In the Tel Aviv-Jaffa District Court | **LF 44348-04-16**
Application no. 20

Before the Honorable Chief Justice, Judge Eitan Orenstein

In re: **The Companies Law, 5759-1999**

The Law

The Companies Regulations (Application for a Settlement or Arrangement), 5762-2002

The Settlement or Arrangement Regulations

and in re: Urbancorp Inc. Canadian company no. 2471774

the Company

and in re: **Adv. Guy Gissin - the provisional official of Urbancorp, Inc.**

acting by his attorneys Advs. Yael Hershkovitz *et al*, of Gissin & Co., Advocates, of 38B Ha'Barzel Street, Tel Aviv 69710, tel. 03-7467777, fax. 03-7467700

The Official

and in re:
1. **Ronen Nakar**
2. **Daphna Aviram Nitzan**
3. **Eyal Geva**
4. **Doron Rosenblum**

acting by their attorneys, Advs. Maya Sabari *et al*, of Matry, Meiri & Co., Law Offices, of 7 Menachem Begin Street, Ramat Gan 52681, tel. 03-6109000, fax. 03-6109009

The Applicants

and in re: **The Official Receiver**

of 2 Ha'Shlosha Street, Tel Aviv, tel. 03-6899695, fax. 02-6462502

The Official Receiver

The Official's Response to the Application
for the Grant of Leave to File a Third Party Notice

In accordance with the Court's decision of September 8, 2016, the Official hereby respectfully files with the Honourable Court his response (objection) to the Applicants' application of September 7, 2016, for the grant of leave to file a third party notice against the Company (hereinafter - the **"application"**), in the framework of the class action filed by Mr. Fechthold Tuvia, *inter alia* against the Company, and against the Applicants, which appears in the register of actions as CA 1746-04-16 (hereinafter - the **"class action"**).

The Honourable Court is moved to dismiss the application, for the reasons detailed below in this response.

And these are the grounds of the response:

A. Introduction

1. On June 6, 2016 the Honourable Court ordered a stay of proceedings against the Company and in particular the proceedings pending against the Company in the class action (hereinafter - the **"stay of proceedings order"**).

2. The Applicants' application for the grant of leave to file a third party notice against the Company has two bases: (a) by virtue of the letters of indemnity which they claim to hold (paragraph 17.1 of the application); (b) since according to the Applicants, if and insofar as the class plaintiff's plea is accepted, it is the Company's conduct that resulted in the directors' failure and deception (paragraph 17.2 of the application).

3. In the alternative, the Applicants are asking the Court to order that monies be left in the Official's fund in an amount sufficient for the purpose of clarifying the Company's liability to the Applicants (we would mention that the relief claimed in the class action is in a sum of approx. NIS 42 million), until a final decision is handed down in the class action.

4. As will be explained below, the Official's position is that there is no place to allow the directors' application to deviate from the stay of proceedings order, nor is there room to order that monies be left in the Official's fund for the purpose of clarifying the Company's liability. Let it be noted that the practical significance of this relief application is an attempt to impose an attachment on the liquidation fund. Just like that.

5. So long as the Company has not repaid all its debts to its creditors and covered all the costs of the insolvency proceedings, there is no basis or need to leave any amount in the fund for the Applicants.

B. <u>The "letter of indemnity" does not give the Applicants a relevant creditor's right against the Company or at the most a deferred creditor's right</u>

6. As aforesaid, the Applicants are contending that they have a right to indemnity from the Company, by virtue of a "letter of indemnity" that was supposedly granted to them by the Company in the scope of their employment as directors of the Company. In practice, the Applicants' plea is that the said letter of indemnity vests them with the status of "conditional creditors" of the Company, in the event that it is determined that they are liable and found in respect of the pleas raised against them in the class action.

   It goes without saying that the directors simultaneously filed a debt claim with the Official, *inter alia* by virtue of precisely those pleas (hereinafter - the **"debt claim"**). The debt claim has not yet been heard or decided by the Official.

   A copy of the debt claim that was filed with the Official by the directors - Applicants 1-3, is annexed hereto as **<u>appendix "1"</u>**.

7. A preliminary examination of the Applicants' pleas, in this application and in the debt claim, raises considerable doubt that they can be treated as creditors of the Company on the basis of their plea regarding the Company's undertaking to indemnify them for claims filed against them in connection with their liability as officers of the Company.[1]

8. **Firstly,** the Official was unable to track down duly signed letters of indemnity that were given to the Applicants. The document purporting to be a letter of indemnity that was presented by the Applicants in the scope of the debt claim filed by them appears to be signed solely by Mr. Saskin (other than in accordance with the signatory rights in the Company); there is no date next to his signature; and the Applicants have not signed confirmation of its receipt in the designated place.

   A copy of confirmation of the signatory rights in the Company that were in force at the relevant time is annexed hereto as **<u>appendix "2"</u>**.

9. **Secondly,** even if we ignore the aforesaid and assume (merely for the purpose of debate) that the directors will succeed in proving that despite the faults and inconsistency with regard to the signatory rights, the letter of indemnity presented by them is somehow valid (and this is not the case), still, in accordance with the letter of indemnity, it is provided that:

   > "The total indemnification amount paid by the Company to all of the Officers of the Company in the aggregate under the letters of indemnity

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[1] Unlike their claim, which was included in the debt claim, for salary and remuneration of expenses that was not paid to them.

> ... **Will not exceed an amount equal to 25% of the Effective Equity of the Company** ... In this regard, **"The Effective Equity of the Company"** shall mean an amount of the Equity of the Company attributed to the Shareholders of the Company under the most recent consolidate financial statements audited or reviewed, of the Company as applicable correct **as of the date of the indemnification payment**".

Since the overall amount of all the payments that the Company might be held liable to make by virtue of the letters of indemnity to all the Company's officers cannot exceed a sum equal to one quarter of the equity attributed to the Company's shareholders just before actual payment of the indemnity;

and since, as everyone knows, the Company (like the companies in its group) is currently insolvent and involved in proceedings in Israel and in Canada;

it is clear that there is not and cannot be any **"equity attributed to the shareholders"**, except after the payment in full of all the Company's debts to its creditors, including the costs of the insolvency proceedings.

10. **Hence - the letters of indemnity, even if and insofar as they are somehow valid towards the Company, do not give any of the Applicants a right to be considered ordinary creditors or even conditional creditors of the Company.**

    If at all - in accordance with the priority amongst creditors of an insolvent company, the Applicants can be considered deferred creditors, whose rights are inferior to those of all other creditors, and limited to a sum of one quarter of the Company's capital, which reflects the rights that any of the Company's shareholders might have (only theoretically) after payment of all the obligations to creditors and all the costs of the insolvency proceedings.

C. The cause for the Applicants' alleged right to indemnity is theoretical and it is not possible to assess when it will become relevant

11. Moreover, in the application, the Applicants referred to matters pending in the class action that has not yet been heard on its merits or decided by the Court hearing it, while over the six months that have elapsed since the filing of the class action, not even one hearing has yet taken place on the merits of the matters mentioned in the application and the Respondents' reply to these matters has not even been filed.[2]

[2] On July 26, 2016 the Applicants even applied to postpone filing their response to the amended application for approval of the class action to November 30, 2016.

12. Let it be noted that even if and insofar as the decisions in the class action would indeed lead to the conclusion that the Applicants are liable in the framework of the class action, the Applicants would not have a right to indemnity and participation from the Company, as pleaded by them in the application.

13. It appears that the relief requested in the framework of this application is aimed at "being a game changer" and entitling the Applicants to remedies and relief to which they are not entitled pursuant to any law and/or agreement. Allowing any of the alternative relief sought by the Applicants (for the grant of a chance to file a third party notice against the liquidation fund or for the grant of an order to freeze amounts in the liquidation fund to secure compensation in respect of the alleged theoretical indemnity). [The sentence is incomplete]

14. The relief sought might frustrate the Official's ability to formulate a creditors' arrangement and might prejudice the principle of equality amongst creditors in insolvency proceedings, while giving unjustified preference to someone who is not even a creditor (not today and not in the future), or at the most is a conditional and deferred creditor vis-à-vis the other creditors.

15. In any event it is clear that allowing the alternative relief sought by the Applicants, the meaning of which is leaving a significant amount in the Official's fund, for a lengthy period, is also unjustified; not only does the inferiority of the indemnity undertaking compared with the other creditors' rights make the theoretical creditors' rights of the Applicants deferred, but leaving amounts in the Official's fund will oppress the rights of the Company's other creditors, and might even result in the failure of any creditors' arrangement that the Official acts to formulate and propose.

    See in such regard the words of Her Honor Judge Alshech in BF (Tel Aviv) 1361/02, Agicoa - International Association for the Collective Management of Audioviaual [translator - should be "Audiovisual"] Works v. Mr. Zvi Yochman, CPA:

    > **"Having considered the circumstances of the case, in view of the proper law in a stay of proceedings, I have found that the Applicant's application, to leave a reserve in the fund in the huge amount of its claim, and in this way effectively delay execution of the entire creditors' arrangement, should not be allowed."**

    It appears that the aforesaid is sufficient for the application's dismissal. Merely for the sake of caution, and without derogating from the aforesaid, below are additional reasons justifying the application's dismissal on its merits.

D. Filing a third party notice against the Company will prejudice the equality amongst creditors and the purposes of formulating a creditors' arrangement

16. As aforesaid, the Honourable Court some time back ordered a stay of proceedings order against the Company that will remain valid until another decision of the Court, for the purpose of formulating a creditors' arrangement in the Company.

17. The application for a stay of proceedings that was filed by the Official on June 19, 2016 (hereinafter - the **"stay of proceedings application"**) expressly referred to the existence of the class action and a stay of the proceedings against the Company in the framework thereof, such that most of the Applicants' pleas with regard to the conduct of proceedings against the Company in the class action were already available to the Court at the time of its decision to grant a stay of proceedings order against the Company.

18. As clarified in the stay of proceedings application, the object of the stay of proceedings was to give the Official a chance to formulate a creditors' arrangement for the benefit of all the Company's creditors, while suspending all claims against the Company in Israel, simultaneously with the automatic stay of proceedings that was applied in Canada with recognition of these proceedings as foreign main proceedings.

19. The case law has taken a stand on the decisive importance of a stay of proceedings in order to enable formulation of a suitable creditors' arrangement, and for the purpose of maximizing the value of the Company's assets, equitably, for all its creditors, and obtaining a picture as clear and accurate as possible of the Company's inventory of assets, rights of action available to it and against it, as quickly as possible.[3]

20. The lifting of the stay of proceedings order solely with regard to the Applicants will prejudice the equitable nature of the proceedings with the Company's ordinary creditors, both Canadian and Israeli, who filed their claims in the scope of the debt claim proceedings that were approved in both Canada and Israel. This result is even harder for the Company's Canadian creditors, whose access to the Israeli courts is more complex, and who filed their debt claim with the Official in the scope of the debt claim proceedings that were approved and published in Canada.

    And so it is held in such regard by Her Honor, Judge Alshech, in in re Warner:

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[3] See the words of Her Honour Judge Alshech in BF (Tel Aviv District) 1361/02, Mr. Zvi Yochman, CPA in his capacity as Trustee and Special Manager of [incomplete] v. Warner Bros. International Television Distribution (published in Nevo, February 10, 2003) (hereinafter - "in re Warner").

> **"It should be recalled that a stay of proceedings is for a limited and tight timetable, and the significance of continuing lengthy civil proceedings outside the scope of the court of insolvency might considerably prejudice formulation of the necessary picture of the Company's position and assets, and consequently its chances of recovery. Hence, it is of the utmost importance to actually reach a swift decision on proceedings aimed at determining the Company's inventory of assets, as distinct from those that are merely aimed at determining the amount of the creditors' debt claims against it. It should be recalled that while the process of checking the debt claims might continue also after the arrangement's approval, in that it generally has no relevance except to the way in which the consideration obtained from the investor will be distributed amongst the creditors, the continuation of pending proceedings with regard to the Company's actual inventory of assets that might be transferred to the investor, might pose an obstacle to the very possibility of reaching a proper arrangement from the outset." [The emphases are in the source]**

And subsequently:

> **"It is a well-known principle in insolvency law, and in particular in a stay of proceedings, that the law strives to make it possible for the trustee to focus his interest on the company's recovery, and accordingly tends to take a negative view of being forced to spread out its powers and resources over a range of various civil proceedings."**

21. It emerges that the *de facto* lifting of the stay of proceedings order solely with respect to the Applicants will prejudice both the ordinary creditors of the Company, Israeli and Canadian as one, and the Official's ability to formulate a debt arrangement for the benefit of all the Company's creditors, and for this reason should not be allowed.

E. The directors' rights should be clarified in the framework of the debt claim filed by them and no in external proceedings

22. Moreover, as detailed above, a debt claim of most of the Applicants for the full amount of the class action was filed some time back with the Official. The debt claim is being considered on its merits by the Official, and will be decided before a distribution is made to the Company's ordinary creditors.

23. A creditor of an insolvent company may apply to the Court for leave to conduct a legal claim against it instead of filing a debt claim, but may not adopt both measures jointly, i.e. the filing of a debt claim together with the conduct of legal proceedings on the same matter. Thus, for example, it was held by His Honour

Judge Ailabouni in LF (Nazareth) 21285-02-13, Amir Shehada Construction & Development Ltd v. The Official Receiver, as follows:[4]

> **"Hence, a creditor conducting a claim against a company which is becoming insolvent will have to consider if it wishes to continue conducting the legal claim against the company (in which case it must file an orderly application with the court of insolvency and obtain its approval) or follow another track and file a debt claim with the official appointed in the suspension period. If it chooses the first track and obtains the Court's approval, it may conduct the legal proceedings against the Company to the end, but may not demand a decision on a debt claim that it filed on the same cause and may not vote at creditors' meetings of the company. If it chooses the second track - the legal proceedings against the Company will be stayed and a debt claim will be filed that will be checked and decided as customary in insolvency proceedings, with the said creditor reserving the right to vote at creditors' meetings, as it deems fit." [The emphasis is ours]**

24. It emerges that from the moment of filing the debt claim, the Applicants must conduct the proceedings in connection therewith in the framework of these proceedings, like any other creditor of the Company, instead of conducting it in the framework of separate proceedings.

F. Conclusion

25. The relief sought by the Applicants (the grant of approval to file a third party notice against the Company or leave amounts in the Official's fund for the purpose of covering the theoretical obligation to them) is inconsistent with the principles of the law and case law, and will prejudice the efficacy, equality and uniformity of the proceedings that are being conducted with regard to the Company, to the point of effectively frustrating the Official's ability to formulate a creditors' arrangement in the Company.

26. Hence, the Court is moved to dismiss the relief sought in the framework of the application and to leave the stay of proceedings order in place.

(Signed)	(Signed)
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Yael Hershkovitz, Adv.	Sandra Schneider, Adv.

Attorneys for the Official for Urbancorp, Inc.

[4] See also the words of His Honour Judge Benjamin Arnon in LF (Center) 25351-01, The Tel Aviv New Central Station (in Suspension of Proceedings) v. The Official Receiver.

Today, September29, 2016, Tel Aviv