

CITATION: Labrador Iron Mines Limited (Re), 2015 ONSC 2146
COURT FILE NO.: CV-15-10926-00CL
DATE: 2015-04-02

SUPERIOR COURT OF JUSTICE - ONTARIO

RE: 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 LABRADOR IRON MINES LIMITED

BEFORE: Regional Senior Justice Morawetz

COUNSEL: *Massimo Starnino*, for the Applicants

Melaney Wagner, for Duff & Phelps Canada Restructuring Inc., Proposed Monitor

HEARD: April 2, 2015

ENDORSEMENT

[1] Labrador Iron Mines Holdings Limited ("LIMH"), Labrador Iron Mines Limited ("LIM") and Schefferville Mines Inc. ("SMI", and together with LIMH and LIM, the "Applicants") apply for an initial order (the "Initial Order") under the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36, as amended (the "CCAA").

[2] The Applicants seek an order:

- (a) appointing Duff & Phelps Canada Restructuring Inc. as Monitor of the Applicants (the "Proposed Monitor");
- (b) staying all proceedings and remedies taken or that might be taken against or in respect of the Applicants or any of their property, except as otherwise set forth in the Initial Order;
- (c) authorizing the Applicants to carry on business in a manner consistent with the preservation of their property and to make certain payments in connection with their business and the proceedings; and
- (d) creating the Administration Charge, Directors' Charge and Intercompany Charge.

[3] The Applicants intend to use the stay period to:

- (a) consult with their creditors and stakeholders with a view to securing agreement to a restructuring plan which would compromise creditor claims and restructure the Applicants key operating contracts;
- (b) pursue negotiations for the monetization of certain of the Applicants' non-core assets;
- (c) continue discussions with LIM's major outside creditors, RBRG Trading (UK) Limited ("RBRG" and formerly RBR Metalloyd Limited) and Grey Rock Services Inc. ("Grey Rock") with a view to concluding an agreement to compromise their claims;
- (d) continue discussions with Gerald Metals SA ("Gerald"), an affiliate of RBRG with a view to concluding a support agreement and a potential mine development financing with such parties generally as contemplated in a non-binding memorandum of understanding, dated November 4, 2014; and,
- (e) identify opportunities and pursue interim debtor-in-possession financing ("DIP Financing") on a basis to be determined to cover the costs of the Applicants' care and maintenance operations during these proceedings should it appear that the Applicants do not have sufficient liquidity or resources to fund these costs and these CCAA proceedings.

[4] LIMH is incorporated under the Business Corporations Act (Ontario), R.S.O. 1990 c.B.16 (the "OBCA").

[5] LIM is constituted under the laws of the Province of Ontario pursuant to articles of amalgamation dated November 30, 2007 under the OBCA. LIM was formed by LIMH to be the operating company in respect of iron ore properties located within the Province of Newfoundland and Labrador and previously held or controlled by LIMH.

[6] SMI is incorporated under the *Canada Business Corporations Act*, R.S.C. 1985 c.C.44 (the "CBCA"). SMI was formed by LIMH to be the operating company in respect of iron ore properties located within the Province of Québec and previously held or controlled by LIMH.

[7] The Applicants' registered and executive offices are located at 220 Bay Street, Suite 700, Toronto, Ontario M5J 2W4.

[8] LIMH is a publicly held company whose share capital consists of an unlimited number of common shares without par value of which 126,323,123 common shares are issued and outstanding. In addition, 13,800,000 warrants and 1,030,000 options to purchase totals of 13,800,000 and 1,030,000 additional common shares, respectively, are issued and outstanding.

[9] The Applicants currently have 15 full time employees and independent contractors, including 8 at the Applicants' corporate offices and 7 at other locations. At the peak of its mining operations in August 2013 the Applicants had 250 employees and independent contractors,

including 75 aboriginal people from local communities, employed at its mine and exploration sites, offices and other locations.

[10] The Applicants' operations are carried out in the central part of the Labrador Trough iron ore region (the "Schefferville Projects").

[11] The Schefferville Projects are centered in the Menihek area in the Province of Newfoundland and Labrador around the town of Schefferville, Québec. Schefferville is a community of less than 1,000 people, the majority of whom are Innu of the Matimekush Lac John First Nation. There are no roads connecting Schefferville to southern Labrador or to Québec. The Schefferville Projects are connected by a direct railway to the Port of Sept-Îles on the Atlantic Ocean.

[12] The Applicants' mine has operated seasonally from approximately the beginning of April to the end of November in 2011, 2012 and 2013. The mine operations have been shut down each winter from approximately the beginning of December to the end of March.

[13] The Applicants' operations have been funded largely by LIMH which raised capital through public share offerings in December, 2007, March, 2010, April, 2011, March, 2012, November, 2012, and February, 2013.

[14] Through these public offerings, LIMH raised total gross proceeds (before underwriting commissions and offering expenses) of \$342,620,728. To date, a total of approximately \$270 million has been loaned by LIMH to LIM on an unsecured basis making LIMH LIM's largest creditor (unsecured).

[15] The Applicants contend that, with the exception of limited security interests granted over certain iron ore stockpiles of the Applicants, over the Applicants' fleet of rail cars and in respect of certain capital leases, all of the Applicants' obligations are unsecured.

[16] During 2012, there was a major decline in world iron ore prices in the middle of the Applicants' April to November seasonal operations. In particular, the price dropped from US\$147.65/tonne in April 2012 to US\$86.70/tonne in September 2012.

[17] This price decline reduced the Applicants' cash flow significantly and required the Applicants to severely curtail operations in 2012. The Applicants experienced operating losses in 2012 of approximately \$58.0 million.

[18] In 2014, the iron ore price declined nearly 50% to approximately US \$66.00/tonne by late December, 2014. The iron ore price has continued at the US\$60.00 to US\$65.00 range during the 2015 year to date. By the end of March, 2015 the price was approximately US\$52.00/tonne.

[19] The current price of iron ore, operational problems in 2012 and 2013, together with significant capital investment for plant upgrades and expansion have put considerable strain on the Applicants' cash resources.

[20] The Applicants' financial position and the results of their operations are consolidated in LIMH's financial statements which are publicly disclosed in accordance with applicable securities laws. The financial statements are contained in the record.

[21] After recognition of non-cash impairment charges totalling \$198,168,728 in the period ending December 31, 2014, the Applicants had current and non-current assets of \$3,479,483 and \$12,390,450, respectively, and current and non-current liabilities of \$65,728,733 and \$3,826,211, respectively.

[22] Presently, as a result of the sale of their joint venture interest relating to its Howse Project, the Applicants have an unrestricted, consolidated cash balance of \$5.5 million. The Applicants' banking arrangements together with those of the Applicants' other affiliated companies are operated on a centralized offset banking basis such that all but \$1,000 of the available cash balances of each of LIM and SMI are transferred to and held in an operating account in the name of LIMH. Intercompany obligations arising as a result of this system are tracked and recorded in the non-consolidated financial records of each of the Applicants. It is intended that these banking arrangements will continue. Current operations of the Applicants have been funded by advances from LIMH which are recorded as intercompany obligations. Intercompany advances by LIMH to LIM and SMI are currently approximately \$270.2 million and \$21.3 million, respectively.

[23] In addition to the intercompany debt owing to LIMH, the Applicants' most significant creditors are currently:

- (a) RBRG (deferred revenue) (approximately US\$20.6 million); and
- (b) Grey Rock and its affiliates (accounts payable) (approximately \$15.6 million).

The majority of amounts due to creditors have been outstanding since the end of the Applicants' operating season in 2013.

[24] The Applicants contend that the amounts owed to these, and all other creditors, are unsecured except that (i) RBRG holds a security interest in certain iron ore stockpiles owned by the Applicants; (ii) the Port Authority holds a security interest in the Applicants' fleet of rail cars; and (iii) LIM's mine camp and certain office equipment are subject to capital leases.

[25] Counsel to the Applicants also disclosed that Grey Rock has recently taken steps to file a lien relating to its claim. The effect of the lien is uncertain.

[26] In 2013, the Applicants generated negative gross margin of \$49,188,203, with rail and port costs accounting for more than 50% of the unit cost of the Applicants' production. The Applicants state that they did not resume mining operations in 2014 due in part to these costs, particularly in the context of deteriorating iron ore market conditions.

[27] The Applicants have developed an operating plan (the "Operating Plan") which addresses both its operating plans for the next mining season (the "Current Mining Plan") and longer-term plans. The Operating Plan is based upon balancing product quality and quantity and minimizing operating costs.

[28] At this time, the Applicants submit they do not have the necessary financial resources to re-commence mining operations in 2015. The Applicants will not be able to implement the Operating Plan unless they can secure additional financing for capital costs and working capital, and reduce their mining, rail and port infrastructure and other operating costs. If additional financing cannot be secured on a timely basis, the Applicants state they will have to defer re-commencement of their mining operations.

[29] The Applicants contend that they require restructuring of their current accounts payable and new investment or financing facilities to provide necessary working capital to ensure operations can effectively continue and to enable the development of the Houston project in accordance with the current operating plan.

[30] Over the past 18 months, the Applicants state that (working with Canaccord Genuity Corp. ("Canaccord"), an independent Canadian investment bank, and, more recently, in consultation with Duff & Phelps, they have made significant efforts to identify and negotiate additional financing for capital costs and working capital.

[31] Over the same period, the Applicants have met regularly with RBRG to keep it apprised of developments and explore possible new financing arrangements. Through these efforts and after extensive negotiations over several months, the Applicants entered into a non-binding memorandum of understanding ("MOU") with RBRG and its related company, Gerald Metals SA, dated November 4, 2014 which contemplated RBRG's agreement to support the Applicants' proposed restructuring and to compromise the debts owed to it on terms to be set out in a support agreement. As of the date hereof, these support and financing agreements have not been concluded.

[32] The Applicants have also been negotiating with their suppliers and service providers since the end of its 2013 operating season in an effort to restructure their operating costs.

[33] The Applicants submit that CCAA proceedings are necessary to permit the Applicants an opportunity to secure financing and complete negotiations with their suppliers and service providers to restructure the Applicants' accounts payable, as well as to permit the Applicants a further opportunity to canvas the market for potential sources of financing or other means of effecting a restructuring of their business and operations.

[34] The issues on this Application are:

- (a) Does this Court have jurisdiction to grant the CCAA relief requested?
- (b) Should a Stay of Proceedings be granted as requested?
- (c) Should the Monitor be approved as requested? and
- (d) Should the requested charges be granted?

[35] The CCAA applies to a "debtor company" with total claims against it of more than \$5 million. The Applicants submit they are "debtor companies" entitled to relief under the CCAA.

[36] I am satisfied that the Applicants meet this definition, as follows:

- (a) LIMH is a holding company incorporated under the OBCA;
- (b) LIM is an company constituted under the laws of Ontario; and
- (c) SMI is a company incorporated under the CBCA.

[37] The Applicants are insolvent because their consolidated current liabilities exceed their consolidated current assets by approximately \$62.2 million, and, but for the commencement of these proceedings, they are unable to meet their obligations as they become due.

[38] The Applicants have liabilities in excess of \$5 million dollars.

[39] In addition, the Applicants have met the other threshold requirements required by section 10 of the CCAA. Further, since the head office and chief place of business of the Applicants is located in Toronto, Ontario, this Court has jurisdiction to hear this application pursuant to section 9(1) of the CCAA.

[40] Given the Applicants' current financial condition, I am of the view that CCAA proceedings at this time are in the best interests of the Applicants and their stakeholders and are both appropriate and necessary. The stay of proceedings requested is appropriate in the circumstances and is consistent with the purpose of the CCAA. Duff & Phelps is appointed Monitor.

[41] The Applicants seek approval of three charges: an Administration Charge, a Directors' Charge, and an Intercompany Charge. (collectively, the "Charges").

[42] This Court has the jurisdiction to grant the requested charges. The Applicants are not requesting that the Charges rank in priority to any encumbrances in favour of persons who are not served with notice of this application.

[43] The proposed Initial Order contemplates the indemnification of directors and officers (and deemed and *de facto* directors and officers) of the Applicants (defined, collectively, in the proposed Initial Order as the "Directors"), the creation of a Directors' Charge in relation thereto, and a related stay of proceedings of claims against Directors.

[44] Section 11.51 of the CCAA provides statutory authority to grant a directors' and officers' charge on a super-priority basis.

[45] The Applicants state that LIM has obtained directors' and officers' insurance coverage ("D&O Insurance"), but there may be significant limitations to coverage that may leave directors and officers exposed to personal liability. The proposed Directors' Charge is to protect Directors against exposure beyond that which is covered by insurance.

[46] Further, the Applicants submit that it is important to have the Directors' Charge to keep the Directors in place during the restructuring and to protect them against liabilities that they

could incur during the restructuring that are ultimately found to not be covered by the D&O Insurance.

[47] The Applicants request that this court exercise its discretion to approve the Directors' Charge proposed in the Initial Order, to rank second in priority after the Administration Charge, in the maximum amount of \$300,000. The Applicants submit this amount is appropriate to protect the Directors from possible exposure and that the Directors' Charge is appropriate to avoid destabilization that would result without the experienced Directors during the restructuring proceeding.

[48] I accept these submissions and conclude that it is reasonable and appropriate to anyone the Directors' Charge.

[49] The Applicants also request an Administration Charge to provide security for the fees and disbursements of the Monitor, counsel to the Monitor, and the Applicants' counsel, through a charge over all present and after-acquired assets of the Applicants.

[50] The Administration Charge includes a charge not to exceed an aggregate of \$500,000 as security for the fees and disbursements of those entitled to the benefit of the Administration Charge, and would have a first priority over all other charges.

[51] Section 11.52 of the CCAA provides the authority to grant an administration charge.

[52] In *Re Camwest Publishing*, Pepall J. provided a non-exhaustive list of factors to be considered in approving an administration charge, including:

- (a) the size and complexity of the businesses being restructured;
- (b) the proposed role of the beneficiaries of the charge;
- (c) whether there is an unwarranted duplication of roles;
- (d) whether the quantum of the proposed charge appears to be fair and reasonable;
- (e) the position of the secured creditors likely to be affected by the charge; and
- (f) the position of the Monitor.

[53] The proposed Monitor has concluded that the quantum of the proposed charge is reasonable. Having reviewed the record, I am satisfied that the Administration Charge should be granted in the amount requested.

[54] In order to ensure that creditors of the individual Applicants are not prejudiced by these proceedings, the Applicants are also asking that an Intercompany Charge be imposed to secure amounts that may be advanced by one Applicant to another in the ordinary course of operations.

[55] The authority to grant the Intercompany Charge is found, in s. 11.2 of the CCAA, with the factors to be considered in sub-section 11.2(4). I am satisfied that the Intercompany Charge

is justified by the fact that the business and affairs will be amply managed during these proceedings. I have also taken into account that the Intercompany Charge is not intended to prioritize or secure the interests of a particular stakeholder or creditor

[56] For the foregoing reasons, CCAA protection is granted. The Initial Order has been signed in the form submitted, as amended.

[57] The Stay Period is in effect until May 1, 2015. The Applicants are to schedule the comeback hearing through the Commercial List Office.



Regional Senior Justice G.B. Morawetz

Date: April 2, 2015