Court File No. CV-19-615862-00CL

ONTARIO
SUPERIOR COURT OF JUSTICE
COMMERCIAL LIST

IN THE MATTER OF THE *COMPANIES' CREDITORS ARRANGEMENT ACT*, R.S.C. 1985, c. C-36, AS AMENDED

AND IN THE MATTER OF A PLAN OF COMPROMISE OR ARRANGEMENT OF JTI-MACDONALD CORP.

Applicant

COMPENDIUM OF PRICEWATERHOUSECOOPERS INC., IN ITS CAPACITY AS RECEIVER OF JTI-MACDONALD TM CORP.

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Judgment and the other multi-billion dollar claims currently being pursued against it. The requested stay under the CCAA will allow JTIM time and a platform to achieve such a solution.

III. OVERVIEW OF THE APPLICANT

A. *Corporate Structure*

10. JTIM is a private company that was continued as a corporation under the *Canada Business Corporations Act* in April 2012, and maintains its registered head office in Mississauga, Ontario (the "**Head Office**"). JTIM is owned indirectly by Japan Tobacco Inc. ("**Japan Tobacco**"), a publicly listed company in Japan.

11. A copy of an organization chart of the relevant related-party tobacco companies outside of Japan (such companies, collectively, "**JT International**") is attached as Exhibit "**B**".

12. On May 11, 1999, JTIM, then known as RJR-Macdonald Corp. was acquired by JT Nova Scotia Corporation, an indirectly wholly-owned subsidiary of Japan Tobacco.

13. Following an amalgamation and corporate reorganization in 2012, JTIM is now a direct wholly-owned subsidiary of JT Canada LLC Inc. ("**ParentCo**"), a Nova Scotia corporation and an indirect subsidiary of Japan Tobacco.

14. JTIM is the parent and sole shareholder of JTI-Macdonald TM Corp. ("**TM**"). TM owns many of the trademarks that JTIM uses in its business and is a secured creditor of JTIM. As a result of the Recapitalization Transactions (as defined herein), ParentCo is a secured creditor of TM.

15. On April 13, 2015, ParentCo demanded payment of the secured indebtedness owing from TM to ParentCo, then in the amount of approximately $1.0 billion. TM was unable to satisfy that

demand. Pursuant to the terms of the security agreements granted by TM in favour of ParentCo, on July 9, 2015, ParentCo privately appointed PricewaterhouseCoopers Inc. as the receiver and manager of TM (the "**TM Receiver**"). Subsequent to the appointment of the TM Receiver, each of the directors of TM resigned.

16. TM is not a party in any of the litigation involving JTIM. For that reason, TM is not a part of these proceedings.

B. ***The Business***

17. Most of JTIM's senior management are located at the Head Office in Mississauga, Ontario. The Head Office is responsible for all functional areas regarding the sales and distribution of JTIM's products in Canada. Managerial responsibilities for the manufacturing of JTIM's products are carried out at a manufacturing facility located at 2455 Ontario Street East, in Montreal, Quebec (the "**Plant**").

18. JTIM employs approximately 500 full-time employees in Canada. In addition, JTIM leases offices and warehouse space and employs sales representatives and associates across Canada. JTIM has been on the Aon Hewitt Best Employers list for Canadian companies and was recently certified as a Top Employer in Canada by the Top Employers Institute.

19. JTIM is the third largest tobacco company defendant in the Class Actions (as defined herein) based on volume of sales in Canada. JTIM's products consist of cigarettes, fine-cut tobacco, cigars and accessories branded under various trademarks and brand names for distribution throughout Canada and for export. JTIM imports tobacco products for distribution in Canada mainly from JT International SA ("**JTI-SA**"), a foreign sister company to ParentCo.

TAB 2

25. All employee contributions and solvency deficiency payments are current in respect of each of the Pension Plans.

26. JTIM provides other post-employment benefits ("**OPEBs**") to former salaried and hourly employees (unionized and non-unionized) and their dependants, including drug, medical, dental and life insurance benefits. As of December 31, 2018, the total present value for future OPEB contingent liabilities is estimated at $109.2 million. It is contemplated that these CCAA proceedings will not affect any payments required to be made in respect of the Pension Plans or the OPEBs.

D. ***Material Contracts***

i) Trademark Agreement

27. JTIM's market share in Canada is largely attributed to the brands of tobacco products it exclusively sells in the Canadian market. JTIM licenses or has the right to use all of the trademarks with respect to such brands from related parties. If such arrangements were terminated, JTIM's business would effectively cease in its current form.

28. Many of the trademarks that JTIM is permitted to use in its operations are owned by TM. Pursuant to the Trademark License Agreement dated October 8, 1999, as amended from time to time (collectively, the "**Trademark Agreement**"), TM granted to JTIM a non-exclusive, world-wide license to use TM's trademarks in association with the manufacturing, distribution, advertising and sale of the licensed products for the remuneration set out therein.

29. In August 2017 and January 2018, after a default by JTIM under its secured facilities with TM as a result of the issuance of the Judgment (such default is discussed in more detail below), JTIM and TM negotiated amendments to the Trademark Agreement (the "**Trademark**

Amendments") as consideration for TM's agreement to forbear from exercising its enforcement rights against JTIM. The August 2017 amendment changed the frequency of royalty payments paid by JTIM to TM under the Trademark Agreement from semi-annual payments to monthly payments. The aggregate annual amounts payable under the Trademark Agreement remained unchanged. The January 2018 amendment to the Trademark Agreement, which was a condition of the extension of the forbearance arrangement, made the supply of goods and services under the Trademark Agreement solely in the discretion of TM, acting through the TM Receiver, and required JTIM to provide a deposit to TM in an amount equal to 1.5 times the average monthly payment under the Trademark Agreement against which outstanding liabilities could be set-off. JTIM provided TM with a deposit, which as of February 28, 2019 is $1,330,000, in satisfaction of this term of the January 2018 amendment. Attached as Exhibit "**C**" are copies of the Trademark Amendments.

30. The Trademark Amendments were required by ParentCo as part of a forbearance arrangement and in response to the possibility of liquidity constraints on JTIM in the event that the Judgment was upheld. ParentCo. is the senior secured creditor of TM and has enforced its security and appointed the TM Receiver over TM. As a result of the forbearance arrangement, the TM Receiver has agreed to forbear from enforcing on the loan and security granted by JTIM to TM.

31. JTIM is required to continue paying TM pursuant to the terms of the Trademark Agreement. Termination of the right to use the trademarks licensed pursuant to the Trademark Agreement (which license is provided on a discretionary basis) would likely cause the cessation of JTIM's business. Although not every aspect of the business is affected by the TM trademarks,

TAB 3

IV. REVIEW OF TM SECURITY

28. The monies owed by the Applicant to TM are evidenced by debentures (the "**TM Term Debentures**") governed by the laws in the Province of Nova Scotia that are due November 18, 2024. The TM Term Debentures are redeemable at the option of the Applicant and convertible into special preference shares of JTIM at the option of TM. As part of an agreement by JTIM's secured creditors to forbear from exercising their enforcement rights against JTIM, the TM Term Debentures were amended by an agreement dated August 3, 2017, which amendment changed the interest payment dates (but not the amounts) from bi-annually to monthly; monthly interest payments are approximately $7.6 million and principal payments, due every May and November, are approximately $950,000.

29. The Proposed Monitor has requested that Monitor's Counsel review and opine on the security granted by JTIM to TM to secure obligations owing by JTIM to TM (the "**TM Security**"). The Proposed Monitor understands that JTIM owns real and personal (i.e: moveable and immovable) property in the Province of Quebec, and personal property in the other nine provinces.

30. Subject to the assumptions and qualifications as more particularly described in the opinions of the Monitor's Counsel, TM holds a valid security interest in the personal property of JTIM located in Nova Scotia, Ontario, Alberta and British Columbia and in the personal property and real property of JTIM located in Quebec. Copies of the Monitor's Counsel's legal opinions will be made available to the Court at the hearing of this matter and to stakeholders on appropriate arrangements regarding confidentiality, reliance and privilege.

31. Monitor's Counsel has also conducted searches of the personal property security registries against JTIM in Saskatchewan, Manitoba, New Brunswick, Prince Edward Island and Newfoundland & Labrador (the "**Additional Provinces**"). The searches disclose registrations in favour of TM, which on the face of the search have not expired. The Monitor's Counsel is not licenced to practice law in these jurisdictions, and no legal opinion has been given in respect of the validity or perfection of the TM Security in the Additional Provinces. The Proposed Monitor has been advised that JTIM's collateral in these jurisdictions is limited to non-material amounts of inventory compared to the total indebtedness owing to TM (i.e. $1.2 billion). As a result, the Monitor did not engage counsel in the Additional Provinces to provide security opinions.

32. As noted in the McMaster Affidavit, ParentCo privately appointed PricewaterhouseCoopers Inc. as receiver of TM on July 9, 2015 pursuant to the security granted by TM to ParentCo. Accordingly, references hereinafter to TM are to TM, in receivership.

V. OTHER RELATED PARTY SECURITY

33. In addition to the TM Security, JTIM has granted security to ParentCo to secure JTIM's obligations under a revolving line of credit. The Monitor understands there are currently no amounts owing under that credit facility.

34. JTIM has also granted security to secure ordinary course trade terms in favour of certain related party suppliers. Such trade terms and related security are discussed in greater detail in the McMaster Affidavit.

TAB 4

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13. Following an amalgamation and corporate reorganization in 2012, JTIM is now a direct wholly-owned subsidiary of JT Canada LLC Inc. ("**ParentCo**"), a Nova Scotia corporation and an indirect subsidiary of Japan Tobacco.

14. JTIM is the parent and sole shareholder of JTI-Macdonald TM Corp. ("**TM**"). TM owns many of the trademarks that JTIM uses in its business and is a secured creditor of JTIM. As a result of the Recapitalization Transactions (as defined herein), ParentCo is a secured creditor of TM.

15. On April 13, 2015, ParentCo demanded payment of the secured indebtedness owing from TM to ParentCo, then in the amount of approximately $1.0 billion. TM was unable to satisfy that

demand. Pursuant to the terms of the security agreements granted by TM in favour of ParentCo, on July 9, 2015, ParentCo privately appointed PricewaterhouseCoopers Inc. as the receiver and manager of TM (the "**TM Receiver**"). Subsequent to the appointment of the TM Receiver, each of the directors of TM resigned.

16. TM is not a party in any of the litigation involving JTIM. For that reason, TM is not a part of these proceedings.

B. ***The Business***

17. Most of JTIM's senior management are located at the Head Office in Mississauga, Ontario. The Head Office is responsible for all functional areas regarding the sales and distribution of JTIM's products in Canada. Managerial responsibilities for the manufacturing of JTIM's products are carried out at a manufacturing facility located at 2455 Ontario Street East, in Montreal, Quebec (the "**Plant**").

18. JTIM employs approximately 500 full-time employees in Canada. In addition, JTIM leases offices and warehouse space and employs sales representatives and associates across Canada. JTIM has been on the Aon Hewitt Best Employers list for Canadian companies and was recently certified as a Top Employer in Canada by the Top Employers Institute.

19. JTIM is the third largest tobacco company defendant in the Class Actions (as defined herein) based on volume of sales in Canada. JTIM's products consist of cigarettes, fine-cut tobacco, cigars and accessories branded under various trademarks and brand names for distribution throughout Canada and for export. JTIM imports tobacco products for distribution in Canada mainly from JT International SA ("**JTI-SA**"), a foreign sister company to ParentCo.

TAB 5

Amendments") as consideration for TM's agreement to forbear from exercising its enforcement rights against JTIM. The August 2017 amendment changed the frequency of royalty payments paid by JTIM to TM under the Trademark Agreement from semi-annual payments to monthly payments. The aggregate annual amounts payable under the Trademark Agreement remained unchanged. The January 2018 amendment to the Trademark Agreement, which was a condition of the extension of the forbearance arrangement, made the supply of goods and services under the Trademark Agreement solely in the discretion of TM, acting through the TM Receiver, and required JTIM to provide a deposit to TM in an amount equal to 1.5 times the average monthly payment under the Trademark Agreement against which outstanding liabilities could be set-off. JTIM provided TM with a deposit, which as of February 28, 2019 is $1,330,000, in satisfaction of this term of the January 2018 amendment. Attached as Exhibit "**C**" are copies of the Trademark Amendments.

30. The Trademark Amendments were required by ParentCo as part of a forbearance arrangement and in response to the possibility of liquidity constraints on JTIM in the event that the Judgment was upheld. ParentCo. is the senior secured creditor of TM and has enforced its security and appointed the TM Receiver over TM. As a result of the forbearance arrangement, the TM Receiver has agreed to forbear from enforcing on the loan and security granted by JTIM to TM.

31. JTIM is required to continue paying TM pursuant to the terms of the Trademark Agreement. Termination of the right to use the trademarks licensed pursuant to the Trademark Agreement (which license is provided on a discretionary basis) would likely cause the cessation of JTIM's business. Although not every aspect of the business is affected by the TM trademarks,

the remaining lines of business would likely not be viable on a stand-alone basis. These arrangements have allowed JTIM to continue operating in the ordinary course.

ii) Other Related Party Agreements

32. JTIM is a party to numerous services agreements and limited risk distribution agreements (the "**LRD Agreements**") with related parties, which are required for JTIM's continued operations.

33. JTIM also has related party contracts in respect of manufacturing, distribution, leaf sourcing and other miscellaneous agreements.

34. I have been advised by legal counsel that the Proposed Monitor (as defined below) in this proceeding has reviewed the material related party agreements, including the payment provisions thereunder. The service charges in place have also been audited by Canada Revenue Agency ("**CRA**") up to the 2013 taxation year and no adjustments have been required to date. CRA is currently in the process of auditing the 2014-2016 taxation years and, to date, no adjustments have been proposed.

iii) 2018 Amendments and Forbearance of Related Party Agreements

35. Against the backdrop of litigation and related credit risk, JTIM's related-party suppliers expressed concern about their potential exposure in the event that enforcement steps were taken by a judgment creditor resulting in JTIM's need to seek creditor protection. Under the intercompany arrangements then in place, such credit risk was viewed by the related parties as unacceptable. The related party suppliers advised JTIM that the intercompany supply agreements were at risk of termination. Given the unique nature of the goods and services provided, it would not be possible for JTIM to find satisfactory replacement supply arrangements. The agreements

TAB 6

issue on which the Court does not rule, does not lead to the conclusion that the court cannot take them into account when assessing the company's actual assets".

32. The recapitalization of the Applicant and the security granted in respect thereto has been in place since the acquisition of the RJR Group by Japan Tobacco in 1999. Apart from the fraudulent conveyance challenge in the AG Claim, although full particulars of the Recapitalization Transactions were disclosed and widely known as a result of the 2004 CCAA Proceedings and the Safeguard Motion, I am informed by legal counsel of the Applicant that no party has challenged the validity or enforceability of the security, there are no outstanding proceedings to which JTIM is a party and there are no Court rulings adverse to the enforceability of the debt and security of JTI-TM.

Payment of Royalties

33. As outlined in the Initial Affidavit, JTIM is the parent and sole shareholder of JTI-TM that owns many of the trademarks that JTIM uses in its business and is a secured creditor of JTIM. JTIM's market share and profits in Canada is largely attributed to the brands of tobacco products it exclusively sells in the Canadian market. If such arrangements were terminated, JTIM's business would effectively cease in its current form.

Effect of Failure to Pay Interest and Royalties

34. At the commencement of the 2004 CCAA Proceedings, JTIM and JTI-TM agreed that JTIM would stop making principal, interest and royalty payments to JTI-TM as at the date of filing. During the 2004 CCAA Proceeding, JTIM was the subject of numerous unexpected business developments, including declining sales volumes due to increased untaxed cigarettes in the market

TAB 7

66. Any damage to the ongoing operations of the business would negatively affect JTIM's stakeholders. In the majority of cases, it would be difficult to quickly replace a trade creditor that stopped supply as a result of JTIM's failure to pay its outstanding obligations. The cost of any potential disruption to JTIM's business and the costs that would be associated with any claim identification and determination process involving a multitude of trade creditors for relatively minor amounts as compared to the stated litigation claims would be uneconomical and unnecessary. JTIM's total third party ordinary course trade liabilities represent less than 0.30% of the total liabilities of JTIM as at December 31, 2018, including the QCA Judgment but excluding any other litigation claims. Preservation of going concern value, including by minimizing supply disruption, is in the best interests of all stakeholders.

67. JTIM's employees are paid periodically, usually in arrears through a payroll provider. All payments to employees are being made, and are proposed to continue to be paid, in the ordinary course.

68. JTIM proposes to pay all Pension Plan obligations, including OPEBs, in accordance with applicable requirements and in the ordinary course.

69. JTIM pays substantial amounts in taxes and duties to the various provincial and federal governments. All obligations are current in accordance with required terms and are proposed to continue to be paid in the ordinary course.

70. Pursuant to the Trademark Agreement, the next monthly royalty payment to TM is due, and is proposed to be paid, on April 1, 2019, in the ordinary course. The amount of the royalty payment varies with sales, but has historically been approximately $1 million per month.

TAB 8

during the CCAA proceedings, have contributed and will continue to contribute to the restructuring of the Applicant, and there will be no unnecessary duplication of roles among the parties.

93. I am advised by legal counsel that the Proposed Monitor believes that the proposed quantum of the Administration Charge to be reasonable and appropriate in view of JTIM's CCAA proceedings and the services provided and to be provided by the beneficiaries of the Administration Charge. I am further advised by legal counsel that the only secured creditors that will be affected by the Administration Charge are ParentCo, TM and certain other secured related party suppliers, each of which support the Administration Charge.

F. ***Directors' Charge***

94. To ensure the ongoing stability of JTIM's business during the CCAA proceedings, JTIM requires the continued participation of its directors and officers who manage the business and commercial activities of JTIM. The directors and officers of JTIM have considerable institutional knowledge and valuable experience.

95. There is a concern that the directors and officers of JTIM may discontinue their services during this restructuring unless the Initial Order grants the Directors' Charge (as defined below) to secure JTIM's indemnity obligations to the directors and officers that arise post-filing in respect of potential personal statutory liabilities.

96. JTIM maintains directors' and officers' liability insurance (the "**D&O Insurance**") for the directors and officers of JTIM. The current D&O Insurance policies provide a total of $12.908 million in coverage. In addition, under the D&O Insurance, a retention amount, akin to a deductible, is applicable for certain claims in the amount of $45,178.

97. The proposed Initial Order contemplates the establishment of a second-ranking charge on the Property in the amount of $4.1 million (the "**Directors' Charge**") to protect the directors and officers against obligations and liabilities they may incur as directors and officers of JTIM after the commencement of the CCAA proceedings, except to the extent that the obligation or liability is incurred as a result of the director's or officer's gross negligence or wilful misconduct. The Directors' Charge was calculated by reference to the monthly payroll, withholding and pension obligations of JTIM totalling approximately $4 million. The payroll obligations of JTIM are paid primarily in arrears which increases the potential director and officer liability.

98. JTIM worked with the Proposed Monitor in determining the proposed quantum of the Directors' Charge and believes that the Directors' Charge is reasonable and appropriate in the circumstances. The Directors' Charge is proposed to rank behind the Administration Charge, but ahead of the Tax Charge (as defined below) and the existing security granted by JTIM in favour of TM and ParentCo. I have been advised by counsel that the Proposed Monitor is of the view that the Directors' Charge is reasonable and appropriate in the circumstances.

99. Although the D&O Insurance is available, the directors and officers of JTIM do not know whether the insurance providers will seek to deny coverage on the basis that the D&O Insurance does not cover a particular claim or that coverage limits have been exhausted. JTIM may not have sufficient funds available to satisfy any contractual indemnities to the directors or officers should the directors or officers need to call upon those indemnities. It is proposed that the Directors' Charge will only be engaged if the D&O Insurance fails to respond to a claim.

TAB 9

and decreased earnings due to a shift to value brands until 2008 when sales began to recover. JTIM also lost over $97 million during the 2004 CCAA Proceedings as a result of its investments in asset-backed commercial papers (the "**ABCP Loss**"). Earnings from operations had deteriorated from approximately $137 million in 2001 to $47 million in 2006 which is less than half the total royalties and regular interest expense. Earnings from operations have since grown to $207 million in 2018.

35. As outlined in the Eleventh Report of the 2004 Monitor dated January 13, 2006 (the "**Eleventh Report**"), a copy of which is attached as Exhibit "**J**", JTIM and its affiliates began to experience a significant and avoidable tax burden as a result of JTIM's failure to pay principal, interest and royalties. JTI-TM and JT-LLC had no other source of revenue, other than the payments originating from JTIM. As outlined in the Eleventh Report, if JTIM simply accrued the amounts owing to JTI-TM without payment, those amounts would have to be included in the income of JTIM in the subsequent third taxation year following the year the expense was incurred unless a joint election is made to deem the amount paid and loaned back to JTIM. However, the joint election only addresses certain of the implications of non-payment as set out in the Eleventh Report. For example, interest would continue to accrue and be compounded in accordance with the loan and security agreements granted by JTIM to JTI-TM at the rate of 7.75% per annum. Interest on any unpaid royalties would accrue at the rate of 5.85%.

36. I estimate that the annual interest accrual on the debentures granted by JTIM to JTI-TM would equal approximately $2.4 million in the first year and compound thereafter such that it would escalate to $30.8 million by 2023. The estimated annual interest accrual on the royalties

would be approximately $133,000 in 2019 and build to $2.2 million by 2023.

37. If the joint election is made by JTIM and JTI-TM, and also between JTI-TM and JT-LLC and JT-LLC and JT International Holding BV ("**JTIH-BV**"), withholding taxes would become payable by JT-LLC but no funds would be available to pay the withholding taxes. The filing of the election would trigger the payment by JT-LLC of withholding taxes that would not otherwise be payable until the funds flowed from JT-LLC to JTIH-BV. I estimate that the withholding taxes that would be payable by JT-LLC would be approximately $4.3 million in 2023 and $6.5 million annually thereafter. JT-LLC would have no alternative but to attempt to secure financing to pay the withholding taxes, incurring further interest expense and, I am informed by legal counsel to the Applicant that the loan and security documents state, that such cost would ultimately be passed back to JTIM. As a result, JT-LLC and JTIH-BV may determine that it is not in their best interest to make the joint election. Similarly, JT-LLC and JTI-TM may not agree to make the election and JTI-TM may also decide not to make the tax election with JTIM.

38. Neither JTI-TM nor JT-LLC are parties to the Class Actions, the HCCR Actions or the Other Class Actions. Within the next few months, neither of these entities will have sufficient funds to pay their outstanding taxes and will be subject to compounding interest obligations if the payments that are properly due and owing are not paid. In order to pay its outstanding taxes, JTI-TM would require financing in the amount of $2.3 million in 2019 which would grow to $54.5 million in 2023 and JT-LLC would require $3.8 million in 2020 which would grow to $39.2 million in 2023.

39. The Class Action Plaintiffs argue that JTIM should revise their related party security and royalty agreements to eliminate or dramatically decrease the payments of interest and royalties

TAB 10

Applicant that this website was drawn to the attention of counsel to the plaintiffs in the Quebec Class Actions by letter dated May 16, 2005, a copy of which is attached hereto as **Exhibit "B"** (along with an unofficial English translation); and

(c) the plaintiffs in the Quebec Class Actions confirmed their knowledge of the transactions by no later than 2012, as evidenced by their unsuccessful Safeguard Motion.

20. Lastly, I note from the Report of the Proposed Monitor dated March 8, 2019, that counsel to Deloitte Restructuring Inc. (the "**Monitor**") has provided an opinion that, subject to the usual assumptions and qualifications contained in such opinion, JTI-TM holds a valid security interest in the personal property of JTIM located in Nova Scotia, Ontario, Alberta and British Columbia and in the personal and real property of JTIM located in Quebec.

21. For all of the above reasons, from a commercial perspective, I view the debt and security of JTI-TM as being binding commercial obligations. If a party wishes to attack the debt and security before a court, then JTI-TM should be named as a party and have a chance to address squarely all claims being made against it, something that I understand from counsel to the Applicants has not happened to date.

STATUS OF ROYALTY STRUCTURE

22. As with the debt and security of JTI-TM, the transactions of 1999 by which some of the trademarks used by the Applicant were transferred to JTI-TM are also not subject to any outstanding court challenge.

23. For a number of different reasons, a separate company may be created for the sole purpose of managing intangible property, including trademarks. In my experience, placing trademarks in an affiliate as an alternative to an operating entity is common practice. By way of example, I note that both ITL and RBH employ similar structures.

24. A holding company for trademarks may, for example, help value the market price for a trademark. A holding company's purpose would be to license the trademark to the operating company. If the money gained from licensing that trademark is going through the holding company, it is easier to show third-parties how much a brand is worth for purposes of valuation and sales.

25. I have read the affidavit of Robert McMaster sworn April 1, 2019 in connection with the comeback motion (the "**McMaster Comeback Affidavit**"). I agree with his observations that, by moving trademarks into a wholly-owned subsidiary, the Applicant reduced its capital tax payments by a significant amount each year, estimated by Mr. McMaster to be approximately $3.6 million annually commencing in 1999. I also understand this tax advantage was eliminated at the end of 2010 by a change in legislation.

26. I am also advised by Mr. McMaster that, pursuant to the Trademark Agreement (as defined in the Initial Affidavit), the amount of the royalties payable were set by the parties to the Trademark Agreement and were compared to a transfer pricing trademark royalty study that confirmed these rates were within an arm's length range. Also, I am advised by Mr. McMaster that Canada Revenue Agency ("**CRA**") has, in the normal course, completed audits of the royalty payments by JTIM to JTI-TM up to the 2013 taxation year (and is in the process of auditing the 2014-2016 taxation years) and that CRA has not raised any proposed adjustments to the royalty payments.

TAB 11

Court File No. CV-19-615862-00CL

ONTARIO
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(COMMERCIAL LIST)

IN THE MATTER OF THE *COMPANIES' CREDITORS ARRANGEMENT ACT*, R.S.C. 1985, C.C-36 AS AMENDED

AND IN THE MATTER OF A PLAN OF COMPROMISE OR ARRANGEMENT OF JTI-MACDONALD CORP.

NOTICE OF MOTION

The Quebec Class Action Plaintiffs[1] will make a motion to Justice McEwen presiding over the Commercial List on Monday, March 18, 2019 at 10:00 a.m., or as soon thereafter as the motion can be heard, at 330 University Avenue, Toronto, Ontario.

PROPOSED METHOD OF HEARING: The motion is to be heard orally.

THE MOTION IS FOR:

1. an order, if necessary, abridging the time for service and filing of this Notice of Motion and the Motion Record of the Quebec Class Action Plaintiffs, and dispensing with service on any person other than those served;

2. an order suspending the operation of paragraphs 8(c) and 8(d) of the Initial Order of Justice Hainey dated March 8, 2019 (the "**Initial Order**") by prohibiting payments of principal,

[1] The plaintiffs in the two class action lawsuits instituted in Quebec in 1998 on behalf of approximately 1.1 million members known as *Blais* and *Letourneau*.

interest and royalties to JTI-Macdonald TM Corp. ("**TM**") pending further order of the Court;

3. an order reserving the rights of the Quebec Class Action Plaintiffs to oppose or seek a variation of the Initial Order at the hearing of the Comeback Motion[2] scheduled for April 4, 2019; and

4. such further and other relief as this Court may deem just.

THE GROUNDS FOR THE MOTION ARE:

1. At an *ex parte* hearing before Justice Hainey on March 8, 2019 on an application by the Applicant under the CCAA, the Applicant was granted various extraordinary relief, including but not limited to, the power to make principal and interest payments to its related entity TM, under certain debentures described in the McMaster Affidavit[3], on the grounds that "there would be potential adverse tax consequences to its senior secured creditor if such payments were suspended for a significant period of time." Similarly, the Applicant was authorized to make royalty payments to TM on the grounds that the failure to make such payments, if it led to the termination of the Trade Mark Agreement as defined in the McMaster Affidavit, would likely cause the cessation of the Applicant's business.

2. The event triggering the application for the Initial Order was the unanimous judgment of a bench of five justices of the Court of Appeal of Quebec (the "**Quebec CA**") released on March 1, 2019 (the "**Appeal Judgment**") upholding, with very minor exceptions, the

[2] All capitalized terms not defined herein are used as defined in the Initial Order.
[3] Affidavit of Robert McMaster sworn March 8, 2019.

decision of the lower court rendered on May 27, 2015 (the "**Riordan Judgment**")[4] which ordered the Applicant, together with Imperial Tobacco Canada Limited ("**ITL**") and Rothmans, Benson & Hedges Inc. ("**RBH**") to pay damages to the Quebec Class Action Plaintiffs that, with interest and the additional indemnity provided by law, exceed $13.5 billion in the aggregate.

3. In the Riordan Judgment, Justice Riordan characterized "the tangled web" of JTIM's interco contracts as "a creditor proofing exercise". Those contracts include the debentures and trade mark agreements pursuant to which the Applicant proposes to continue to make payments to its related entity during the pendency of this CCAA proceeding. All of these contracts are subject to review and challenge.

4. There is no reason why the Applicant should be empowered and authorized to make any payments of principal, interest or royalties due to related parties absent a full hearing on all issues arising from the Initial Order, currently scheduled for April 4, 2019. Among other things, no evidence has been submitted by the Applicant to suggest that these payments are required to be made in order to preserve or carry on its business while operating under the protection of this Court.

5. Furthermore, when the Applicant obtained an Initial Order from Justice Farley on its previous CCAA filing on August 24, 2004[5], these same payments to TM were not permitted.

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[4] Only the Conclusions of the Riordan Judgment were filed as Exhibit X to the McMaster Affidavit, but the reasons of the trial judge were not included.

[5] The Initial Order of Justice Farley was filed as Exhibit FF to the McMaster Affidavit.

6. As appears from the Riordan Judgment, the purpose of the interco transactions was to eliminate the Applicant's average annual earnings through the payment of interest and royalties to related parties in transactions characterized by Justice Riordan, as a "sham".

7. As further appears from the Riordan Judgment, after it sought protection under the CCAA in 2004, and in respect of essentially the same obligations:

   (a) the Applicant made no interest or royalty payments in 2004 and 2005;

   (b) in 2006, the Applicant paid interest and royalties after furnishing the CCAA Monitor with letters of credit issued on the strength of a related party;

   (c) no interest or royalty payments were paid by the Applicant in 2007 and 2008;

   (d) from 2009 through 2012, the interest rate on the debentures due to TM was reduced from 7% to zero;

   (e) in 2009, TM "amended" the Trade Mark Agreement to reduce the rate of royalty payments by 50%; and

   (f) in 2012, TM once again "amended" its debentures to increase the rate of interest from zero to 7%, thereby reinstating an obligation on the part of the Applicant to pay approximately $100 million per annum starting in 2013.

8. In a 2017 Debenture Amending Agreement[6] dated August 3, 2017, the interest rate payable by the Applicant to TM on the debentures was fixed at the rate of 7.75% per annum.

[6] Filed as Exhibit N to the McMaster Affidavit.

9. The present motion is urgent as the next interest payment to TM in the amount of $7.648 million is to be paid by the Applicant during the week of March 18, 2019 according to the Applicant's 13-week cash flow statement.

10. Rules 37.14(1) and 39.01(6) of the Rules of Civil Procedure (Ontario).

11. Such further grounds as counsel may advise and this Honourable Court may permit.

THE FOLLOWING DOCUMENTARY EVIDENCE will be used at the hearing of the motion:

1. The Affidavit of Amy Casella sworn on March 15, 2019 and the documents attached thereto; and

2. Such further and other materials as counsel may advise and this Honorable Court may permit.

March 15, 2019

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Lawyers for the Quebec Class Action Plaintiffs

TAB 12

Court File Number: CV-19-615862-00CL

Superior Court of Justice
Commercial List

FILE/DIRECTION/ORDER

Re: JTI Macdonald Corp.
Plaintiff(s)

AND

Defendant(s)

Case Management ☑ Yes ☐ No by Judge: McEwen J

Counsel	Telephone No:	Facsimile No:
(see attached)		

☐ Order ☐ Direction for Registrar **(No formal order need be taken out)**
☐ Above action transferred to the Commercial List at Toronto **(No formal order need be taken out)**

☐ Adjourned to: _____
☐ Time Table approved (as follows):

The Quebec Class Action Plaintiffs ("the Plaintiffs") bring this motion seeking an order suspending the operation of paragraphs 8(c) and 8(d) of the Initial Order of Justice Hainey dated March 8, 2019 (the "Initial Order") thus prohibiting the payments of principal, interest and royalties to JTI-Macdonald TM Corp.

19 March 19
Date

Judge's Signature

☑ Additional Pages nine

Court File Number: _____

Superior Court of Justice
Commercial List

FILE/DIRECTION/ORDER

Judges Endorsment Continued

pending Further Order of the Court.

The Plaintiffs also seek an Order permitting them to oppose or seek a variation of the Initial Order at the Comeback hearing scheduled for April 4 and 5, 2019.

The Plaintiffs are supported by HMQ for Ontario.

JTI Macdonald Corp ("JTIM") opposes the relief sought. It is supported by JT Canada LLC and PWC, as well as the Monitor.

For the reasons below I am prepared to grant the relief sought pending the return of the Comeback hearing or further order made by me as the Case management judge.

The plaintiffs raise a number of arguments primarily as follows:

- JTIM did not disclose to

Judges Initials DM

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Superior Court of Justice
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FILE/DIRECTION/ORDER

Judges Endorsment Continued

Justice Hainey the negative comments made by Justice Riordan against JTIM and JTI-Macdonald TM Corp ("TM") with respect to their inter-company contracts concerning payments of principal, interest and royalties: see in particular paras: 1095-97, 1101, 1103 and 2141;

- the affidavit of Robert McMaster filed in support of the Application was vague regarding potential adverse tax consequences;
- when JTIM obtained an initial order from Justice Farley in August 2004 these same payments to TM were not requested nor made;
- subsequent to the order of Justice Farley at various times royalty payments and interest were not paid or in the case of interest the

Judges Initials TM

Court File Number: _____

Superior Court of Justice
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FILE/DIRECTION/ORDER

Judges Endorsment Continued

interest rates reduced;

• JTIM also did not disclose to Justice Hainey comments made by Justice Schrager who heard a motion to have JTIM and others post security: see in particular paras 42 and 52.

Based on the foregoing the Plaintiffs submit the Intercompany Royalty and Interest payments that are scheduled to take place before the comeback hearing ought to be suspended. They argue that JTIM had an obligation to put all of the above information before Justice Hainey and failed to do so. Based on the above the Plaintiffs claim that there is nothing to suggest that JTIM or TM will be prejudiced if the payments stop and that the payments in any event are a sham.

Judges Initials JM

Court File Number: _____

Superior Court of Justice
Commercial List

FILE/DIRECTION/ORDER

Judges Endorsment Continued

Last, the Plaintiffs submit that it is unfair to allow JTIM to continue to make the payments in the above circumstances. It is not in keeping with the purpose of the CCAA and payments ought to be suspended pending an opportunity to adjudicate the matter at the comeback hearing.

JTIM vigorously opposes the relief sought primarily submitting as follows:

- the proper materials were before Justice Hainey;
- the decision of Justice Morgan in effect "cancels out" the comments made by Justice Riordan;
- the relief sought is designed to inflict pain on a secured creditor;
- there is no request to pay principal and none will be paid absent a

Judges Initials TM

Court File Number: _____

Superior Court of Justice
Commercial List

FILE/DIRECTION/ORDER

Judges Endorsment Continued

Further Order of this court;

- if pre-filing royalties are not paid they will be deducted from a deposit held by TM
- royalties going forward must be paid pursuant to the provisions of s.11 of the CCAA;
- with respect to the issue of interest, it is a secured debt and its suspension could lead to an enormous debt later as it will compound - this would adversely affect plaintiffs in all actions;
- there is a repayment agreement in place to satisfy any judgment with a proper capitalized entity - JT International Holding B.V., with respect to interest (not royalties);
- the Monitor approved JTIM's submissions and neither JTIM or for that fact the Monitor sought to vary in any

Page 6 of 9

Judges Initials TM

Court File Number: _____

Superior Court of Justice
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FILE/DIRECTION/ORDER

Judges Endorsment Continued

way mislead the Court or provide insufficient information.

[TIM] - I submit that it is premature to grant the orders sought. I disagree.

While I am not prepared to cast aspersions with respect to the material before Justice Hainey at this time the arguments raised by the Plaintiffs persuade me that there should be a pause in the payments pending the return of the comeback hearing.

The comments of Justices Riordan[1] and Schrager raise clear concerns about the legitimacy of the inter-company contracts. Their decisions post-date the decision of Justice Morgan which was released pre-trial.

Further, given the history of

Judges Initials _____

1. Justice Riordan's factual findings were upheld on appeal.

Court File Number: _____

Superior Court of Justice
Commercial List

FILE/DIRECTION/ORDER

Judges Endorsment Continued

reduced or lack of payments after the 2004 order of Justice Farley. I am not satisfied at this juncture that the adverse consequences described by Mr McMaster will be borne out. Further, as noted, the relief concerning principal, interest and royalty payments was not sought before Justice Farley, nor granted.

In all of the above circumstances, pending the comeback hearing or further order, I agree with the Plaintiffs that it is equitable to suspend the payments referred to at Tab DD of Vol 4 of the Application Record, namely the Interim Royalty and Interest payments (as well as any principal payments although as noted GTTM is not making these payments).

Judges Initials JM

Court File Number: _____

Superior Court of Justice
Commercial List

FILE/DIRECTION/ORDER

Judges Endorsment Continued

There is no real prejudice to STIM or TM in obtaining this interim suspension pending the return of the matter at the comeback hearing.

Based on the submissions I believe that the ad relevant payments the Plaintiffs seek[sic] to suspend are noted at Tab DD above. If further clarification is required I can be spoken to as I appreciate that paras. 8(c) and 8(d) of Justice Haire's order are somewhat broader in nature than the above-noted payments.

Judges Initials _____

TAB 13

Court File Number: _____

Superior Court of Justice
Commercial List

FILE/DIRECTION/ORDER

Judges Endorsment Continued

Last, the Plaintiffs submit that it is unfair to allow JTIM to continue to make the payments in the above circumstances. It is not in keeping with the purpose of the CCAA and payments ought to be suspended pending an opportunity to adjudicate the matter at the comeback hearing.

JTIM vigorously opposes the relief sought primarily submitting as follows:

- the proper materials were before Justice Hainey;
- the decision of Justice Morgan in effect "cancels out" the comments made by Justice Riordan;
- the relief sought is skewed to reflect pain on a secured creditor;
- there is no request to pay principal and none will be paid absent a

Judges Initials TM

Court File Number: _____

Superior Court of Justice
Commercial List

FILE/DIRECTION/ORDER

Judges Endorsment Continued

Further Order of this court;

- if pre-filing royalties are not paid they will be deducted from a deposit held by TM
- royalties going forward must be paid pursuant to the provisions of s.11 of the CCAA;
- with respect to the issue of interest, it is a secured debt and its suspension could lead to an enormous debt later as it will compound - this would adversely affect plaintiffs in all actions;
- there is a repayment agreement in place to satisfy any judgment with a present capitalized entity - JT International Holding B.V., with respect to interest (not royalties);
- the Monitor approved TTIM's submissions and neither TTIM or for that fact the Monitor sought to [redacted] in any

Judges Initials TM

TAB 14

such other practices as may be agreed upon by the supplier or service provider and each of the Applicant and the Monitor, or as may be ordered by this Court.

NON-DEROGATION OF RIGHTS

24. **THIS COURT ORDERS** that, notwithstanding anything else in this Order, no Person shall be prohibited from requiring immediate payment for goods, services, use of leased or licensed property or other valuable consideration provided on or after the date of this Order, nor shall any Person be under any obligation on or after the date of this Order to advance or re-advance any monies or otherwise extend any credit to the Applicant. Nothing in this Order shall derogate from the rights conferred and obligations imposed by the CCAA.

SALES AND EXCISE TAX CHARGE

25. **THIS COURT ORDERS** that the Canadian federal, provincial and territorial authorities that are entitled to receive payments or collect monies from the Applicant in respect of Sales & Excise Taxes shall be entitled to the benefit of and are hereby granted a charge (the "**Sales and Excise Tax Charge**") on the Property, which charge shall not exceed an aggregate amount of $127 million, as security for all amounts owing by the Applicant in respect of Sales & Excise Taxes. The Sales and Excise Tax Charge shall have the priority set out in paragraphs 46 and 48 herein.

PROCEEDINGS AGAINST DIRECTORS AND OFFICERS

26. **THIS COURT ORDERS** that during the Stay Period, and except as permitted by subsection 11.03(2) of the CCAA, no Proceeding may be commenced or continued against any of the former, current or future directors or officers of the Applicant with respect to any claim against the directors or officers that arose before the date hereof and that relates to any

IN THE MATTER OF THE *COMPANIES' CREDITORS ARRANGEMENT ACT*, R.S.C. 1985, c. C-36, AS AMENDED

AND IN THE MATTER OF A PLAN OF COMPROMISE OR ARRANGEMENT OF JTI-MACDONALD CORP.

Applicant

Court File No. CV19-615862-00CL

ONTARIO
SUPERIOR COURT OF JUSTICE
(COMMERCIAL LIST)

COMPENDIUM OF PRICEWATERHOUSECOOPERS INC., IN ITS CAPACITY AS RECEIVER OF JTI-MACDONALD TM CORP.

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