposal.

[194] The Applicants submitted that the November Loan and the Loan Extension constituted part of the same transaction or were connected transactions. The November Loan (US$125 million) and the Loan Extension (of US$312 million) together amount to US$437 million. That amount exceeded 25% of MID's market capitalization which, at the relevant time, was approximately US$146 million (determined in accordance with MI 61-101).

[195] The Applicants also submitted that the November Reorganization Proposal was a connected transaction to the November Loan and the Loan Extension.

MID

[196] MID submitted that the November Loan was a transaction which is separate from both the Loan Extension and the November Reorganization Proposal. On that basis, MID asserted that the November Loan qualified for the Market Cap Exemption. (As noted above, the November Loan was for US$125 million and 25% of MID's market capitalization at the relevant time was

approximately US$146 million.) MID also submitted that the November Loan, the Loan Extension and the November Reorganization Proposal are not "connected transactions" because the November Loan was not conditional upon the Loan Extension or the November Reorganization Proposal.

[197] MID also submitted that the Loan Extension was not a related party transaction in any event because the Loan Extension was not a material amendment of the terms of the existing loans to which it related (as referred to under clause (1) of the definition of "related party transaction" in MI 61-101). MID also submitted that the Loan Extension was not "an amendment" to the existing loans because the extension was made unilaterally by MID as it was legally entitled to do.

[198] MID also submitted that the November Reorganization Proposal was to be put to shareholders for approval, including Minority Approval, and, accordingly, should not be considered in determining whether the Market Cap Exemption was available for the November Loan or the Loan Extension.

Staff

[199] In Staff's submission, the evidence does not suggest that MID divided up the November Transactions to avail itself of the Market Cap Exemption. By definition, the November Loan and the Loan Extension were connected because they were negotiated at the same time and were between the same parties, but those transactions were not linked in substance. Staff submitted that the Commission should give that factor considerable weight in determining whether the Market Cap Exemption was available in respect of the November Loan, the Loan Extension and the November Reorganization Proposal.

2. Analysis and Conclusions as to the November Transactions

[200] As noted above, there is no dispute that the November Loan was a related party transaction between MID and MEC for purposes of MI 61-101. The Loan Extension was also a related party transaction if it constituted a material amendment to the existing loans from MID to MEC to which it related.

[201] The availability of the Market Cap Exemption is determined based on the fair market value of a transaction relative to the issuer's market capitalization. The purpose of the "connected transactions" concept is to link related transactions for this purpose and, among other things, to prevent an issuer from arbitrarily dividing up or staging a transaction in order to be able to rely on the Market Cap Exemption for each separate step or transaction. It is intended to capture transactions that are linked in substance but that may be divided as a matter of form. Accordingly, the concept of "connected transactions" is an anti-avoidance provision.

[202] At the same time, the definition of "connected transactions" is, by its terms, extremely broad and may capture transactions that, for legitimate business or economic reasons, should not be viewed as linked. While we are not prepared to limit the application of the concept to only transactions that are arbitrarily divided up or staged, we recognise that there may be transactions

captured by the breadth of the term that one can argue should not be appropriately linked for purposes of the Market Cap Exemption.

[203] We note that subsection 2.7(1) of the Companion Policy provides as follows:

> "Connected transactions" is a defined term in the Instrument, and reference is made to connected transactions in a number of parts of the Instrument. For example, subparagraph (a)(iii) of section 5.5 of the Instrument requires connected transactions to be aggregated, in certain circumstances, for the purpose of determining the availability of the formal valuation exemption for a related party transaction that is not larger than 25 per cent of the issuer's market capitalization. In other circumstances, it is possible for an issuer to rely on an exemption for each of two or more connected transactions. However, we may intervene if we believe that a transaction is being carried out in stages or otherwise divided up for the purpose of avoiding the application of a provision of the Instrument.

That paragraph suggests that the Commission expects connected transactions to be aggregated for purposes of determining the availability of the Market Cap Exemption but that "in other circumstances", it is possible for an issuer to rely on an exemption for two or more transactions that might be viewed as connected. However, in the latter case, the Commission may intervene if a transaction is being carried out in stages or is otherwise divided up for the purpose of avoiding the application of a provision of the Instrument.

[204] In our view, the November Loan and the Loan Extension are connected transactions within the meaning of MI 61-101. They were both negotiated and completed at the same time, were between the same parties and related to the on-going financing of MEC. They are clearly linked in substance from a business perspective. While there is no suggestion that they were structured as separate transactions for the purpose of avoiding the requirement for Minority Approval, that is not a condition precedent to concluding that two transaction are connected transactions for purposes of the Market Cap Exemption. As we noted above, the definition of "connected transactions" is very broad and, in our view, was intended to capture, at least as a threshold matter, transactions such as the November Loan and the Loan Extension.

The Loan Extension

[205] MID argued, however, that the Loan Extension was not a related party transaction because it was not a material amendment to the relevant loans.

[206] The Loan Extension extended the repayment of the existing loans by four months, from December 1, 2008 to March 31, 2009. It is important to note, however, that at the time of the Loan Extension, it was extremely unlikely that MEC would have been able to repay the existing loans. We do not believe there is any dispute as to that conclusion and we note in this respect that (i) the November Loan was intended, in part, to keep MEC operating until MID shareholders could vote on the November Reorganization Proposal, (ii) these events were occurring in the midst of the 2008 global credit crisis, and (iii) MEC ultimately filed for bankruptcy protection

before the end of the extension period. In the circumstances, MID could have simply refused to extend the loans and, as a result, the loans would have gone into default. In that event, there would have been no amendment to the loans (arguably constituting a related party transaction) and there would have been no change in the economic circumstances: MEC would nonetheless have owed MID approximately US$312 million and it is extremely unlikely that MEC would have been able to repay that amount.

[207] In the result, we believe that there is a reasonable basis to conclude that the Loan Extension was not, from MID's perspective, a material amendment to the existing loans because they likely could not have been repaid by MEC in any event. (We believe that the Loan Extension was a material amendment to the existing loans from the perspective of MEC.) That conclusion would mean that the Loan Extension was not a related party transaction and was not therefore required to be included in determining the availability of the Market Cap Exemption to the November Loan. The result would be that the Market Cap Exemption was available in respect of the November Loan and the Loan Extension was not a related party transaction for purposes of MI 61-101.

[208] Further, we concluded above that the Loan Extension was a connected transaction to the November Loan. In our view, that does not necessarily mean that it should be viewed as a new loan to MEC in the amount of US$312 million (the principal amount outstanding under the existing loans) in applying the Market Cap Exemption. As noted above, it was extremely unlikely that MEC was going to be able to repay the existing loans in November, 2008. The business and economic decision that MID was making was whether to advance further funds to MEC to keep it operating until MID shareholders could vote on the November Reorganization Proposal. A secondary objective was to protect MID's existing secured loans to MEC. In our view, it is unrealistic in these circumstances to suggest that we should view the Loan Extension as, in effect, a new loan by MID to MEC in the amount of the existing loans. The economic substance of the November Loan and the Loan Extension was that an additional US$125 million was being loaned by MID to MEC so that MEC could continue its operations until MID shareholders could vote on the November Reorganization Proposal. In that context, the Loan Extension was simply extending the maturity date of the existing loans for four months. In our view, in economic substance, MID was not lending US$312 million to MEC by effecting the Loan Extension.

[209] The November Loan was for US$125 million and 25% of MID's market capitalization at the relevant time was approximately US$146 million. As a result, in our view, the Market Cap Exemption was available for both the November Loan and the Loan Extension (if one views the Loan Extension as a related party transaction).

The November Reorganization Proposal

[210] The November Reorganization Proposal was a relatively complex corporate reorganization that involved a number of different steps and transactions, not all of which constituted related party transactions. The November Reorganization Proposal was to be submitted to shareholders of MID for approval, including Minority Approval by the holders of MID Class A Shares. Unlike the November Loan and Loan Extension, those transactions were

not to proceed absent that approval. We note that the November Loan and the Loan Extension were not conditional upon the November Reorganization Proposal being approved or proceeding.

[211] As noted above, one of the principal reasons for the November Loan and the Loan Extension was to keep MEC's business operating until shareholders could vote on the November Reorganization Proposal. In that sense, the transactions were linked; but there was an important business reason for treating the November Loan and the Loan Extension as separate from the November Reorganization Proposal. The November Loan and the Loan Extension had to occur immediately if MEC was to continue operating its business. In contrast, the November Reorganization Proposal could await the shareholder vote. Clearly, the November Loan, the Loan Extension and the November Reorganization Proposal were not arbitrarily divided up or staged for purposes of avoiding the application of MI 61-101.

[212] There was insufficient evidence before us with respect to the specific terms of the November Reorganization Proposal to come to a definitive view as to the application of MI 61-101 to the various related party transactions that were to form part of that reorganization. It appeared to us, however, that there was some further negotiation of the terms of the November Reorganization Proposal that was required. Clearly, the November Reorganization Proposal was to be completed at a different time than the November Loan and the Loan Extension. We also note that the November Reorganization Proposal was ultimately abandoned by MID and, accordingly, no related party transaction contemplated as part of the November Reorganization Proposal actually occurred. Accordingly, there was no breach of the Minority Approval requirement by reason of the November Reorganization Proposal.

[213] For these reasons, we have concluded that the November Reorganization Proposal should not be viewed as a connected transaction to the November Loan or the Loan Extension in applying the Market Cap Exemption. Because the related party transactions that formed part of the November Reorganization Proposal did not proceed, no Minority Approval was required in connection with those transactions.

The Relevant Time

[214] The Applicants also argued that MID breached MI 61-101 because the relevant exemption was not available in respect of the November Transactions *at the time the transactions were agreed to* (as required by the terms of the definition of "downstream transaction" and by the terms of the Market Cap Exemption). Section 2.8 of the Companion Policy states that the time a transaction is agreed to "should be interpreted as the time the issuer first makes a legally binding commitment to proceed with the transaction, subject to any conditions such as security holder approval."

[215] The Applicants' argument was based on the assumption that the November Transactions were first agreed to by at least November 24, 2008. It follows, according to the Applicants, that because the Azalea Trust Transaction was not completed until November 25, 2008, the Downstream Exception and the Market Cap Exemption were not available at the time when the November Transactions were first agreed to.

[216] In our view, that is too technical an interpretation of MI 61-101. It makes sense to explicitly provide in that Instrument that it is to be interpreted and applied as of the date transactions are first agreed to (although one could conceive of other possible times that could have been chosen). Fixing such a time is particularly necessary because MI 61-101 requires various value determinations to be made in applying its terms. That does not mean, however, that the Instrument should be treated as establishing a completely inflexible rule for determining whether an exemption is available. We note that in this case, regardless of when the November Transactions were first agreed to (which may not be completely clear), they were not approved by the board of directors of MID until November 26, 2008, the day after the Azalea Trust Transaction.

[217] In any event, if after a transaction has been agreed to and before it is completed, steps are taken to ensure that an exemption is available under MI 61-101 for that transaction, there does not seem to us to be a reasonable basis to challenge the availability of that exemption, absent some abuse in relying on the exemption in the circumstances. There may be many different and legitimate reasons why a transaction would be agreed to in contemplation of the parties taking steps thereafter to ensure that, on completion, the transaction meets all regulatory requirements. We see no reason not to apply that principle in the circumstances before us.

Conclusions as to the November Loan, the Loan Extension and the November Reorganization Proposal

[218] Accordingly, in our view, the November Loan should be viewed as a single transaction for purposes of determining the availability of the Market Cap Exemption. The result is that the Market Cap Exemption was available for the November Loan and, accordingly, no Minority Approval or formal valuation was required under MI 61-101 in respect of it. As noted above, there is a reasonable basis to conclude that the Loan Extension was not a material amendment to the existing loans and was not therefore a related party transaction for purposes of MI 61-101. In any event, we concluded in the circumstances that the Loan Extension should not be viewed, in effect, as a new loan in the amount of the existing loans. Accordingly, no Minority Approval of the Loan Extension was required under MI 61-101.

[219] We also concluded that the November Reorganization Proposal should not be viewed as a connected transaction to the November Loan or the Loan Extension. Because the related party transactions contemplated as part of the November Reorganization Proposal did not proceed, there was no breach of the Minority Approval requirement in connection with those transactions.

[220] We would add that we do not agree with MID that because the Loan Extension was made unilaterally by MID, as it was entitled to do under the terms of its loans to MEC, that action did not constitute or should not be treated as an "amendment" to the existing loans for purposes of MI 61-101.

[221] As a result of our conclusions above with respect to the availability of the Market Cap Exemption, it is not necessary for us to decide whether, as a matter of substance, the Downstream Exception should have been available in respect of the November Transactions.

H. Was the Downstream Exception Available in respect of the March Transactions?

[222] There is no dispute that the DIP Financing and the Amended DIP Financing were related party transactions. The Stalking Horse Bid would also have been a related party transaction if MID had purchased assets from MEC under that bid.

[223] The DIP Financing and the Stalking Horse Bid were both agreed to at substantially the same time and involved or potentially involved related party transactions between MID and MEC. As noted above, the definition of "connected transactions" is very broad and, in our view, would as a threshold matter capture transactions such as the DIP Financing and the Stalking Horse Bid. Those transactions were, however, entered into for quite different business reasons: the DIP Financing was to fund the on-going operations of MEC while it was in bankruptcy while the Stalking Horse Bid contemplated the possible purchase by MID of certain assets of MEC. Those purchases would have occurred at fair market value as a result of the auction process that was contemplated. Those are considerations that, in the circumstances, may have led us to conclude that the DIP Financing and the Stalking Horse Bid should not be treated as connected transactions for purposes of the Market Cap Exemption. Because of our conclusions below, however, it was not necessary for us to come to a conclusion on that question.

[224] It is a different question whether, in substance, the Downstream Exception should be available in respect of the DIP Financing, the Stalking Horse Bid and the Amended DIP Financing. As noted above, Fair Enterprise continued to have a direct economic interest in the Fair Enterprise MEC Shares through the terms of the Promissory Note following the Azalea Trust Transaction. That interest could have potentially given rise to a conflict of interest of the nature intended to be addressed by MI 61-101.

[225] It is clear, however, that when MEC filed for bankruptcy protection on March 5, 2009, the Fair Enterprise MEC Shares became essentially worthless. MID reduced the carrying value of its equity interest in MEC to zero on that date. Azalea Trust subsequently sold the Fair Enterprise MEC Shares for $7,500 on June 29, 2009.

[226] Accordingly, in our view, when MEC filed for bankruptcy protection, the Fair Enterprise MEC Shares ceased to be a potential source of any conflict of interest between the Stronach Group and the minority shareholders of MID. We do not believe that, in the circumstances, it is reasonable to suggest that Fair Enterprise's continuing economic interest in those shares would have had any effect on how the Stronach Group conducted itself with respect to related party transactions between MID and MEC. MEC was indebted to MID in an amount of approximately US$372 million as at March 5, 2009. MID's principal objective was to protect and preserve the value of its interest as a secured lender to MEC. The Stronach Group had no other conflicting interest. Accordingly, in our view, upon the making of the Bankruptcy Filings, the Fair Enterprise MEC Shares ceased to give rise to any potential conflict of interest of the nature described in paragraph 140 of these reasons.

[227] We also note that, as a result of the Bankruptcy Filings, MID also ceased to be able to exercise its share interest as a control person of MEC.

[228] We would add that the Stalking Horse Bid was ultimately withdrawn without the purchase by MID of any assets under that bid. MI 61-101 provides that, absent an exemption, an issuer shall not carry out a related party transaction unless the issuer has obtained Minority Approval. However, if no related party transaction is actually carried out, the issuer has not offended this prohibition.

[229] Accordingly, in our view, the DIP Financing, the Stalking Horse Bid and the Amended DIP Financing each qualified for the Downstream Exception both as a legal matter in interpreting the provisions of the Downstream Exception (based on our conclusions in paragraph 182 of these reasons) and as a matter of substance in considering the circumstances at the time of those transactions (based on our conclusions in paragraph 226 of these reasons).

I. Were there Insider Trading Violations in connection with the Azalea Trust Transaction?

1. Submissions

The Applicants

[230] The Applicants alleged that the carrying out of the Azalea Trust Transaction violated the insider trading prohibitions in the Act. They submitted that such violations should prevent MID from relying on the Downstream Exception in the circumstances.

[231] The Applicants submitted that Fair Enterprise was in a "special relationship" with MEC because, among other things, Fair Enterprise was a party to the Azalea Trust Transaction, a step in implementing the November Transactions. As a result, Fair Enterprise had knowledge of the November Transactions and that knowledge constituted material undisclosed information. Fair Enterprise then traded with knowledge of that information in completing the Azalea Trust Transaction.

[232] The Applicants submitted that the disclosure of the terms of the November Transactions to Mr. Jones was not in the "necessary course of business" of Fair Enterprise (within the meaning of subsection 76(2) of the Act). The purpose of the disclosure to Mr. Jones was to facilitate the purported sale by Fair Enterprise of the Fair Enterprise MEC Shares to Azalea Trust. One of the reasons for selling the Fair Enterprise MEC Shares was to make the Downstream Exception available to MID in order to permit MID to complete the November Transactions.

[233] At the time of the Azalea Trust Transaction, there was also a trading blackout in effect with respect to securities of MEC under MID's corporate policies. According to the Applicants, MID also acted inappropriately in delegating to Fair Enterprise the responsibility for assessing whether the trading blackout applied to the Azalea Trust Transaction and the Applicants submitted that the trading blackout was breached by that transaction.

[234] The Applicants also submitted that it would be contrary to the public interest to allow Fair Enterprise to disclose material undisclosed information solely for the purpose of relying on

the insider trading exemption that applies where both parties to a trade have access to the same material information (see subsection 175(5) of the regulations to the Act). The Applicants contend that is an abuse of the exemption.

Fair Enterprise

[235] Fair Enterprise did not dispute that there was communication of material undisclosed information by Fair Enterprise to Mr. Jones. However, Fair Enterprise submitted that the communication was a disclosure made in the necessary course of business of Fair Enterprise because it was disclosed in the course of a "negotiation" between the parties to effect the sale of the Fair Enterprise MEC Shares. Fair Enterprise submitted that such a negotiation is recognized in section 3.3(2)(d) of National Instrument 51-201 – *Disclosure Standards*.

MID

[236] MID submitted that no insider trading occurred as a result of the Azalea Trust Transaction. Since disclosure was made by Fair Enterprise to the Azalea Trust on the evening of November 25, 2008, after the markets had closed and before the Fair Enterprise MEC Shares were purchased by the Azalea Trust, there was no misuse by Fair Enterprise of material undisclosed information.

Staff

[237] Staff raised a due process concern and submitted that not all of the parties against whom these allegations of insider trading were made are parties to this proceeding and they therefore had no ability to make full answer and defence to the allegations. Fair Enterprise has limited intervener status in this proceeding and Azalea Trust is not a party.

[238] Staff also submitted that there is an insufficient evidentiary foundation on which to make a finding on the allegations of insider trading. Staff submitted that there is a higher standard of proof required where a violation of subsection 76(1) of the Act is alleged (see *Re ATI Technologies Inc.* (2005), 28 O.S.C.B. 8558). Staff says that the standard of proof has not been met in this case.

[239] Finally, Staff questioned whether an allegation of insider trading can be brought by a private party on an application under section 104 or section 127 of the Act.

2. Analysis and Conclusions

[240] We agree with Staff that it would not be appropriate for us to make any finding that MID, Fair Enterprise or any other person engaged in illegal tipping or insider trading in connection with the Azalea Trust Transaction. Fair Enterprise has limited standing in this proceeding that does not extend to submitting evidence or making submissions with respect to alleged insider trading. In addition, a number of other persons who are not parties to this proceeding had some involvement in the transaction alleged to constitute insider trading and may have an interest in responding to those allegations.

[241] In any event, we do not accept the proposition that if MID or Fair Enterprise had engaged in illegal tipping or insider trading in connection with the Azalea Trust Transaction that would necessarily have prevented MID from relying on either the Downstream Exception or the Market Cap Exemption or have led us to exercise our public interest jurisdiction against MID. Insider trading and compliance with MI 61-101 are two quite separate regulatory issues. Insider trading is a serious enforcement matter that, in our view, should be addressed separately and should not generally form the basis for an application by a person other than Staff pursuant to section 127.

[242] Because the allegations of insider trading have been made, however, we believe that it is only fair to add that the communication of material undisclosed information by Fair Enterprise to Azalea Trust and Mr. Jones appears to us to have been in the necessary course of business in order to effect the Azalea Trust Transaction and thereby facilitate the November Transactions. There is nothing improper in that communication in the circumstances described to us. Fair Enterprise did not, through its knowledge of the November Transactions, exercise any unfair informational advantage over Azalea Trust in carrying out the Azalea Trust Transaction. That is because the parties to that transaction had knowledge of the same material undisclosed information when that transaction was entered into (see subsection 175(5) of the regulation to the Act which reflects this principle). There is no suggestion that Fair Enterprise, Azalea Trust or Mr. Jones, while in possession of material undisclosed information, traded in securities of MEC with any third party. Accordingly, in our view, based on the limited evidence and submissions before us, the Applicants have not made out a *prima facie* case of illegal tipping or insider trading in connection with the Azalea Trust Transaction.

[243] We do not consider the provisions of MID's corporate trading policy and the alleged breach of the trading blackout provisions, to be relevant to the determination of whether the November Transactions were exempt from Minority Approval under MI 61-101.

J. Final Considerations

[244] MEC found itself in severe financial difficulties in the Fall of 2008 and MEC ultimately filed for bankruptcy protection on March 5, 2009. The November Loan, the Loan Extension, the DIP Financing, the Stalking Horse Bid and the Amended DIP Financing can all be viewed as attempts by MID to preserve and protect the value of its existing investment in MEC represented by its secured loans to MEC. It is unlikely in such circumstances that an issuer such as MEC would have been able to quickly raise financing from anyone other than a controlling shareholder.

[245] In circumstances such as these, a regulatory requirement to obtain Minority Approval for such transactions may not be a realistic or effective mechanism to protect the interests of minority shareholders. We note in this respect that there is an exemption in MI 61-101 from the requirement to obtain Minority Approval, in certain circumstances, where an issuer is insolvent or on the verge of bankruptcy. We did not ultimately base our decision in this matter directly on the fact that MEC was either on the verge of insolvency or in bankruptcy at the relevant times, but we do consider that a relevant consideration in applying the provisions of MI 61-101 and deciding whether to exercise our public interest jurisdiction under section 127 of the Act.

[246] All of the business decisions to enter into the transactions before us were reviewed and recommended by a special committee of disinterested directors of MID and were approved by the board of directors of MID. There is no evidence before us to suggest that the directors of MID did not act appropriately throughout with a view to complying with their fiduciary duties and their responsibilities to all shareholders. Subsection 6.1(6) of the Companion Policy encourages issuers to constitute a special committee of disinterested directors to review and report on a related party transaction. That section of the Companion Policy states, in part, that "[f]ollowing this practice normally would assist in addressing our interest in maintaining capital markets that operate efficiently, fairly and with integrity". MID followed that practice in this case. The Commission has recognised in the past that a rigorous board and special committee process is a relevant consideration in deciding whether to exercise its public interest jurisdiction (see *Sterling Centrecorp, supra* at paras. 214-215).

[247] The directors of MID faced a number of difficult business decisions in connection with the transactions before us. Whether the business decisions the directors made turn out to be the right ones is not for us, as securities regulators, to speculate on. It is not our role to assess the business or financial merits of the various transactions entered into by MID with MEC or to resolve the conflicting positions of the Applicants and MID with respect to the merits of those transactions. We can only interpret and apply the provisions of our securities regulatory regime to the particular circumstances before us.

VI. CONCLUSIONS

[248] Accordingly, for the reasons discussed above, we came to the following conclusions:

1. We concluded that the Commission does not have the authority under section 104 of the Act to grant the relief requested by the Applicants.

2. We concluded that the Applicants cannot bring the Applications as a matter of right under section 127 of the Act but, in the circumstances, we permitted them to do so.

3. We concluded, on balance, that we would give legal effect to the Azalea Trust Transaction in accordance with its terms. That transaction had the legal effect of transferring the beneficial ownership of, and control or direction over, the Fair Enterprise MEC Shares to the Azalea Trust.

4. As a result, we concluded that, as a matter of the interpretation of the provisions of MI 61-101, MID was entitled, as a legal matter, to rely on the Downstream Exception in respect of the November Transactions, the March Transactions and the Amended DIP Financing.

5. Because Fair Enterprise nonetheless continued to have a direct economic interest in the Fair Enterprise MEC Shares following the Azalea Trust Transaction, we considered whether, as a matter of substance, the Market Cap Exemption was

available for the November Transactions and whether the Downstream Exception was available for the March Transactions and the Amended DIP Financing.

6. We concluded that there was a reasonable basis for concluding that the Loan Extension did not constitute a material amendment to the existing loans to which it related and was not therefore a related party transaction for purposes of MI 61-101. In any event, we concluded that, in economic substance, the Loan Extension was not a new loan in the principal amount of the existing loans and should not be viewed as such in determining the availability of the Market Cap Exemption to the November Loan. Accordingly, the Market Cap Exemption was available in respect of the November Loan and the Loan Extension (assuming the latter was a related party transaction).

7. We concluded that the November Reorganization Proposal should not be treated as a connected transaction to the November Loan or the Loan Extension in applying the Market Cap Exemption. We also concluded that there was no breach of the Minority Approval requirement by reason of the November Reorganization Proposal.

8. We concluded that any continuing direct economic interest Fair Enterprise may have had in the Fair Enterprise MEC Shares after the Azalea Trust Transaction ceased to be relevant for purposes of the Downstream Exception upon the Bankruptcy Filings made by MEC on March 5, 2009, when the equity shares of MEC became virtually worthless. Accordingly, we concluded that, as a matter of substance, MID could rely on the Downstream Exception in connection with the March Transactions and the Amended DIP Financing.

9. We concluded that it would not be appropriate for us to make any finding that MID, Fair Enterprise or any other person engaged in illegal tipping or insider trading in connection with the Azalea Trust Transaction. In any event, we concluded that the Applicants have not made out a *prima facie* case of illegal tipping or insider trading in connection with the Azalea Trust Transaction.

10. As a result, we concluded that no Minority Approval was required under MI 61-101 in connection with any of the November Transactions, the March Transactions or the Amended DIP Financing.

11. We concluded that there were no other grounds that would justify granting the relief requested by the Applicants.

[249] Accordingly, we dismissed the Applications and unconditionally released MID from its undertaking provided to Staff on May 11, 2009 relating to transactions with MEC.

Dated at Toronto this 23rd day of December, 2009.

"James E. A. Turner"	*"Paulette L. Kennedy"*
James E. A. Turner	Paulette L. Kennedy