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The Impact of the BCE Decision on Directors' Duties in Canada

The Facts in the Supreme Court Complaint

- \$52 billion acquisition by OTPP;
- Sale of BCE “put to auction” resulting in 3 bids each required being debt financed by Bell;
- \$30 billion in debt when deal closed;
- Debentureholders owed \$7.2 billion

Impact of transaction:

- Shareholder value increases by 40%
- Debenture value decreases by 20%
- Debenture debt goes from “investment grade” to “below investment grade”, which meant sale at a loss

Grounds bondholders opposed transaction:

- Oppression/Unfairly Prejudicial Provisions in CBCA; “reasonable expectation” their debt would not be affected
- Not “fair and reasonable” under “arrangement” provisions in CBCA (change in control without invoking take over bid requirements)

Shareholders have 4 ways they can control

The Directors:

1. Derivative action (if D's causing wrong to company), shareholder sues directors in name of the company
2. Breach of statutory duty to exercise care
3. Oppression in which shareholders sue directors directly if their personal interests as shareholders are jeopardized
4. Arrangement involving fundamental change to company; has to be "fair" and "reasonable" (judicial mechanism for controlling directors conduct)

What is “oppression & unfairly prejudicial” conduct?

- **Step 1: Did the shareholders, bondholders, creditors have a “reasonable expectation” they would be protected?**
- **Step 2: If “yes” was the Directors’ conduct either:**
 1. “Oppressive”—coercive or abusive conduct by the Directors?
 2. “unfairly prejudicial” conduct—impact creates unfair consequences

Whose interest have to be paramount when the Directors examine the problem?

- On M&A activity the directors can and should consider the interest of shareholders, creditors, consumers, government and other stakeholders, including the environment
- Rejects the “Revlon” line of cases in the USA – shareholders interests are always paramount to creditors

Whose interest have to be paramount when
the Directors examine the problem?

- Says if the interest of the stakeholders differ – Directors must consider what is in the best long term interests of the company
- When a court examines the Directors decision considerable deference should be given to the directors – “business judgment rule”

Oppression:

- Debentureholders had no “reasonable expectations” their economic interest would remain unchanged
- Debentureholders could have put clauses in their debenture to protect themselves in the event of M&A activity
- All 3 bids required some debt load – their economic interest would be affected regardless of which bid was successful
- Directors only had to “consider” the bondholders interest; that did not dictate they had to agree everything by the bondholders (listen to them – do not necessarily have to agree)

Fair and reasonable:

- No change in legal status to bond holders
- The fact that the bonds were worth less was not a change in their legal rights (terms of the debenture)
- The proposed takeover had a “valid business purpose”

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Critical Issues in Dealing with your Insurer



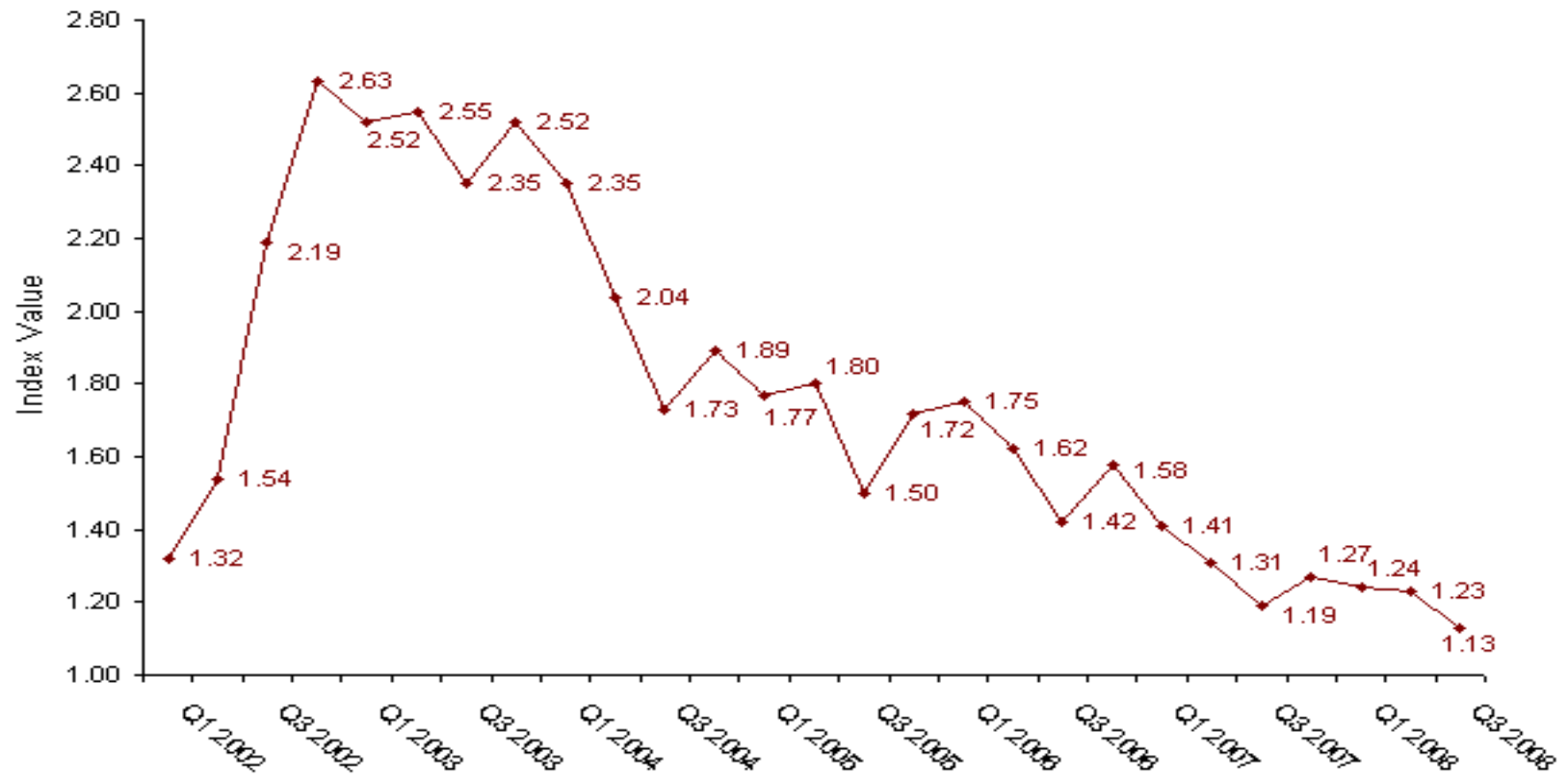
The Purchasing Decision is Changing

- Directors involvement
- Potential conflict between management and insureds (cost v. coverage)
- Third Party Reviews
- Purchasing committee with representatives of management, outside directors and risk management professionals

Recent Soft Market

- The market, in the past few years, has been highly competitive:
 - Securities litigation down
 - Large, high profile claims (ENRON, Worldcom) claims settling
 - New entrants to D&O marketplace
 - Relative financial market stability
 - Demise of Milberg Weiss
 - Underwriters have had healthy balance sheets—large ‘policy holder surpluses’
 - Broad coverage, price reductions

Pricing Trends



D&O Insurance Market—Negative Factors

- Increase in litigation:
 - Market volatility: securities filings increased
 - Downturn in economy
 - Subprime related
 - Increase in financial restatements
- Insurers own poor financials (investments, exposure to credit default swaps)
- Bill 198 litigation commenced: IMAX, Cold FX, Southwestern Resources (settled \$15.5MM, including \$2.5MM in legal)

Canadian Class Action Litigation

| Issuer | Size of claim | Basis of claim |
|-------------------|---------------|---|
| AIG | \$550 million | Disclosure re CDS exposures |
| Arctic Glacier | \$165 million | DOJ investigation |
| Celestica | \$320 million | Timely disclosure of Mexican losses |
| CV Technologies | \$110 million | Overstatement of Cold /FX revenues |
| Gammon Gold | \$80 million | Prospectus misreps—property, options |
| Gildan Activewear | \$500 million | Disclosures re manufacturing facilities |
| Imax | \$600 million | Revenue recognition practices |
| Orsu Metals | \$55 million | Accounting for derivatives |
| Southwestern | \$300 million | Settled for \$15.5 million (\$2.5 m fees) |
| SunOpta | \$110 million | Writedowns not reflected in quarterlies |
| TVI Pacific | \$16 million | Option manipulation—restatement |

Keys to Success

- Differentiate risk
- Relationships matter
- Coverage and contract performance versus pricing
- Begin renewals early
- Add or improve Side A (non-indemnifiable) coverage
- Address insurance solvency issues
- Ensure excess insurance is truly follow form and drops down
- Manuscript solutions



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