



COURT FILE NUMBER 1801-10960

COURT COURT OF QUEEN'S BENCH OF ALBERTA

JUDICIAL CENTRE CALGARY

PLAINTIFF PRICEWATERHOUSECOOPERS INC., LIT, in its capacity as the TRUSTEE
IN BANKRUPTCY OF SEQUOIA RESOURCES CORP.
and not in its personal capacity

DEFENDANTS PERPETUAL ENERGY INC., PERPETUAL OPERATING TRUST, PERPETUAL
OPERATING CORP., and SUSAN RIDDELL ROSE

DOCUMENT **AFFIDAVIT OF W. MARK SCHWEITZER**
FOR APPLICATION FOR SECURITY FOR COSTS

PARTIES FILING THIS DOCUMENT PERPETUAL ENERGY INC., PERPETUAL OPERATING TRUST, and
PERPETUAL OPERATING CORP.

ADDRESS FOR SERVICE AND CONTACT INFORMATION OF PARTIES FILING THIS DOCUMENT Burnet, Duckworth & Palmer LLP
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File No.: 59140-43

AFFIDAVIT OF W. MARK SCHWEITZER

Sworn on May 5, 2020.

I, **W. Mark Schweitzer**, of the City of Calgary, of the Province of Alberta, SWEAR AND SAY THAT:

Introduction

1. I am the Vice-President, Finance, and Chief Financial Officer of the Defendants Perpetual Energy Inc. (**Perpetual**) and Perpetual Operating Corp. (**POC**). I commenced employment in this position with Perpetual in May 2017.

2. As such I have personal information regarding the matters set out in this Affidavit, except where I state my information is from another source, in which case I believe that information to be true.

3. I am a Chartered Professional Accountant, a graduate of Queen's University with a Bachelor of Commerce degree, and a member of the Chartered Professional Accountants of Ontario.

4. Unless otherwise defined, the abbreviations and defined terms in the Perpetual Defendants' Statement of Defence are used in this Affidavit.

5. I was not involved in the Transaction in 2016, but I have been actively involved in Perpetual's review of files, communications with Mr. Paul Darby following Sequoia's bankruptcy and this Action since Mr. Darby's first communication with Perpetual by letter dated May 28, 2018.

6. I have read the Statement of Claim, Statements of Defence, Applications and Affidavits filed on behalf of the Plaintiff and on behalf of the Defendants as well as Justice Nixon's Reasons for Judgment in this Action. I also swore an affidavit in this Action on October 4, 2018.

7. I have also communicated with the Perpetual Defendants' legal counsel in this Action, Burnet, Duckworth & Palmer LLP (**BD&P**) about this Action.

8. I have separately sworn an affidavit in this Action in support of the Perpetual Defendants' second application for summary dismissal. If the Court grants that application and dismisses the *BIA* claim (being the only remaining claim), then the Perpetual Defendants will no longer request security for their costs from this Court.

Reasons for Security for Costs

9. The Perpetual Defendants are concerned that if they are successful in this Action that the Plaintiff PricewaterhouseCoopers Inc., in its capacity as the trustee in bankruptcy of Sequoia Resources Corp. (the **Trustee**), will be unable to pay any costs award out of the estate and the Perpetual Defendants will be unable to enforce an order for costs against the Trustee because the estate has no exigible assets. PricewaterhouseCoopers Inc. in its own capacity (**PwC**) has also refused to agree to be personally liable for costs. As a result, the Trustee is litigating this Action without any consequence of paying a costs award.

10. The Perpetual Defendants are applying now for security for costs because they have become increasingly concerned regarding the Trustee's inability to pay any costs award and the mounting legal fees they are incurring to defend this Action:

- (a) it remains early in the Action, as it has not yet progressed past the pleadings stage, no records have been exchanged and no questioning has occurred;
- (b) the Action will become increasingly expensive if and when it proceeds to discovery, subject to appeals of Justice Nixon's Reasons for Judgment in this Action and the Perpetual Defendants' second summary dismissal application;
- (c) the Perpetual Defendants now have information that the Trustee will likely be unable to pay any costs award; and
- (d) PwC has refused to be personally liable for any costs award.

Request for Security for Costs in the Trustee's Appeal

11. On August 15, 2019, Justice Nixon struck or summarily dismissed all of the claims against the Defendants except for the claim under the *BIA* against the Perpetual Defendants.

12. On August 23, 2019, the Trustee filed an appeal of Justice Nixon's decision striking or dismissing all claims against Ms. Rose and the Perpetual Defendants, except for the *BIA* claim against the Perpetual Defendants. On August 26, 2019, the Perpetual Defendants filed an appeal of Justice Nixon's decision not to grant summary dismissal of the *BIA* claim.

13. On September 6, 2019, counsel for the Defendant Ms. Rose, on behalf of all Defendants, sent a letter to counsel for the Trustee requesting it either confirm that PwC will be personally liable, or that the Trustee will provide security for the Defendants' costs related to the Trustee's appeal. A copy of the letter is attached as **Exhibit A**.

14. PwC and the Trustee refused in a letter dated September 11, 2019, a copy of which is attached as **Exhibit B**.

15. On September 12, 2019, counsel for the Trustee wrote to the Case Management Officer of the Court of Appeal requesting that the Trustee's appeal be heard on an expedited basis in part because of the limited resources available to the Trustee:

At the date of the bankruptcy, all of [Sequoia's] wells had been shut in. Many of the wells were shut in hastily, in a manner which reflected the urgency and the limited resources of Sequoia at the time, in the weeks leading up to the date of bankruptcy. Over the past 17 months since the appointment of the Trustee, all the Sequoia wells and facilities across Alberta have remained unattended. Sequoia has no employees and no operating revenue.

[...] the Trustee is not in a position to implement the phased environmental risk mitigation programs an active, operating company typically would, or to properly monitor the vast majority of the sites.

A copy of the letter from the Trustee's counsel is attached as **Exhibit C**. The Defendants' counsel responded to this letter but those letters are not relevant to this application.

16. On September 23 and 24, 2019, Ms. Rose and the Perpetual Defendants separately applied to the Court of Appeal for security for costs of the Trustee's appeal. Ms. Rose swore an affidavit on September 23, 2019 in support of the applications, a copy of the body of which is attached as **Exhibit D** (the exhibits are already part of the record in this Action, are attached elsewhere as full exhibits to my affidavit, or are not relevant to this application as they relate to the notice of appeal and scheduling before the Court of Appeal).

17. On October 18, 2019, Mr. Darby swore an affidavit opposing the applications for security for costs of the Trustee's appeal, a copy of which is attached as **Exhibit E**. His affidavit provides no specifics as to the ability of the Trustee to pay any costs award, other than a bald assertion that "the funds currently in the estate easily exceed Ms. Rose's estimates of the

anticipated legal fees to be incurred by herself and the Perpetual Defendants." He also stated that "the Defendants have made no request to inspect the books, records and documents relating to the administration of the Estate... pursuant to the provisions of the Act."

18. On November 1, 2019, Ms. Rose and I, along with counsel from BD&P, attended the Trustee's office to inspect the books and records of the Trustee under s. 26(3) of the *BIA*. A copy of the email chain setting up the inspection in preparation for questioning of Mr. Darby on his affidavit is attached as **Exhibit F**. The questioning of Mr. Darby had been rescheduled to take place after the inspection, as stated in emails to counsel for the Trustee: "it will be far more efficient if the inspection happens first, and may eliminate or reduce the need for undertakings" and "it would be a poor use of Mr Darby's and counsel's time to do the questioning before the inspection."

19. Yet on October 30, 2019, the day before the inspection, the Trustee imposed conditions on Perpetual's right to inspect the books and records of the administration of the estate under s. 26(3) of the *BIA*, including Perpetual would only be permitted to review the books and records if "the records and information obtained will not be published generally". A copy of the letter from the Trustee's counsel is attached as **Exhibit G**. Section 26(3) of the *BIA* states: "The trustee shall permit the books, records and documents referred to in subsection (2) to be inspected and copies of them made by the Superintendent, the bankrupt or any creditor or their representative at any reasonable time." It contains no such conditions or limitations.

20. On November 6, 2019, Mr. Darby was cross-examined on his affidavit opposing the applications for security for costs of the Trustee's appeal. A copy of the transcript filed with the Court of Appeal is attached as **Exhibit H** (notations, highlighting and underlining were made by counsel for the Defendants and were part of the copy filed at the Court of Appeal). At Mr. Darby's cross-examination, counsel for the Trustee objected "to the reference or the marking of exhibits in this particular cross-examination with respect to any of the documents that were made available pursuant to your request for inspection of the records" (Transcript of examination of Paul Darby dated November 6, 2019, pg 12; 26 to pg 13; 3).

Court of Appeal Granted Security for Costs of the Trustee's Appeal

21. On January 29, 2020, Justice Veldhuis granted both Ms. Rose and the Perpetual Defendants each 37.5% (\$150,000 of \$400,000) of their separate anticipated solicitor-client costs for the Trustee's appeal (less 20% owing to the prohibition against security for costs in oppression claims, which does not apply here as the *BIA* claim is the only remaining claim). Copies of Justice Veldhuis' Reasons for Decision and her Order are attached as **Exhibits I** and **J**.

22. The Trustee has posted those costs with the clerk of the Court of Appeal.

Request for Security for Costs in this Action

23. On February 7, 2020, BD&P wrote to counsel for the Trustee requesting that either PwC confirm that it is personally liable for all costs awards against the Plaintiff in this Action, or that the Trustee consent to an order that it post security for the costs that the Perpetual Defendants will incur by responding to the outstanding claim under the *BIA*, and requesting a response by February 14, 2020. Attached as **Exhibit K** is a copy of this letter. BD&P informed me that they have received no response.

The Trustee Will Likely be Unable to Pay any Costs Award Granted to the Defendants

24. I believe that the Trustee must be exhausting all cash available from the Sequoia estate, in part to finance this litigation:

(a) attached as **Exhibit L** is a copy of the Trustee's Preliminary Report dated April 11, 2018, setting out that as of that date the estate:

(i) had \$1,776,109 in cash; and

(ii) claims of creditors totalling \$244,501,718, including \$7,054,630 in secured claims;

(b) a review of the Trustee's website regarding the Sequoia bankruptcy shows that the Trustee has not subsequently reported on the financial affairs of the estate of Sequoia, including on the costs and disbursements of the Trustee;

(c) at Mr. Darby's cross-examination on his affidavit opposing the application for security for costs of the Trustee's appeal, he testified that he was "guessing" the estate had approximately \$2.3 million in cash but that the secured creditors' claims are "in the millions", which are "greater than the cash on hand" (Transcript of examination of Paul Darby dated November 6, 2019, pg 19; 14-18; pg 23; 5-17; pg 57; 1-8; pg 106; 2-7). While Mr. Darby implied in his testimony that the Trustee had disallowed secured claims such that the amount of the admitted secured claims was less than the cash on hand (Transcript of examination of Paul Darby dated November 6, 2019, pg 59; 10-18; pg 61; 2 to pg 66; 23; pg 106; 9-20), his response to an undertaking to provide the Trustee's position on the secured creditors' claims in the estate of Sequoia was that "The Trustee has paid out the claim of one secured creditor, but has not considered and formulated a final position on the remaining secured creditors' claims in the estate" (undertaking no. 7, see **Exhibit M**); and

(d) Mr. Darby testified at his cross-examination on his affidavit opposing the application for security for costs of the Trustee's appeal that the Trustee was not selling the assets from the Asset Transaction and the assets Sequoia purchased from AlphaBow Energy Ltd. (Transcript of examination of Paul Darby dated November 6, 2019, pg 39; 22-26; pg 41; 2-6, 17-21; pg 42; 9-12; pg 74, 15-27).

25. On February 21, 2020, Ms. Rose and I, along with counsel from BD&P, again attended the Trustee's office to inspect the books and records of the Trustee under s. 26(3) of the *BIA*. Copies of the emails and letters setting up the inspection are attached as **Exhibit N**. As part of that correspondence, the Trustee placed conditions on Perpetual's right to inspect the books and records of the administration of the estate under s. 26(3) of the *BIA*, including that Perpetual refrain from publishing the books and records, including by filing any part of the books and records with the Court. Perpetual agreed to the condition under protest "reserving Perpetual's ability to have the Court enforce Perpetual's statutory right" under s. 26(3) of the *BIA*. While I will not disclose any books or records so I do not breach the Trustee's condition, my conclusion above that the estate of Sequoia will likely be unable to pay the Perpetual Defendants' costs at the conclusion of this litigation is not changed by having reviewed the books and records.

26. Since the inspection, the Trustee has likely incurred and will likely continue to incur considerable expenses that will further erode any cash available to the Trustee. As a result of the condition imposed regarding the use of records reviewed on the inspections referred to above, I am unable to attach any records addressing such expenses, but it is self-evident that:

(a) litigation costs are expensive, and while the Trustee has not disclosed during Perpetual's inspections of the books and records the Trustee's fees and those of its counsel, the current dispute is complex, as is its litigation against AlphaBow Energy Ltd. in Court of Queen's Bench of Alberta Action No. 1901-09591, and the Trustee has for almost two years been paying three sets of professional fees from the Sequoia estate: its own fees (PwC), those of its counsel with respect to the bankruptcy in general (Torys LLP) and those of its counsel in this dispute (de Waal Law) and appears intent on continuing to do so pending the resolution of this Action;

(b) the Trustee paid \$240,000 to the clerk of the Court of Appeal as security for costs of the Trustee's appeal; and

(c) Ms. Rose, as the successful party in the Action, has a claim for her costs of this Action.

27. According to the above information, and based on my understanding of the Supreme Court of Canada's decision in *Redwater*—namely that the obligation of an insolvent company to perform asset retirement obligations is binding on a trustee in bankruptcy and must be performed prior to payment of either secured or unsecured creditors—it appears that the unsecured creditors of Sequoia stand to recover little or nothing. This is consistent with Mr. Darby's understanding in cross-examination on his affidavit opposing the application for security for costs of the Trustee's appeal:

Q Certainly you'd agree with me that the way things stand now, given the decision in Red Water, which gives the AER a priority status, if that's the right term, and given the quantum of a secured claims that you know about and given the expenses the trustee is being -- is authorized to be being paid, there is no prospect that the unsecured creditors are going to get a penny, is there?

A Unless we were successful on all our actions.

(Transcript of examination of Paul Darby dated November 6, 2019, pg 110; 21 to pg 111; 2)

Q So you've got assets of marginal value that you don't intend to sell or try to sell. You've got expensive lawsuits. You've got secured claims that may or may not be allowed, and you've got a very remote prospect of unsecured creditors being paid anything unless you win on all your lawsuits; right?

A Yes.

(Transcript of examination of Paul Darby dated November 6, 2019, pg 111; 22 to pg 112; 1)

28. On October 22, 2018, the Defendants cross-examined Mr. Darby on his affidavit in support of the Trustee's application for judgment. Mr. Darby was questioned about how the Trustee was proposing to fund this litigation. Mr. Darby testified that the inspectors of Sequoia had been presented with estimated cash flow statements that projected certain legal costs be paid by the Sequoia estate, though he could not recall the projected monthly amounts. Mr. Darby testified:

Q You can't recall ballpark what you estimated for the cost of the lawsuit?

A No, because we did it on a monthly cash-flow basis, not on a single line item.

Q Can you recall the monthly amounts?

A No.

Q Will you agree, based on what you've seen today, this lawsuit is going to cost in the millions of dollars, the trustee?

A I can't estimate the -- I don't know.

(Transcript of examination of Paul Darby dated October 22, 2018 p. 87: 1-10; at his subsequent cross-examination dated November 6, 2019 on his affidavit opposing the Perpetual Defendants' application for security for costs of the Appeal, Mr. Darby refused to produce those "monthly cash-flow" statements as undertakings. A copy of his undertaking responses are attached as **Exhibit M**).

29. Mr. Darby continued that the Trustee had made no arrangements with any other party to finance or fund the litigation:

MR. LEITL: So your answer is you don't know what [this litigation] it's going to cost?

A No. I don't know. I expect it to be expensive.

Q And has the trustee made arrangements with any third parties for any backup financing?

A No.

(Transcript of examination of Paul Darby dated October 22, 2018 p. 87: 19-24)

30. At his cross-examination on November 6, 2019, Mr. Darby reiterated that the Trustee's lawsuit will continue to be expensive and be funded out of the estate:

Q And despite the fact that the secured claims may or may not be allowed by the trustee, you've confirmed that the trustee is incurring legal and professional fees; right?

A Yes.

Q Including the lawsuit that we sit here today to deal with, which you expect to continue to be expensive?

A Yes.

(Transcript of examination of Paul Darby dated November 6, 2019, pg 107; 20-27)

Q ...Last time we examined you, you stated under oath that there is no third party funding for the estate or for the lawsuits; right?

A Yes.

Q And that continues to be the case?

A Yes.

Q No third party backstopping guarantees of any kind?

A No.

Q So the lawsuits that you have decided are in the best interests of the estate are to be funded entirely by the estate?

A They have been funded by the estate entirely so far.

(Transcript of examination of Paul Darby dated November 6, 2019, pg 112; 8-19)

Just and Fair to Order Security for Costs

31. Based on the foregoing, I believe that:

- (a) the Trustee will be unable to pay any costs award out of the estate; and
- (b) the Perpetual Defendants will be unable to enforce an order for costs against the Trustee because the estate has no exigible assets.

32. In all the circumstances, I believe that it would be just and fair that the Trustee be required to post reasonable security, such as a commercially reasonable letter of credit, for the solicitor-client costs of the Perpetual Defendants.

Estimated Costs

33. It is difficult to estimate all of the costs that the Perpetual Defendants will incur in defence of this Action if the Perpetual Defendants' appeal and second summary dismissal application are unsuccessful and this matter proceeds towards trial.

34. To date, BD&P has invoiced the Perpetual Defendants \$824,570 and advises that it has work-in-progress of approximately \$24,774, for a total of approximately \$849,344, in respect of the Trustee's claim, excluding matters related to the appeals.

35. I am advised by BD&P, and I believe, that should the Perpetual Defendants' appeal regarding the *BIA* claim be unsuccessful, they will incur further solicitor-client costs in this Action up to trial estimated to be at least \$2,000,000 and likely substantially more. In this regard, BD&P and I have considered the following:

- (a) this figure represents just over double the solicitor-client costs the Perpetual Defendants have incurred in the proceedings thus far;
- (b) the factual and legal complexity of the *BIA* claim;
- (c) questioning and record production has not even started, and a trial has not been scheduled and is unlikely to occur for several years;

(d) as the Perpetual Defendants' application to strike or dismiss the *BIA* claim on the arm's length issue was unsuccessful, the trial on that issue alone will include *viva voce* evidence of the evidence that was before Justice Nixon, along with additional evidence that Justice Nixon referred to in his Reasons for Judgment when he stated that "the determination of the 'arm's length issue' will turn on the credibility of witnesses who were directly involved in the negotiation of the Asset Transaction, including their alleged control of PEOC" (at paragraph 98). As a result, any questioning and trial will involve the witnesses who participated in the negotiation of the Asset Transaction plus evidence regarding the value of the consideration PEOC gave and received under the Asset Transaction (as defined in the Trustee's Statement of Claim), and whether PEOC was insolvent at the time of the Asset Transaction or rendered insolvent by the Asset Transaction;

(e) the Trustee seeks damages of approximately \$220 million against the Perpetual Defendants; and

(f) the Trustee's Statement of Claim requested costs on a full indemnity basis.

36. Attached as **Exhibit O** is a draft bill of costs prepared by BD&P to assist in estimating the fees and disbursements that will be incurred in the defence of this Action. I understand that BD&P has prepared the Bill of Costs on a multiple of five times Column 5 of Schedule C costs (that apply effective May 1, 2020) on the basis of:

(a) the complexity of the matter, as set out above;

(b) Justice Veldhuis considered \$150,000 as an appropriate amount for security for costs of the Trustee's appeal, having calculated five times Column 5 costs of the appeal as being \$98,000—that is, Justice Veldhuis considered it appropriate that security for costs be equivalent to approximately 7.5 times Column 5 under Schedule C that applied pre-May 1, 2020; and

(c) no multiplier for inflation and no additional lump sum amounts.

Expert Fees

37. I am informed by BD&P and believe that, if this matter proceeds to trial, it will be necessary for the Perpetual Defendants to retain at least three experts to provide opinion evidence.

38. As set out in my Affidavit sworn on October 3, 2018, one expert will be required to provide expert opinion evidence as to the fair market value of the consideration received and given by PEOC under the Asset Transaction and the Transaction as a whole.

39. A second expert will be required to provide expert opinion evidence as to the abandonment and reclamation obligations associated with the Goodyear Assets.

40. A third expert will be required to provide expert opinion evidence regarding PEOC's solvency before and after the Asset Transaction, as well as the causes of Sequoia's ultimate insolvency and bankruptcy.

41. I am advised by BD&P that, based on their experience, the experts' fees will likely amount to or exceed approximately \$100,000 each to prepare a report and attend trial, for a total of at least \$300,000.

Affidavit in Support

42. I make this Affidavit in support of the Perpetual Defendants' application for security for costs.

SWORN BEFORE ME at the City of Calgary, in)
the Province of Alberta this 5th day of May,)
2020.)


_____)
A Commissioner for Oaths in and for the)
Province of Alberta)


_____)
W. Mark Schweitzer)

PAUL GEORGE CHISWELL
Barrister and Solicitor