

[3] On June 12, 2020, Cineworld sent a notice to Cineplex terminating the agreement. The same day, Cineworld withdrew its application for ICA Approval.

[4] Cineplex brings this claim against Cineworld for damages. It says that once Cineworld withdrew its application for ICA Approval, Cineplex was unable to seek specific performance. Cineplex alleges that Cineworld had no basis for terminating the agreement and that its notice was a repudiation of the agreement. Cineplex seeks damages for breach of contract in the range of \$1 billion.

[5] Cineworld submits that it was entitled to terminate the agreement because Cineplex breached its covenants in the agreement – in particular, the covenant to operate in the ordinary course of business between the date of the agreement and closing. Cineworld brings a counterclaim to recover its transaction costs from Cineplex.

[6] The central issues in this trial concern the interpretation of the contract between the parties and issues of risk allocation as between them.

[7] For the reasons that follow, I find for Cineplex. Cineworld had no basis for terminating the agreement. I award damages to Cineplex as set out below. Cineworld's counterclaim is dismissed.

FACTUAL BACKGROUND

[8] The key events in this case occurred over a period of six months from December 2019 to June 2020. Unless otherwise noted, all date references are to 2020. I will first provide a general overview of the undisputed background facts. I will then discuss the evidence in greater detail when I analyze the various allegations of the parties.

[9] Cineplex is an Ontario corporation and is publicly traded on the Toronto Stock Exchange. It operates in the film entertainment and content, amusement and leisure and media sectors. It is Canada's largest film exhibitor and has a circuit of theatres and location-based entertainment venues across Canada.¹

[10] Cineworld is a public company incorporated under the laws of England and Wales. Its shares are listed on the London Stock Exchange. It was founded in 1995, although its roots go back more than 92 years to a theatre opened by the Greidinger family in Haifa, Israel.

[11] In 2018, Cineworld acquired the U.S. cinema chain Regal Entertainment Group (“**Regal**”). Following that acquisition, Cineworld became the second largest cinema chain in the world by

¹ Cineplex also operates businesses in digital commerce (CineplexStore.com), food service, alternative programming (Cineplex Events), cinema media (Cineplex Media), digital place-based media (Cineplex Digital Media) and amusement solutions (Player One Amusement Group). It operates a location-based entertainment business through destinations for ‘Eats & Entertainment’ (The Rec Room), and entertainment complexes specifically designed for teens and families (Playdium). Cineplex is a joint venture partner in SCENE, an entertainment loyalty program.

number of screens. It operates cinemas in ten countries.² Its primary brands are Regal in the U.S., Cineworld and Picturehouse in the U.K. and Ireland, Cinema City throughout Europe, and Yes Planet in Israel.

[12] 1232743 B.C. Ltd. is a wholly-owned subsidiary of Cineworld. It was incorporated solely for the purpose of completing the acquisition of Cineplex. In these Reasons, the term Cineworld includes 1232743 B.C. Ltd., as applicable.

Background to the Arrangement Agreement

[13] The parties entered into an arrangement agreement (the “**Arrangement Agreement**”) following extensive negotiations between Cineplex and Cineworld and their advisors. Initial discussions between Cineplex and Cineworld started in mid-2019 when Ellis Jacob, the Chief Executive Officer (CEO) of Cineplex, met with Mr. Moshe (Mooky) Greidinger, the CEO of Cineworld.

[14] Mr. Jacob testified that he had seen the consolidation trend happening globally. Cineplex faced a decision of whether to expand outside of Canada or be acquired by a strategic buyer. That led it to conclude a transaction with Cineworld. Mr. Mooky Greidinger testified that with the addition of Cineplex’s screens to the recently acquired Regal chain, Cineworld would have become the largest exhibitor in North America and the world. Cineworld was also confident that it could derive significant cost and revenue synergies from the transaction.

The Arrangement Agreement is Signed

[15] On December 15, 2019, the parties entered into the Arrangement Agreement in which Cineworld agreed to acquire all of the shares of Cineplex for \$34 per share (the “**Transaction**”). This was approximately \$10 per share more than the trading price of Cineplex’s shares at the time, a premium of 42%.

[16] The Arrangement Agreement provided for the Transaction to occur through a plan of arrangement pursuant to s. 182 of the Ontario *Business Corporations Act*, R.S.O. 1990, c. B.16, as amended (the “**OBCA**”).

[17] In addition to acquiring the shares, Cineworld agreed to pay Cineplex’s transaction expenses, amounts owed to holders of incentive securities, and unpaid dividends. Since the Transaction would be a change in control under Cineplex’s Scotiabank-led bank facility (“**Company Credit Agreement**”), Cineworld would have to repay Cineplex’s bank debt after closing.

² The ten countries are the U.S., the U.K., Ireland, Poland, Romania, Israel, Hungary, the Czech Republic, Bulgaria and Slovakia.

[18] The Transaction was subject to various conditions and covenants, including approval by shareholders of Cineplex and Cineworld, and approvals under the *Competition Act*, R.S.C., 1985, c. C-34, the *Investment Canada Act* and the U.S. *Hart-Scott-Rodino Antitrust Improvements Act of 1976*, 15 USC §18a (1976) (“**HSR**”). The outside date for closing was June 30.

[19] Cineworld obtained debt financing of approximately USD \$2.28 billion for the Transaction from Bank of America, HSBC, and Goldman Sachs. The financing consisted of a secured term loan of USD \$1,932.2 million and a short-term, unsecured bridge loan of USD \$343.1 million (the “**Bridge Loan**”). The Bridge Loan was intended to fund the acquisition of Cineplex’s non-cinema businesses, which Cineworld planned to sell soon after closing.

Parties Start to Implement the Arrangement Agreement

[20] The parties moved quickly after signing the Arrangement Agreement.

[21] Cineworld initiated the ICA Approval process. The Transaction was subject to dual track review by two agencies – the Cultural Sector Investment Review Division and the Investment Review Division, a division of Innovation, Science and Economic Development (the “**Agencies**”). Cineworld retained an external government relations consultant, Hill & Knowlton, to assist with the ICA Approval process. To obtain ICA Approval, Cineworld had to satisfy the relevant Ministers that the Transaction would likely be of “net benefit” to Canada.

[22] On December 31, 2019, Cineworld filed its application for review under the ICA.

[23] On January 3, Cineplex issued a notice of application in this court with respect to the plan of arrangement. Cineplex obtained an interim order on January 9.

[24] On January 29, Cineworld submitted its initial draft undertakings to the Agencies. As part of the ICA Approval process, the investor (Cineworld) had to file undertakings with the Agencies setting out how it intended to operate the Cineplex business for a period of three to five years after closing. The undertakings covered matters such as the level of employment to be maintained, capital expenditures to be maintained, Canadian participation in senior management, and the presence and functions of a Canadian head office, all benchmarked to Cineplex’s past performance.

[25] By the end of January, Cineworld had taken steps that satisfied the conditions for *Competition Act* and HSR approval.

[26] Cineworld started the integration planning process for the combined two businesses. It retained a consultant, SA Global, to assist with an enterprise resource planning solution for the combined group. Cineworld and Regal representatives attended regular and numerous meetings on integration throughout the months of January and February.

[27] On February 11, both Cineplex and Cineworld received overwhelming shareholder approval for the Transaction. Cineplex obtained final court approval under the OBCA on February 18.

[28] Cineworld submitted revised draft undertakings to the Agencies on February 24.

[29] All that remained to be completed for closing was for Cineworld to obtain ICA Approval. It was originally anticipated by the parties and the Agencies that this could be completed by the end of March.

The Pandemic is Declared and Theatres are Closed

[30] On March 11, the World Health Organization declared the COVID-19 outbreak to be a global pandemic. On March 13, the Government of Quebec declared a provincial state of emergency. On March 15, it ordered various businesses and public spaces, including theatres, to close until March 30. Cineplex closed its Quebec theatres that day.

[31] On March 16, Cineplex closed its theatres across Canada.

[32] On March 17, the Government of Ontario declared a provincial state of emergency and ordered various businesses, including theatres, to close until March 31. The Government of Alberta ordered closures the same day.

[33] On March 17, Cineworld closed its theatres globally as a result of the pandemic.

The ICA Approval Process Continues

[34] On March 17, Cineworld sent revised draft undertakings to Cineplex for review. They were now conditional on the Chief Public Health Officer of Canada declaring COVID-19 to be at an end or fully contained in Canada, and Hollywood studios fully resuming their movie release schedule for North America. Counsel for the parties exchanged emails and had calls with the Agencies. On April 7, Cineworld filed its third set of undertakings. Those included an additional condition that the business return to “Normal Theatre Business Conditions”.³

[35] Further exchanges ensued between counsel. Cineplex’s counsel pressed Cineworld’s counsel to move the process forward and submit signed undertakings. Further discussions were held with the Agencies. The Agencies were concerned that there was not a fixed start date for the conditional undertakings and proposed a longer amortization period for the undertakings. Cineworld continued to require that the undertakings be conditional.

³ According to Mr. Mooky Greidinger, the “Normal Theatre Business Conditions” proviso made the implementation of Cineworld’s big money undertakings contingent on Cineplex’s future revenues being no less than 85% of revenues earned in FY2019, and on Cineplex’s future profit margin being in line with its profit margin for FY2019.

[36] On June 2, representatives of the Agencies and counsel for Cineworld and Cineplex discussed the following schedule – Cineworld would submit revised undertakings by June 5, the Agencies would respond by June 10, and Cineworld would submit its executed undertakings by June 12.

[37] Cineworld submitted its fourth set of draft undertakings on June 5. The Agencies provided detailed written feedback on June 10 and offered some final suggestions for Cineworld to consider as it prepared its final signed undertakings for submission on June 12.

Notice of Default and Termination Notice

[38] On June 5, Cineworld sent a notice to Cineplex alleging numerous breaches of the Arrangement Agreement. The notice said that Cineworld did not believe that the breaches could be cured by Cineplex and reserved Cineworld's rights to terminate the agreement before the end of the 10-day cure period in the Arrangement Agreement. Cineplex responded and denied any breach of the agreement.

[39] On June 12, Cineworld delivered a notice to Cineplex terminating the Arrangement Agreement. The same day, Cineworld withdrew its application for ICA Approval.

OVERVIEW OF RELEVANT CLAUSES IN THE ARRANGEMENT AGREEMENT

[40] The parties to the Arrangement Agreement were Cineplex, Cineworld and 1232743 B.C. Ltd.

[41] Section 4 of the Arrangement Agreement contains various covenants (“**Interim Covenants**”) restricting the manner in which Cineplex could operate the business during the period between the date of the agreement and closing (the “**Interim Period**”). The first is the covenant in s. 4.1(1) (the “**Operating Covenant**”) that reads (my emphasis added):

The Company covenants and agrees that, during the period from the date of this Agreement until the earlier of the Effective Time and the time that this Agreement is terminated in accordance with its terms, except: (i) with the prior written consent of the Purchaser, such consent not to be unreasonably withheld, delayed or conditioned; (ii) as required or contemplated by this Agreement or as expressly set out in the Company Disclosure Letter; or (iii) as required by Law, the Company shall, and shall cause each of its Subsidiaries to, conduct its business in the Ordinary Course and in accordance with Laws, and the Company shall, in good faith, use commercially reasonable efforts to maintain and preserve its and its Subsidiaries business organization, assets, properties, employees, goodwill and business relationships with customers, suppliers, partners and other Persons with which the Company or any of its Subsidiaries has material business relations.

[42] “Ordinary Course” is defined in s. 1.1 to mean actions “taken in the ordinary course of the normal day-to-day operations of the business of the Company...consistent with past practice.”

[43] Section 4.1(2) lists, without limiting the generality of the Operating Covenant, 30 specific actions that Cineplex agreed not to take in the Interim Period. At issue in this litigation are the following covenants:

- not to sell or transfer, directly or indirectly, any of Cineplex's assets with a value greater than \$1 million individually (or \$3 million in the aggregate) (s. 4.1(2)(g));
- not to create any new source of indebtedness in excess of \$5 million (s. 4.1(2)(o));
- not to permit or cause any amendments to its Significant Contracts (including Material Leases) whether in the Ordinary Course or otherwise (s. 4.1(2)(x));
- not to permit or cause any amendments to Cineplex's leases outside the Ordinary Course (s. 4.1(2)(y));
- not to make any changes to the Annual Budget, including moving of line items within the Annual Budget (s. 4.1(2)(cc));
- not to agree, resolve, or commit to do any of the acts that are not permitted under section 4.1(2) (s. 4.1(2)(dd)).

[44] The Arrangement Agreement contains various conditions of closing. Section 6.2 sets out the conditions of closing for the exclusive benefit of Cineworld. They include the following:

- all representations and warranties of Cineplex are true and correct as of the Effective Time unless they do not, individually or in the aggregate, have a Company Material Adverse Effect. Cineplex has to confirm same by a certificate signed by two senior officers (s. 6.2(1));
- Cineplex has fulfilled and complied in all material respects with its covenants in the Arrangement Agreement. Cineplex has to confirm same by a certificate signed by two senior officers (s. 6.2(2));
- no Company Material Adverse Effect has occurred since the date of the Arrangement Agreement (s. 6.2(4));
- Cineplex's bank debt under the Company Credit Agreement does not exceed \$725 million (the "\$725M Debt Condition") (s. 6.2(5)).

[45] The term Company Material Adverse Effect is defined in s. 1.1 as:

... any change, event, occurrence, effect or circumstance that, individually or in the aggregate, with other such changes, events, occurrences, effects or circumstances, is or would reasonably be expected to have a material and adverse effect on the business, affairs, operations, assets, liabilities, financial condition or results of operations of the Company and its Subsidiaries taken as a whole, except any such change, event, occurrence, effect or circumstance arising out of, relating to, resulting from or attributable to: ...

- (e) any earthquake, flood or other natural disaster or outbreaks of illness or other acts of God;

[46] There is no dispute that the COVID-19 pandemic is an “outbreak of illness” and is excluded from the definition of a Company Material Adverse Effect. There are 12 exclusions from the definition of Company Material Adverse Effect including changes to the motion picture industry, changes in general economic or market conditions, changes in laws, and labour strikes.⁴ As is generally the case in material adverse effect clauses and as discussed further below, the exclusions relate to “systemic” factors, the risk of which was allocated to Cineworld, the buyer.

[47] The parties agreed in s. 4.8(1) that they would use their reasonable best efforts to obtain Regulatory Approvals to enable the closing to occur as soon as reasonably practicable and in any event before the outside date. Cineworld agreed that it would not take any action that would reasonably be expected to delay obtaining the approvals or closing the Transaction.⁵ While the parties agreed to work together in seeking Regulatory Approvals and Cineworld had to consider the views of Cineplex, Cineworld had the final authority over the strategy, tactics and decisions in obtaining those approvals.

ISSUES TO BE DECIDED IN THIS CASE

[48] The following issues are to be decided in this case:

- (a) Was Cineworld entitled to terminate the Arrangement Agreement due to Cineplex’s alleged breach of the covenants in the agreement?
- (b) If not, what are Cineplex’s damages?

DID CINEWORLD WANT OUT OF THE TRANSACTION?

[49] Before turning to the issue of whether Cineworld was entitled to terminate the Arrangement Agreement, I will consider Cineplex’s submission that Cineworld wanted out of the Transaction by as early as March or April. There was a great deal of evidence on this issue at trial. It provides context to the circumstances in which Cineworld terminated the Arrangement Agreement in June. However, while I will review the evidence and make certain findings below, this review has no

⁴ The exceptions do not apply to any event that has a materially disproportionate effect on the Company and its Subsidiaries, taken as a whole, relative to other comparable companies and entities operating in the industries in which the Company or any of its Subsidiaries operate. Cineworld does not take the position that the outbreak of illness had a materially disproportionate effect on Cineplex.

⁵ With respect to the ICA Approval process, Cineworld agreed that it would negotiate “commercially reasonable” amendments or enhancements to undertakings proposed by the government (on how Cineworld would operate the business after closing). The parties also entered into a Joint Defence Privilege and Strategy Agreement at the same time as the Arrangement Agreement. The parties agreed to abide by the strategy set out in Appendix “A” to the Joint Defence Privilege and Strategy Agreement. It states that Cineworld will have met its obligation under s. 4.8(5)(a) of the Arrangement Agreement (to offer commercially reasonable undertakings) provided it offered to the Minister the set of ICA undertakings that the parties listed in Appendix “A”.

bearing on the contractual interpretation issues or my analysis of whether Cineplex breached any covenants in the Arrangement Agreement.

[50] Mr. Mooky Greidinger, his brother Israel Greidinger, and Cineworld's Chief Financial Officer (CFO), Nisan Cohen, testified that at all times after signing the Arrangement Agreement, Cineworld remained committed to closing the Transaction and had the financing in place to do so. They testified that while they had doubts that Cineplex would be able to meet the \$725M Debt Condition, Cineworld was always prepared to close and Mr. Mooky Greidinger was particularly intent on doing the deal. It was only when they became aware of Cineplex's breaches that they decided to terminate the agreement.

[51] Mr. Cohen testified that by as early as mid-February, he had personal doubts that Cineplex would be able to meet the \$725M Debt Condition given Cineplex's weak box office performance in December and early 2020. Mr. Israel Greidinger testified that his doubts arose by the second half of March. Mr. Mooky Greidinger testified that after the theatres closed in mid-March, he started to have his own doubts but thought the theatre closures would be for a few months only and that the Transaction still had a chance. Also, around that time, he was engaged in without prejudice discussions with Mr. Jacob.⁶

[52] I have reviewed the documentary evidence. It paints a very different picture. By March, the pressure was on Cineworld to reconsider the Transaction. Its share price was collapsing. On January 2 it closed at 220p, on February 28 it closed at 155.15p, and on March 17 it closed at 21.38p. Investors sent panicked emails to Cineworld's executives, urging Cineworld to reconsider and walk away from the Cineplex deal. For example, on March 2, Steven Levey of ION Asset Management, one of Cineworld's largest shareholders, exchanged the following text messages with Mr. Cohen:

Ion Guy: WTF is going on??
Mr. Cohen: People are panic from th Virus [...]
Ion Guy: Serious question - have you considered paying the \$30m break up fee and walking away from Cineplex? Based on where the market is now, there is clearly a case for paying a much lower price.
We are long term investors. you know that. But there is no way that you would pay that price today. NO WAY.
Mr. Cohen: We understand and analyzing all options, step by step

[53] Schroders, one of Cineworld's 20-largest shareholders, wrote directly to Tony Bloom, the Chair of Cineworld's board on March 9 saying "[w]hile we appreciate that there would be break fees to be paid by both Cineworld and the Greidinger family, and that the Material Adverse Effect

⁶ I am not drawing any inferences about what led to or occurred during the without prejudice discussions.

clauses add further complication, risking the business as a going concern with the Cineplex deal should be questioned.” I note that there are references in the correspondence between the bankers and Cineworld to a break fee but the Arrangement Agreement does not contain one for Cineworld to walk away in such circumstances.

[54] Mr. Cohen testified that Cineworld was not considering its options and that he was merely trying to placate Mr. Levey. This is inconsistent with his text to Mr. Levey that Cineworld was analyzing all options and Mr. Bloom’s response to Schroders that the board was reviewing all possible options.

[55] On March 12, Cineworld released its preliminary results for the year ended December 31, 2019. The release noted that Cineworld intended to complete the Transaction but included a downside scenario in which if it completed it and had no revenue for two to three months because of cinema closures, Cineworld risked defaulting on the financial covenant ratios set out in its bank loans, which in turn risked Cineworld’s ability to continue as a going concern.

[56] Mr. Levey sent a text message to Mr. Cohen that day. He told Mr. Cohen to say that Cineworld was reconsidering the Cineplex deal – “Nissan, I am shocked you guys write that Cineplex is closing as planned? Surely the sensible thing to do would be to tell the truth – that you are considering your options?” He said, “by making a statement like that it looks like you guys aren’t looking at what’s going on in the world!” Mr. Cohen responded: “There is a different between what yuh can say and what you can do... We are dealing with it.” Mr. Cohen testified that he was informing Mr. Levey that a public announcement was not the appropriate place to discuss plans, mergers or legal contracts.

[57] A Cineworld board meeting was held on March 19. Prior to the meeting, Mr. Bloom asked Mr. Mooky Greidinger for information to send a note updating the board on various matters, including the Cineplex situation. Mr. Mooky Greidinger testified that he did not believe a note was prepared or that the board discussed the Transaction at its meeting because it “was not up to us to avoid the deal”. In light of the pandemic and the pressure from shareholders, I do not accept his testimony that the board did not discuss the Cineplex deal at that meeting.

[58] Cineworld was also facing liquidity concerns. In early March, Cineworld was working with Rothschild & Co. on a USD \$110 million incremental increase to its revolving credit facility (“RCF”). Mr. Cohen testified that the potential lenders were not initially receptive to the increase, that they were “very cold”. Mr. Israel Greidinger explained that many of the potential RCF lenders, who were also lenders on the Cineplex deal, did not want to increase their exposure to Cineworld. Bank of America suggested, for example, that it would increase the RCF but only if Cineworld reduced the Bridge Loan.

[59] Mr. Cohen told the lenders he thought Cineplex would be unable to meet the \$725M Debt Condition. For example, on March 16, HSBC asked Mr. Cohen: “If the Fox [Cineplex] transaction does not go ahead, is the \$48m break fee due? When would it be payable?” Mr. Cohen responded

that: "If Cineplex were to break their leverage threshold of CAD725m on their RCF, the break fee of \$48m + deal costs (c.\$50m) would be payable to [Cineworld]."

[60] The potential RCF lenders continued to seek confirmation that the deal would not proceed. Citizens Bank asked when the Cineplex deal would be "shelved". Barclays asked when there would be certainty around the Cineplex process terminating. Cineworld did not respond in writing. Mr. Cohen repeatedly told the lenders that he would explain the situation to them over the phone. He testified that this was because he preferred to explain his personal views about Cineplex's inability to meet the \$725M Debt Condition orally, not in writing.

[61] By the end of April, Cineworld had not secured an increase in the RCF. On April 24, Mr. Cohen sent a text to Paramvir Sethi of HSBC saying:

You need to trust us about the deal.

There is no double exposure!!!. . .

You need to trust us there is NO deal at 34; no double exposure.⁷

[62] Cineworld continued its efforts to increase the RCF. At 11:25 p.m. on May 14, Mr. Israel Greidinger wrote to HSBC attaching a proposed side letter to be signed by Cineworld and the three lead banks. It stated:

[W]e undertake to HSBC that prior to July 1, 2020 we shall not:

1. draw any amounts of the New Incremental Revolving Commitments; or
2. complete the acquisition of Cineplex.

[63] Almost immediately, Mr. Israel Greidinger emailed HSBC asking it to ignore what he had sent. He and Mr. Cohen then sent identical letters to HSBC and Bank of America stating that the increase in the RCF would be conditional on the Transaction not proceeding:

[W]e undertake to BOA that prior to July 1, 2020 we shall not draw any amounts of the New Incremental Revolving Commitments.

We shall be entitled to draw amounts under the New Incremental Revolving Commitments from July 1, 2020 onwards provided that we have not completed the acquisition of Cineplex Inc.

⁷ Mr. Cohen and Mr. Israel Greidinger testified that the banks' concern about "double exposure" was that Cineworld might waive the \$725M Debt Condition, close the Cineplex deal, and apply the RCF funds towards Cineplex's bank debt. There is no evidence from any of the lenders or documentary evidence to support this testimony. Rather, it appears from the documentary evidence that the real concern on double exposure was that the lenders did not want to finance both the Bridge Loan and Cineworld's operations under the increased RCF.

[64] Mr. Mooky Greidinger testified that the reason Cineworld agreed to conditionality on the RCF increase on May 14 was because it had a commitment on Project Quantum – a USD \$250 million facility secured against Cineworld's assets outside the U.K. and U.S. The documentary evidence does not support that testimony.

[65] After initial discussions with potential lenders to increase the RCF, Cineworld started to look for alternative financing. Due diligence on Project Quantum was carried out in April and May. Mr. Cohen testified that by mid-May, Cineworld was confident that it would be able to raise the USD \$250 million. He testified that by May 14, negotiations had progressed well with Centerbridge Partners Europe LLP, the key lender for Project Quantum. However, by May 14, Arcmont, one of the three potential lenders, was still 11 days away from holding its first due diligence session and Sand Grove, another lender, was a week away from joining the financing process. A financing letter with Centerbridge for USD\$100 million was not signed until May 28, two weeks after Cineworld agreed to conditionality on the RCF. Cineworld did not secure the Project Quantum credit facility until June 22.

[66] Cineworld's pressing need for the RCF increase was apparent. On May 27 (the day the RCF increase was finalized), Cineworld agreed to assume approximately USD \$27 million in foreign exchange liability from Goldman Sachs for it to participate in the additional RCF lending. This converted Cineworld's liability for these fees from deal contingent to an absolute liability, all so that Cineworld could secure the \$110 million loan.

[67] On another front, the work on integration that had progressed actively during the months of January and February stopped in mid-March. From that point onward, all contact between Regal and Cineplex stopped, as did all internal integration planning work at Regal. It never resumed. Mr. Israel Greidinger shut down SA Global's work on March 18 and never restarted it. While Mr. Mooky Greidinger testified that 90% of the integration plan was finished by then, the evidence of Cineplex's witnesses was that there was much left to be done. For example, in the area of personnel alone, the evidence of Raghu Viswanathan (Cineplex's VP of Purchasing, Supply Management & Facility Services) and Chris Doulos (Cineplex's Senior VP Real Estate) is that they received little information about their future positions and those of their teams. Further, Mr. Viswanathan testified that while Regal had engaged Cineplex in discussions about transitioning supplier contracts to Regal, at no point did anyone at Regal reach out with specific steps for the transition process.

[68] I also note that although Cineworld obtained a waiver of the leverage covenant under its RCF around May 28, it did not obtain or even try to obtain a waiver of the same leverage covenant in the Bridge Loan. Mr. Israel Greidinger testified that Cineworld did not seek this waiver because nothing had been drawn on the Bridge Loan by then. However, Cineworld would have had to draw the Bridge Loan on closing (just a few weeks later), which would have subjected Cineworld to a covenant test as at June 30 (to be measured 90 days later).

[69] Considering all of the evidence, I cannot accept the testimony of Messrs. Greidinger and Cohen that Cineworld remained intent on closing the Transaction at \$34 per share throughout the

relevant period. Rather I find, on a balance of probabilities, that by mid-March Cineworld was considering its options. I find that by the third week of April, Cineworld had no intention of proceeding with the deal at \$34 per share. Cineworld was assuring its shareholders that the Transaction would not proceed at that price (or at all). Cineworld was assuring its bankers that the deal would not be going ahead at that price (or at all). Cineworld agreed to conditionality on the RCF increase because it needed the funds and knew that it could not get them if it completed the Transaction. Mr. Israel Greidinger, in order to obtain the RCF increase, went so far as to agree in his May 14 note (that he immediately withdrew) that Cineworld would not close the Cineplex deal.

[70] While I accept that Messrs. Greidinger and Cohen believed Cineplex would not be able to meet the \$725M Debt Condition, I also conclude that they saw that condition (and their control of the ICA Approval process) as Cineworld's way to exit the deal. This is evident from the notes taken by PJT Partners, Cineworld's advisor on Project Quantum, at a due diligence meeting with two potential lenders at the end of April.⁸ Mr. Cohen said (my emphasis added):

- We have a deal with the Canadians. Very happy with it, great company. Good fit with Cineworld/Regal. Run everything from Knoxville, Tennessee office. Unfortunately Canadian cinemas closed from Mid-March. Had to analyze acquisition again. Agreement protects us as there are some scenarios to exit from the transaction
- Main two answers:
 - o Agree w Canadian government on commercial points (20 points) how much capex, employees will hold etc. Only looking on benefit of Canadian economy, not shareholders
 - o Second thing is they commit not to be over CAD725m debt at closing. Will be very hard for them to keep, already CAD625 end of year and paid dividend, spent capex etc.
- Not high chances that deal will happen (**personal view**) [Emphasis in original]. If it happens, will happen in a different part. You can look at share prices, trading well below offer price, so their shareholders understand deal not realistic in current terms. Complex legal issue. Time is working for us. Nobody in cinemas will be open in the next week or two, but in the next few weeks it will be more clear.
- Q: If transaction does not happen, as contract is written, is there a breakage fee you have to pay?
- A: They will not meet the terms of the deal; they will have to pay us. They cannot manage to fulfil CAD725m debt limit. We take rent deferral as part of net debt, same with payments to studios etc. So cannot see scenario where they can commit to \$725m
- Q: Strategic preference for CW on how to proceed?

⁸ It is also evident from the email of April 1 that Mr. Cohen sent to Rothschild, which was asking for information to give to Bank of Ireland on how Cineworld could get out of or renegotiate the Cineplex deal. Mr. Cohen pointed to the ICA Approval clause and the \$725M Debt Condition in the Arrangement Agreement.

- A: Analyzing every hour. Depends on when and how cinemas open. Must be very attractive price to take the deal. Otherwise better to wait. But clear synergy strategy, great fit etc. Analyzing it carefully. Can also discuss on commercial discussion

[71] Not only did Mr. Cohen think that Cineplex would exceed the \$725M Debt Condition, he knew that this was the way for Cineworld to get out of the Transaction. Cineworld expected that without revenues from its theatres, it was only a matter of time before Cineplex would exceed the debt limit. As it turned out, Cineplex never did exceed the \$725M Debt Condition. On May 29, the total amount owing by Cineplex under its Company Credit Agreement was \$665 million. On June 5, that amount was \$656 million.

[72] On June 5, Cineworld sent the notice of default to Cineplex alleging a wide range of breaches under the Arrangement Agreement. Cineworld sent the notice of termination to Cineplex a week later.

ALLEGED BREACHES BY CINEPLEX

[73] I now turn to the alleged breaches of the Arrangement Agreement. Cineworld submits that it was entitled to terminate the agreement due to Cineplex's breach of the Operating Covenant and the other Interim Covenants.

Alleged Breach of the Operating Covenant

[74] Cineworld submits that Cineplex breached the Operating Covenant when it deferred payments to suppliers, film studios and landlords and reduced capital expenditures during the Interim Period.

Cineplex's Cash Management Tools

[75] Gord Nelson, the CFO of Cineplex, testified about Cineplex's cash management tools. He testified that cash flow in the cinema business is highly unpredictable and subject to large swings, as it is dependent upon the quality of the films that exhibitors receive from studios.

[76] Mr. Nelson testified that Cineplex's toolkit of cash management measures consists of three measures:

- EBITDA maximization - includes measures such as accelerating pricing changes and deferring expenses from periods of low revenue to periods of higher revenue;
- Contingency planning, to be used when additional measures are needed in order to effect short-term changes on an expedited timeline; such additional measures included deferral of discretionary expenditures (cap-ex and otherwise), and assessment of payment terms with suppliers; and

- EBITDA challenge – to be used as part of a longer-term response to attendance declines; innovation-based, while also incorporating elements of the two above-noted programs.

[77] For example, Mr. Nelson testified that Cineplex routinely defers its accounts payable at quarter-ends and year-ends to minimize the interest expense that would be incurred on its credit facility in the following quarter.

[78] Professor Mark Zmijewski, an expert in accounting, finance and economics called by Cineplex, testified about the use of cash management tools. He testified that it is standard practice for many companies to manage their working capital in financially challenging times. This includes “shortening the cash conversion cycle” by accelerating accounts receivable, selling inventory, and delaying payment of accounts payable. He testified that extending accounts payable to finance operations is preferable to using bank debt as it does not involve the payment of interest, the pledge of collateral or the imposition of debt covenants. He also said that companies often rely on trade credit (extending accounts payable) as a form of financing when access to credit is limited.

Cineplex’s Conduct Prior to Theatre Closures

[79] Cineworld alleges that Cineplex immediately started to deviate from the ordinary course after the Arrangement Agreement was signed on December 15, 2019, well before COVID-19 became an issue. It submits that Cineplex’s overriding concern was to keep its bank debt under the \$725M Debt Condition.

[80] In December 2019, Cineplex held back payment of \$20 million in trade payables. Mr. Nelson testified that he did this to show Cineworld that its bank debt level was close to the targeted level. He paid the \$20 million in the first week of January. I find that this was consistent with Cineplex’s practice of holding payables from one quarter end to the beginning of the next quarter.

[81] The first two months of 2020 were weak due to disappointing box office performance. The *Star Wars Episode IX* film had underperformed in December 2019. Cineplex’s bank debt balance was increasing. By February 6, Cineplex was projecting a debt balance of \$712 million for the week of April 3. The contemporaneous emails show that in mid-February, Mr. Nelson and Susan Campbell (Senior VP Finance at the time) were becoming increasingly worried about approaching the \$725M Debt Condition and jeopardizing the closing.

[82] On March 2, Ms. Campbell suggested to Mr. Nelson that Cineplex defer all trade payables by 60 days, except for film studios and Cineplex’s main food supplier, Wallace & Carey. Earlier that day, Ms. Campbell and Andrew Imrie (Cineplex’s VP of Financial Planning and Analysis) exchanged text messages noting that Cineworld’s share price had plummeted and that the deal was at risk. Ms. Campbell said that she was “paralyzed with fear” that it would not close and that if it did not, they would have to do it all over again with someone else (as Mr. Imrie commented, at half the price).

[83] Ms. Campbell emailed Mr. Nelson a few hours later and said she wanted to ensure that Cineplex did not “blow the covenant on cash in the deal.” Mr. Nelson immediately agreed to the

deferral. They also agreed to “clamp down hard on spending.” At the same time, Cineplex implemented a plan to review accounts payable on a weekly basis to identify critical suppliers who needed to be prioritized and paid.

[84] On March 8, Mr. Nelson emailed the Cineplex leadership team. He said that by April 1, when the rent roll of \$20 million was due, Cineplex was forecasting that it would exceed \$725 million in bank debt. He explained that he had been actively managing working capital but that other procedures had been put into place to defer payables, accelerate collection of accounts receivable, and restrict capital and discretionary spending. He said that the internal messaging was that “this is a temporary matter in advance of the transaction close and in response to timing of cash receipts as a result of the coronavirus – not a cash crunch.”

[85] Cineworld submits that the deferral of payables on March 2 had nothing to do with COVID-19 and were driven solely by Cineplex’s desire to stay under the \$725M Debt Condition until the Transaction closed. I disagree. The evidence clearly establishes that the impact of COVID-19 on the film exhibition business was on the horizon. Cineplex had learned that the release of a much-anticipated Chinese film, *Detective Chinatown 3*, was being postponed (along with another film, *Rescue*) due to the closure of cinemas in China.

[86] Mr. Jacob testified that the concerns in the cinema industry focused on the availability of film product. Studios depend upon revenues from worldwide releases and the concern was that with government-mandated closures in certain countries, studios might choose to delay the release of film product. On February 18, Mr. Jacob met with representatives from Walt Disney Studios and Universal Studios to discuss their commitment to release certain movies expected in the coming months, including *Mulan* and the latest installments in the *James Bond* and *Fast and Furious* franchises. By March 2, he was urging Mr. Mooky Greidinger to work hard with the studios to keep the product coming because “everyone is freaking out”.

[87] Mr. Viswanathan testified that Cineplex started to experience supply chain challenges in early-to-mid February as factories in Asia began to shut down as a result of COVID-19.

[88] Articles were being written about COVID-19. Trade associations and the Retail Council of Canada were sending newsletters to its members. By the end of February, Cineplex was starting to see a trend of group booking cancellations for both its cinemas and location-based entertainment venues. Those increased on March 4 when the *James Bond* film was delayed from April to November.

[89] I accept that Cineplex was focused on staying under the \$725M Debt Condition in early 2020. However, this focus must be seen in the larger context of what was going on at the time. While Cineplex may not have been predicting theatre closures in January and February, the evidence establishes that there was a steady and growing concern about the impact of COVID-19

on the industry.⁹ There was uncertainty about how long the situation would last. Cineplex was trying to preserve and manage its cash flow during this period of economic uncertainty. I find that the decision to defer payables and restrict spending in early March was made in the context of the very real concerns about COVID-19 and the reality of its impact on the Cineplex business.

Cineplex's Conduct After Theatre Closures

[90] On March 16, Cineplex closed its theatres in response to the pandemic. It was legally required to do so on March 15 in Quebec and on March 17 in Ontario and Alberta. Cineplex quickly took steps to deal with the closure of its theatres and the corresponding decrease in revenues.

Deferral of Payments to Landlords

[91] In mid-March, Cineplex told its landlords it would not be paying April rent and proposed a three-month rent deferral. Mr. Doulos testified that Cineplex's strategy then changed, and it decided to secure abatements. On March 30, Cineplex told its landlords that it would not be paying April rent on the first of the month. Cineplex executives instructed the team that no payment deals were to be made with any landlord. A number of landlords issued default notices. By May 1, Cineplex had received 18 default notices (Regal had received 86 notices by then). According to Messrs. Doulos and Jacob, the landlords were issuing the default notices simply to protect their interests.

[92] Mr. Doulos testified about the strong position that Cineplex held with its landlords. Cineplex held long term leases for theatre spaces that were expensive to build and are extremely difficult to repurpose. Ed Sonshine, the former CEO and current non-Executive Chair of RioCan Real Estate Investment Trust ("**RioCan**"), the landlord of 23 of Cineplex's 160 locations, testified that cinemas function as commercial magnets, attracting customers who then will frequent other businesses on the property. He testified that given how difficult it is to convert cinema spaces to other uses, Cineplex enjoys a particularly strong position with its landlords.

[93] Mr. Jacob testified that he joined a coalition of retail tenants and major landlords to lobby for a government-supported rent relief program. In mid-May, the federal government announced the Large Employer Emergency Financing Facility, which was different from the retail-specific program sought by the consortium. Mr. Jacob testified that he continued to try to persuade the government to adopt a retail-specific solution, but Cineplex shifted its efforts towards negotiating agreements with individual landlords.

⁹ In an article with the publication *Deadline* on April 6, Mr. Mooky Greidinger said that Cineworld had been preparing for a shutdown of theatres two months before the theatre closures. On cross-examination, he said he had been exaggerating but admitted that Cineworld had been preparing for closures one month before they occurred. He testified that by late February, Cineworld was considering the possibility that cinemas might be closed.

[94] By the end of May, Cineplex sent out one of two offers to its landlords, each of which sought abatements. Cineplex ultimately signed agreements with its landlords (after the Arrangement Agreement was terminated) and obtained approximately \$80 million in savings under its leases. By June 26, Cineplex had resolved over 50% of the default notices and negotiated over \$4 million in savings for the April to June closure period with the potential to obtain an additional \$5.5 million in savings for the post-June period. By October 9, Cineplex had agreements that included over \$20 million in abatements for April to June and had resolved all but two of the default notices it had received. Cineplex also expected to enjoy additional negotiated savings of up to \$45 million for the post-June period. Mr. Doulos testified that had Cineplex paid its rent for April to June, it would not have been able to achieve these savings.

[95] There is no evidence that the rent deferral in April to June impaired Cineplex's relationships with its landlords and indeed the evidence is to the contrary. Cineplex has maintained all of its leases in Canada. Mr. Doulos testified that Cineplex maintained great relationships with its landlords as of the termination date. Mr. Sonshine testified that RioCan has an excellent relationship with Cineplex that is absolutely the same today as it was before the pandemic.

Deferral of Payments to Film Studios

[96] Mr. Jacob testified that Cineplex typically pays film studios 35 days after a movie has been exhibited, although there is flexibility in these arrangements. He testified that once Cineplex knew that theatres would be closing in mid-March, Cineplex made the decision to slow down payments to the studios to help with cash management in light of the lost revenues. On March 18, Cineplex deferred payments to film studios by 60 days, except for Disney and a small studio called Videoville Showtime Inc. Enzo Carlucci of KPMG, Cineworld's expert, calculated that Cineplex's payment terms for film studios from March to June ranged from 57 to 123 days after the invoice date.

[97] Mr. Nelson testified that Cineplex negotiated payment plans with the studios over the course of April and into the first week of May and started making payments the week ending May 8. He said that by the week ending June 26, the total owing to film studios (approximately \$6 million) was lower than what the film payables would typically be during non-COVID-19 times.

[98] Mr. Jacob testified that all of the studios were cooperative with Cineplex during this period. Chris Aronson, the President of Domestic Theatrical Distribution at Paramount Pictures, testified that he and Mr. Jacob negotiated a payment schedule for amounts owed to Paramount. Mr. Aronson confirmed that Paramount enjoys an excellent relationship with Cineplex to this day. Mr. Jacob testified that Cineplex did not encounter any difficulty with securing product from film studios after it opened in July.

Deferral of Payments to Non-Film Suppliers

[99] As noted above, Cineplex decided on March 2 to defer its trade payables to non-major suppliers by 60 days. This continued after the theatres were closed although the deferral period

was increased to 90 days and Cineplex started to defer its payables to major suppliers as well. Mr. Carlucci calculated that between March and June, Cineplex paid suppliers between 119 and 156 days after the invoice date.

[100] Mr. Viswanathan testified that Cineplex started to catch up on its payments by the end of June or early July and were caught up by August. He said that Cineplex has not experienced any difficulties securing supplies as a result of its decision to defer payments in March. Some large suppliers even provided fee reductions or credits to Cineplex. Mr. Viswanathan testified that Cineplex continues to have strong relationships with its suppliers and that the recent reopening of its theatres was a resounding success due in part to how suppliers stepped up.

Reduction in Capital Expenditures

[101] By the end of February, Cineplex decided to slow down and delay any uncommitted capital expenditures. Mr. Carlucci calculates that as at March 31, the balance in Cineplex's construction and capital expenditure payables (the accruals for construction costs incurred for capital expenditures) was \$17.3 million and decreased to \$7.5 million by June. He calculates that from April to June, Cineplex underspent on its capital expenditure budget by 101% and did not incur any growth or acquisition related capital expenditures.

Repayment of Bank Debt

[102] Cineworld notes that Cineplex was paying down its bank debt at the same time that it was deferring its payables and rent. Between March 8 and 13, Cineplex repaid \$17 million under the Company Credit Agreement and by March 31 it paid an additional \$26 million. It paid \$2 million on May 8, \$5 million on May 22 and \$12 million on June 5. Cineplex also drew down on its credit facility during this time: \$5 million on April 1, \$2 million on May 1, \$3 million on June 5, and \$7 million on June 12. Mr. Nelson's evidence is that Cineplex ordinarily paid down and drew on its credit facility as the needs of the business warranted.

Cineplex told Cineworld about the Deferrals

[103] Cineplex told Cineworld that it was making these payment deferrals and spending reductions. Mr. Nelson testified that on April 4, he told Mr. Cohen that Cineplex was not paying any rent and was seeking government assistance. He also told Mr. Cohen that Cineplex was deferring its payables. On April 16, Mr. Doulos spoke to his counterpart at Regal and discussed the efforts being made to deal with landlords. Mr. Nelson and Mr. Cohen corresponded in May and Cineplex advised that it was continuing to withhold rent. Mr. Jacob also testified that he told Mr. Mooky Greidinger that Cineplex was deferring payments to film studios.

Case Law and Applicable Legal Principles

[104] In mergers and acquisition agreements where there is a period of delay between signing and closing, the parties typically address the problems posed by that delay in two ways. The first is through the material adverse effect clause (MAE). The second is through interim covenants.

[105] MAE clauses address events that occur during the interim period. An MAE has been defined as "...the occurrence of unknown events that substantially threaten the overall earnings potential of the target in a durationally-significant manner.": *Fairstone Financial Holdings Inc v. Duo Bank of Canada*, 2020 ONSC 7397, at para. 64. Typically, where a party has suffered an MAE, the other party can cancel the deal without cost: *Akorn Inc. v. Fresenius Kabi AG Inc.*, C.A. No 2018-0300-JTL (Del. Ch. Crt) at p. 118, citing Robert T. Miller, *the Economics of Deal Risk: Allocating Risk Through MAC Clauses in Business Combination Agreements* (2009) 50 Wm & Mary L. Rev. 2007 at p. 2012 ("Miller").

[106] The risks of unknown events can range from systemic risks (that are beyond the control of all parties) to business risks (over which the seller has significant control). Generally, an MAE clause provides for the seller to retain the business risks while the buyer assumes the other risks, including systemic risks: *Akorn*, at pp. 122-123, citing Miller, at pp. 2071-91.

[107] In this case, the Company Material Adverse Effect clause squarely addressed the risk of a pandemic and allocated that systemic risk to the buyer, Cineworld. The definition excludes "outbreaks of illness". Under s. 6.2(4) of the Arrangement Agreement, Cineworld could refuse to close if a Company Material Adverse Effect occurred between signing and closing. However, if that event was a pandemic, the exclusion applied and Cineworld could not refuse to close.

[108] While MAE clauses address events that occur between signing and closing, interim covenants, including an "ordinary course" covenant, address the manner in which the seller has to operate the business during the interim period.

[109] The caselaw has established that interim covenants (and in particular the covenant to operate in the ordinary course) serve two fundamental purposes:

- To ensure that the business the buyer bargained for at closing is essentially the same as the one it decided to buy when signing the agreement of purchase and sale: *Fairstone*, at para. 167; *Akorn*, at p. 206.
- To eliminate or mitigate the "moral hazard" of sellers acting in their own interest to the detriment of the purchaser during the interim period: *Fairstone*, at para. 167; Miller, at p. 2038.

[110] The concept of what is in the ordinary course of business for a particular business is a flexible and contextual one and is a question of mixed fact and law: *Stelco Inc. (Re)*, 2007 ONCA 483, [2007] O.J. No. 2533, at para. 81 citing *369413 Alberta Ltd. v. Pocklington*, 2000 ABCA 307, 271 A.R. 280 (C.A.), at para. 23. In the mergers and acquisitions context, the cases have

considered whether a buyer can be relieved from completing a transaction where the seller operated outside of the ordinary course. The court's analysis tends to be fact specific.¹⁰

[111] In general terms, buyers have been excused from closing a transaction where the seller's actions significantly change the nature of the business or have a long-lasting impact that would affect the buyer in operating the business after closing: *Fairstone*, at paras. 163, 179.

[112] For example, in *AB Stable VIII LLC v MAPS Hotels and Resorts One LLC*, C.A. No. 2020-0310-JTL (Del. Ch. Ct), the seller (AB Stable) agreed to sell its Strategic hotel business to the buyer (MAPS Hotels and Resorts). The pandemic intervened, the buyer refused to close the transaction, and the seller brought an action for specific performance. The court found that the buyer was not excused from closing under the MAE clause. However, it held that the seller breached the ordinary course covenant. The court found that the seller had significantly altered its business in response to COVID-19 and acted in ways that it never had in the past by closing (not in response to government mandates) two of its hotels and limiting the operations of thirteen other hotels. In particular, the court held that by laying off or furloughing 5200 full time employees, the seller had created a situation where the buyer would be left with serious staffing shortages and labour relations challenges once it tried to re-open. This would have been contrary to the purpose of the operating covenant as it would have left the buyer with a business that was inoperable and not what it had initially bargained for.

[113] This can be contrasted with the case of *Fairstone*. In that case, the seller (Fairstone) sought specific performance when the buyer (Duo) refused to close in light of Fairstone's responses to the pandemic. The court found that Fairstone, a consumer finance company, did not operate outside of the ordinary course of business when it dismissed 40 out of 1400 employees; decreased expenditures by 10%; tightened customer credit requirements; limited real estate appraisals to exterior viewers; ceased automobile auction services; and implemented a foreclosure moratorium. The court found that this conduct was temporary, had been terminated by the closing date, had no long-lasting effect on business, and imposed no obligation on the buyer. The court held that Fairstone's response to the pandemic was consistent with the measures it had taken in past economic contractions to reduce expenditures and tighten lending requirements. The court held that apart from the alleged changes to accounting methodology that were not material, none of the alterations Fairstone made to its business involved non-arm's length transactions, potential moral hazards, equities that weighed in favour of Duo, created long-term obligations or created structural changes to Fairstone's business.

[114] The court's focus on the nature and degree of the operational changes that would excuse a buyer from closing is evident in two non-pandemic cases. In *Cooper Tire & Rubber Co. v. Apollo (Mauritius) Hldgs. Pvt. Ltd.*, 2014 WL 5654305, *17 (Del. Ch. Oct. 31, 2014), relied on in *AB Stable*, the buyer (Apollo) contracted to buy the seller (Cooper), a large American tire company

¹⁰ Some of the cases have articulated various factors that the court may consider in determining whether conduct has been in the ordinary course of business: *Stelco*, at para. 101; *Fairstone*, at para. 182.

that was the majority owner of a joint venture that manufactured and sold tires in China. The principal of the minority owner opposed the merger and physically seized the joint venture's facility, preventing production of the seller's products at the facility and limiting its access to financials. These events were held to be a breach of the ordinary course covenant. Further, to stop the minority owner, the seller ceased making payments to suppliers who continued to ship supplies to the facility. The court held that this was a conscious effort by the seller to disrupt operations and a failure by the seller to cause its subsidiary to conduct business in the ordinary course. In that case, the court also found that because of the wording of the contract, the seizure of the facility was not covered by the exclusion to the MAE clause (unlike this case where the pandemic is excluded from the definition of Company Material Adverse Effect).

[115] In *Akorn*, the court held that the seller (Akorn), a pharmaceutical company, breached the ordinary course covenant when it cancelled regular audits, did not maintain a data integrity system as it was supposed to do, submitted a regulatory filing that relied on fabricated data, and failed to respond appropriately to whistleblower letters that it had received. The court held that these actions were material, a departure from the practices of the seller as well as other companies in a similar industry, and a deviation from what the buyer could reasonably expect from what it would receive at closing. The court also found that the buyer was excused from the transaction because a material adverse effect had occurred.

The Parties' Positions

[116] Cineplex's position is two-fold. First, it submits that the exclusion of "outbreaks of illness" from the definition of Company Material Adverse Effect allocated the risk of a systemic event – a pandemic – to Cineworld. It says that this event, and any responses to it, are governed by the Company Material Adverse Effect clause, not by the Operating Covenant. Second, Cineplex submits that even if its conduct is governed by the Operating Covenant, Cineplex did not breach the covenant when it responded to the pandemic as it did. Cineplex argues that in interpreting the Operating Covenant, the court must read the contract as a whole and not interpret the clause in a way that negates the other clauses that allocate the risk of a pandemic to Cineworld.

[117] Cineworld submits that the definition of the Company Material Adverse Effect has nothing to do with how Cineplex was required to operate its business during the Interim Period.¹¹ It says that the Company Material Adverse Effect clause only comes into play at closing in determining whether the condition in s. 6.2(4) is met and Cineworld is relieved of the obligation to close. Cineworld argues that Cineplex's operations during the Interim Period are governed solely by the Operating Covenant. It submits that under that covenant, Cineplex was required to operate in the Ordinary Course at all times during the Interim Period, consistent with its past practices

¹¹ In its June 5 default letter, Cineworld took the position that Cineplex had suffered a Company Material Adverse Effect when it fractured its relationships with its landlords. Cineworld did not pursue that allegation at trial.

benchmarked against the previous two to five years.¹² Cineplex was not permitted to deviate from the Ordinary Course, even in the face of the pandemic, and was required to operate as it usually did in non-pandemic times. Cineworld says that this was the risk Cineplex assumed under the Arrangement Agreement when it agreed to operate in the Ordinary Course during the Interim Period.

Did Cineplex Breach the Operating Covenant?

[118] I accept Cineworld's submission that the conduct of the business during the Interim Period is governed by the Operating Covenant (and the other covenants in s. 4.1 of the Arrangement Agreement.) Section 4.1 is clearly the operative section that sets out how Cineplex is to operate the business and the restrictions that apply to those operations during the Interim Period. However, I agree with Cineplex that in interpreting the clause, I must read the agreement as a whole and not interpret the clause in a way that negates any other provision of the Arrangement Agreement.

[119] According to the Supreme Court of Canada in *Sattva Capital Corp. v. Creston Moly Corp.*, 2014 SCC 53, [2014] 2 S.C.R. 633, at para. 47, when interpreting a contract, the overriding concern is to determine the intent of the parties and the scope of their understanding. In order to determine their intent and understanding, the court must read the contract as a whole, giving the words used their ordinary and grammatical meaning, consistent with the surrounding circumstances known to the parties at the time of formation of the contract. The Supreme Court of Canada emphasized, at para. 64, that construing a contract as a whole is "a fundamental principle of contractual interpretation."

[120] In *Tercon Contractors Ltd v. British Columbia (Transportation and Highways)*, 2010 SCC 4, [2010] 1 S.C.R. 69, at para. 64, Cromwell J., for the majority, emphasized that "[t]he key principle of contractual interpretation here is that the words of one provision must not be read in isolation but should be considered in harmony with the rest of the contract and in light of its purposes and commercial context."

[121] I first look at the wording of the Operating Covenant. Cineworld's interpretation ignores the wording of that clause in its entirety. The covenant has two parts. Both parts apply and neither is subordinate to the other. The first part requires Cineplex to "conduct its business in the Ordinary Course and in accordance with Laws." The second part requires Cineplex to "use commercially reasonable efforts to maintain and preserve its and its Subsidiaries business organization, assets, properties, employees, goodwill and business relationships with customers, suppliers, partners and other Persons with which the Company or any of its Subsidiaries has material business relations." Cineworld focuses only on the first part, not the second.

¹² Mr. Carlucci calculated that for rent, the benchmark is payment on the first day of the month. For trade payables, the benchmark is to be measured against the average days payable outstanding (DPO) of 60 days. For film studios, the benchmark is 35 days. For capital expenditures, the benchmark is underspending by 15% on an annual basis.

[122] The first part of the Operating Covenant requires Cineplex to operate the business in the Ordinary Course and in accordance with Laws. Ordinary Course means actions “taken in the ordinary course of the normal day-to-day operations of the business of the Company...consistent with past practice.” In this case, Cineplex’s theatres were closed due to government mandates. Cineplex could not conduct its operations normally as it had in the past. It had to operate with its theatres closed. In my view, Cineplex cannot be held in default of the Ordinary Course covenant when it was prevented from conducting its normal day-to-day operations by government mandate.

[123] Further, Cineplex’s response to the closures was consistent with the measures it had used to manage its liquidity in the past. As noted in *Fairstone*, at paras. 194-195, “consistent” does not mean identical; it means congruous, compatible and adhering to the same principles of thought and action. In this case, Cineplex did not sell assets, restructure the business or change the nature of its operations. It used the cash management tools of payment deferrals and spending reductions to preserve its cash flow during the period that its theatres were closed. As Mr. Nelson and Ms. Campbell both testified, these were levers that Cineplex had previously used to manage its liquidity in a business with fluctuating and unpredictable revenues. Although Cineplex used these tools on a larger scale because of the mandated theatre closures, this practice was consistent with its use of cash management tools in the past.

[124] With respect to the second part of the Operating Covenant, I find that the deferral and spending reductions taken by Cineplex to conserve its liquidity were commercially reasonable efforts to maintain and preserve the business once the theatres were closed. In particular, my finding is supported by the following evidence:

- Mr. Carlucci’s evidence is that if Cineplex had operated as it did during non-pandemic times, it would have exceeded the overall limits of its \$800 million credit facility by the end of April and been left with zero liquidity. In my view, it cannot be commercially reasonable for a company to manage its business in a way that will leave it with no liquidity.
- Professor Zmijewski testified that a business without revenues has to conserve cash in order to survive. He explained that if Cineplex had not deferred its payables and curtailed spending, that would have weakened Cineplex’s financial position and undermined its ability to preserve its assets and goodwill. Further, if Cineplex had drawn on its bank debt to make these payments, that would have compromised its leverage with third parties; failed to preserve its ability to access additional capital if needed; converted unsecured debt into secured debt; and put Cineplex to increased interest expense. This is consistent with the evidence of Mr. Nelson who testified that it was important for Cineplex to keep ample head room under its

revolving credit facility.¹³ Mr. Cohen also agreed that it is a prudent move to preserve credit in the face of economic uncertainty.¹⁴

- Mr. Mooky Greidinger testified that when Cineworld closed its cinemas in response to the pandemic, it also withheld payment and negotiated deals with suppliers, landlords and film studios. Professor Zmijewski testified that Cineplex's deferrals and steps were consistent with steps taken by other peer companies at the time. While Cineworld points to differences in the precise details of how Cineworld and other peer companies dealt with third parties, there is no question that Cineplex was not alone in adapting its payment and spending practices once its theatres were closed.¹⁵
- Cineplex deferred payment of rent to landlords while it was working with a consortium to seek rent relief from the government. Landlords were a part of the consortium and it was a cooperative effort. When that effort proved unsuccessful, Cineplex started to negotiate directly with its landlords, ultimately securing significant rent savings.
- There is no evidence that Cineplex's relationships with third parties were damaged or impaired. The evidence is to the contrary. The Cineplex witnesses, along with Mr. Aronson and Mr. Sonshine, all testified that Cineplex's relationships continued throughout the pandemic and remain strong to this day. Further, when deferring rent, Cineplex knew that it had a strong position with its landlords and would be able to work through the pandemic on a cooperative basis, without jeopardizing its leases.¹⁶

[125] Cineworld submits that under the Operating Covenant, Cineplex was required to operate during the pandemic exactly as it did during non-pandemic times, failing which Cineplex would

¹³ He testified that although Cineplex's credit facility was for \$800 million, for practical purposes it was \$750 million because the bank imposed a \$50 million liquidity requirement. Cineworld argues that the credit agreement imposed no such liquidity requirement but did not put this to Mr. Nelson in cross-examination. I accept Mr. Nelson's evidence that he was managing to a \$750 million credit limit, which was not much higher than the \$725M Debt Condition in the Arrangement Agreement.

¹⁴ Some of the peer companies reviewed by Professor Zmijewski did increase their credit facilities during the Interim Period. That option was not available to Cineplex as it was precluded from accessing new credit under the Arrangement Agreement. In any event, Mr. Nelson and Mr. Cohen agreed that preserving credit in the face of economic uncertainty was prudent and important.

¹⁵ Cineworld argues that the definition of Ordinary Course required Cineplex to operate consistent with its own past practice, precluding any comparison to others. That argument only relates to the first part of the Operating Covenant. My consideration of peer companies relates to the second part, namely whether Cineplex's efforts to preserve the business were commercially reasonable.

¹⁶ Cineworld points to a reference in Mr. Sonshine's email to Mr. Jacob of May 28 to in which he said that RioCan was planning to start enforcing its remedies the following week and would find out which tenants were going to be willing to go CCAA. I see that statement (which referred to all tenants, not just Cineplex) as posturing for negotiations.

be in breach of the Operating Covenant. I cannot accept that interpretation. It ignores the other provisions of the Arrangement Agreement and fails to read the agreement as a whole.

[126] The parties agreed, through the operation of s. 6.2(4) and the exclusion of a pandemic from the definition of Company Material Adverse Effect, that Cineworld could not refuse to close if a pandemic occurred between signing and closing. They allocated this systemic risk to Cineworld. Cineworld's narrow interpretation of the Operating Covenant would reallocate this risk back to Cineplex. It would effectively permit Cineworld to refuse to close if a pandemic occurred between signing and closing. It would render the other provisions of the agreement meaningless. It would not be a harmonious reading of the various clauses of the Arrangement Agreement. Cineworld's approach would not be in keeping with the principles of *Sattva* and *Tercon* set out above.

[127] I also do not accept Cineworld's argument that the deferrals changed the economics of the deal. Mr. Carlucci testified that Cineplex's actions shifted \$200 million in financial obligations onto Cineworld after closing. However, Peter Graham of KPMG, Cineworld's expert, testified that the real issue is whether a deferral of payables results in a build-up of overdue liabilities, which could change the profile of the company's balance sheet. The evidence before me is that the profile of the company did not change. The liabilities of Cineplex as at June were no greater than they were at the time the Arrangement Agreement was signed.¹⁷ Further, I accept Cineplex's submission that the \$200 million figure itself is overstated as it does not account for the \$80 million in rent savings and the remaining capacity on Cineplex's credit facility up to the \$725M Debt Condition.¹⁸

[128] The reality is that the economics of the deal did not change because of the deferrals and spending reductions. It was the pandemic that changed the economics of the Transaction. Because of the pandemic, Cineplex was no longer the attractive deal to Cineworld at \$34 per share that it had been when the Arrangement Agreement was signed. That is manifestly clear from the reactions of Cineworld shareholders and lenders described above. However, that was the systemic risk that Cineworld assumed when it agreed to exclude the pandemic from the definition of Company Material Adverse Effect. In my view, Cineworld is attempting to use the Operating Covenant as a means of circumventing the very risk that it assumed.

[129] The case of *AB Stable*, on which Cineworld relies, is distinguishable. There were several differences between the wording of the covenant in question and the one at bar. More important,

¹⁷ Cineplex's Total Liabilities on June 30 were \$2.420 billion compared to \$2.509 billion as at the date of the Arrangement Agreement and \$2.422 billion on September 30, 2019. Cineplex's Current Liabilities (which include such items as trade payables and overdue rent) were \$528.9 million as at June 30. This is \$60 million less than the Total Current Liabilities as at December 31, 2019 and \$70 million more than as at September 30, 2019. Moreover, the Total Current Liabilities as at June 30 could have been reduced to \$468.9 million if Cineplex had borrowed up to the \$725M Debt Condition imposed by the Arrangement Agreement, and had used that increased borrowing to satisfy some of its payables.

¹⁸ Cineplex also points out that in his calculation of deviations from past practice, Mr. Carlucci used a DPO figure of 60 instead of 79 days for payables and 15% instead of 40% underspend for capital expenditure, both of which would have reduced the financial impact of Cineplex's deferrals and spending reductions.

the court observed, at p. 181, that the steps taken by the seller had not preserved the business; rather, the seller had “gutted it”. The court found that the changes were “drastic”, “dramatic”, “extraordinary”, “unprecedented”, and that they departed “radically from the normal and routine operation” of the hotels. The court found, at p. 177, that the decisions of the seller in response to the pandemic (which were not legally required) were actions that “radically changed the character of their operations.”

[130] In this case, Cineplex’s responses were temporary cash management measures put into place when its theatres were closed by government mandate. Those measures were consistent with Cineplex’s use of cash management tools to manage its liquidity in the past. Its actions enabled it to preserve its business and emerge with its business and relationships intact. The conduct did not render the nature of the business different than it was at the time of signing. The reason for the conduct was to preserve the cash flow of the company when its revenues were drastically reduced from the theatre closures. The conduct was pursued in good faith for the purpose of continuing the business and avoiding its deterioration. Cineplex’s actions did not engage any of the concerns underlying the purpose of ordinary course covenants.

[131] Cineworld is highly critical of Cineplex for taking the \$725M Debt Condition into account in managing its cash flow during the Interim Period. Cineplex concedes that it could not have deferred its payables solely for the purpose of staying under the \$725M Debt Condition in a non-pandemic situation but that it was commercially reasonable for Cineplex to consider all debt limits as a factor in managing its cash flow during the pandemic. I agree.¹⁹

[132] Finally, with respect to the decision to defer payables on March 2, I find that Cineplex used the cash management tools in the context of the growing concerns about COVID-19 and its impact on the theatre business. The fact that Cineplex was also concerned about staying under the \$725M Debt Condition did not disentitle it from using this cash management tool. In any event, Cineplex points out that the earliest date on which any of Cineplex’s suppliers were affected by the decision to defer payables was its pay-thru date of March 7, just nine days before the theatres were closed. There was no impact on Cineplex’s days payable outstanding for its invoices by the end of March. Even if I accept Cineworld’s argument that this was a breach of the Operating Covenant, it was not in a material respect and would not have enabled Cineworld to refuse to close the Transaction under s. 6.2(2) of the Arrangement Agreement.

[133] In summary, I conclude that based on the applicable legal principles and the evidence before me, Cineplex did not breach the Operating Covenant.

¹⁹ There are some references in the record to Cineworld taking the position that it would apply the deferrals towards the \$725M Debt Condition. Cineworld has not pointed to anything in the Arrangement Agreement that permits Cineworld to count deferrals towards the debt limit under the Company Credit Agreement.

Alleged Breach of other Interim Covenants

[134] Cineworld alleges that Cineplex breached several other covenants during the Interim Period.

Impermissible Transfer of an Asset

[135] Cineworld alleges that in its dealings with RioCan, Cineplex breached the covenant in s. 4.12(2)(g) not to transfer an asset with a value greater than \$1 million individually (or \$3 million in the aggregate) and the covenant in s. 4.1(2)(dd) not to agree, resolve or commit to do so.

[136] As noted above, RioCan holds 23 of Cineplex's leases. One of those leases is for the Cineplex Cinemas Queensway in Etobicoke ("**Queensway**"). It is one of Cineplex's busiest theatres and its highest cash flow generating site (\$11 million per year). RioCan and its partner Talisker owned the land and had a ground lease with Cineplex with a remaining term of 25 years. Cineplex had contractual rights that restricted RioCan's ability to fully redevelop the entire site and more limited rights that restricted RioCan from developing the Pad Lands at the north end of the Queensway site.

[137] For years, RioCan had discussed with Cineplex the possibility of Cineplex terminating its lease at Queensway to permit RioCan to completely redevelop the site or to lift Cineplex's rights over the Pad Lands. In a letter dated February 14, Mr. Sonshine wrote to Mr. Jacob about redeveloping the Pad Lands and said "I have spoken to you previously regarding this property and certainly understand at this point, the approval of Cineworld will be required for what I am proposing." Mr. Jacob also testified that he knew that Cineworld approval was required before Cineplex could conclude any deal with RioCan.

[138] Cineplex did not pay rent to its landlords on April 1. After it became clear that there was not going to be a government relief program, Cineplex and RioCan started working on a negotiated solution. RioCan linked the resolution to its plans to redevelop the Pad Lands. RioCan was also interested in redeveloping its property at the Colossus site, where Cineplex has a theatre.

[139] On May 11, RioCan sent notices of default to Cineplex in respect of all 23 leases, including Queensway. On May 27, Mr. Jacob and Mr. Sonshine met. At the meeting, and in subsequent phone calls and emails, the parties focused on terms in which RioCan would pay Cineplex \$21 million in tranches; Cineplex would allow RioCan to redevelop the Pad Lands; RioCan would relocate and construct the theatre at the Colossus; Cineplex would pay all of its rent in full by September; and RioCan would give an abatement of 33% of gross rent for October to December. Even though these terms were worked out, there were terms that still needed to be addressed, as set out in the email dated June 2 from Andrew Duncan, Senior VP, Development at RioCan, to Mr. Doulos at Cineplex.

[140] Cineworld argues that Cineplex breached its covenant not to transfer assets when it agreed to the essential terms of the deal with RioCan.²⁰ It submits that without Cineworld's knowledge or consent, it agreed to sell valuable contractual and location rights in exchange for rent forgiveness and the promise of a new theatre building at Colossus. I disagree.

[141] It is clear from the record that both Cineplex and RioCan knew that Cineworld's consent was required before any agreement could be finalized. This is supported by the testimony of Mr. Sonshine, Mr. Jacob, Mr. Doulos and Anne Fitzgerald (Cineplex's Chief Legal Officer). It is further supported by Mr. Sonshine's contemporaneous email of February 14.

[142] This is consistent with how Cineplex sought approval from Cineworld for other contracts during the Interim Period. Cineplex did not involve Cineworld in the negotiation process (nor was it required to under the Arrangement Agreement). Rather, Cineplex sent several agreements to Cineworld for its approval but only after negotiations had concluded and the essential terms settled. This was no different in the case of the RioCan locations.

Amendment of Contracts

[143] Cineworld argues that Cineplex breached the covenant in s. 4.1(2)(x) not to amend in a material respect any of its Significant Contracts, which included 35 of its Material Leases as defined in the Arrangement Agreement. Cineworld submits that in withholding rent, Cineplex guaranteed that its Material Leases would be amended.

[144] I reject this submission. Whatever actions Cineplex took or discussions it had with its landlords, there were no amendments to any of the leases while the Arrangement Agreement was in effect. As noted above, the uncontradicted evidence is that Cineplex knew that it required consent from Cineworld before entering into binding agreements with any of its landlords and that it followed that requirement.

Indebtedness Covenant

[145] Cineworld argues that Cineplex breached the covenant in s. 4.1(2)(o) not to create any new source of indebtedness over \$5 million when it deferred rent and payables. I reject this submission. The language of this covenant clearly applies to bank debt. It refers to the creation of new "credit facilities". It refers to indebtedness under a "guarantee, indemnity, bond, standby or documentary letter of credit, banker's acceptance of any other instrument issued by a bank of financial institution". It does not apply to fluctuations in Cineplex's working capital.

²⁰ It also submits that this was a breach of the Operating Covenant and the covenant in s. 4.1(2)(dd) not to agree, resolve, or commit to do anything not permitted by s. 4.1(2). My analysis on the RioCan leases applies to these other covenants.

Budget Covenant

[146] Cineworld argues that Cineplex also breached the covenant in s. 4.1(2)(cc) not to amend its annual budget when it unilaterally deferred spending and diverted its funds to pay down its Company Credit Agreement. There is no evidence to support that allegation. Mr. Nelson's uncontradicted evidence is that variations in expenditures or revenues compared to the budget would not be considered an amendment of the budget nor would the budget be amended if certain revenues or expenditures did not materialize. This is consistent with Mr. Mooky Greidinger's evidence that Cineworld did not revise its budget if results did not meet budgeted targets. There is no evidentiary basis to find that Cineplex amended its budget during the Interim Period.

Alleged Breach of Duty of Honest Performance

[147] Cineworld alleges that Cineplex breached its duty of honest performance by deliberately and knowingly misleading Cineworld with respect to material and relevant information related to Cineplex's compliance with the Arrangement Agreement, particularly its performance of the Interim Covenants. I reject this submission.

[148] In *Bhasin v. Hrynew*, 2014 SCC 71, [2014] 3 S.C.R. 494, the Supreme Court of Canada held, at para. 73, that there is a general duty of honesty in contractual performance and that "[t]his means simply that parties must not lie or otherwise knowingly mislead each other about matters directly linked to the performance of a contract". In *C.M. Callow Inc. v. Zollinger*, 2020 SCC 45, 452 D.L.R. (4th) 44, at para. 3, the majority of the Supreme Court of Canada affirmed that parties must not lie or otherwise knowingly mislead one another.

[149] Cineworld seeks to impose on Cineplex a general duty to provide information about its operations that Cineworld was not entitled to receive under the Arrangement Agreement. Its information rights are set out in s. 4.9(1), which gives Cineworld the right to request "such financial and operating data and other information relating to the business of the Company and its Subsidiaries as [Cineworld or its representatives] may reasonably request."

[150] As noted above, Mr. Nelson told Mr. Cohen about the rent and payment deferrals in their phone call on April 4 before Cineworld issued any information requests. Cineworld issued formal requests under s. 4.9(1) on April 16 and May 19. Cineplex responded on April 27, May 13 and May 26. According to Mr. Nelson, some of those requests were overreaching and burdensome, which was difficult because employees were working from home. For example, Cineworld sought an invoice by invoice analysis of all of Cineplex's accounts payable. Mr. Nelson asked Cineworld to prioritize its requests to those required for ICA Approval but Cineworld refused. I find that despite these constraints, Cineplex provided answers to the information requests in a timely manner.

[151] Cineworld alleges that Cineplex provided misleading information on the type and status of rent relief it was seeking from the government and landlords.²¹ I disagree. Cineplex was clear that it had not been paying rent, had received default notices from landlords, was trying to obtain government relief through the consortium, and was in the process of negotiating with individual landlords when the government rent relief was not forthcoming. Cineworld's position that it wanted more details is insufficient to ground a claim for breach of the duty of honest performance.

[152] Cineworld alleges that Cineplex's conduct in deferring payables was an attempt to evade its contractual duties. Given that I have found that Cineplex did not breach of any of its contractual duties by deferring payables, there is no basis for this submission.²²

DAMAGES

[153] Cineplex advances various damage calculations for breach of contract. It relies on the expert evidence of Howard Rosen, an expert in damages quantification, business valuation and corporate finance from the Secretariat firm. His alternative and complimentary measures of damages are set forth in the following chart:

	(In millions)	Loss	Prejudgment interest	Total
1.	The consideration that Cineworld would have paid to the Securityholders less the value of the securities retained	1,315.7	8.6	1,324.2
2.	Diminution in value of Cineplex's future cash flow	807.8	5.3	813.0
3.	Loss of synergies expected to be achieved by Cineplex	1,236.6	8.0	1,244.6
4.	Cineplex's liability to redeem DSUs, PSUs, and RSUs	6.4	0.0	6.4
5a.	Cineplex's credit facilities	663.0	4.3	667.3
5b.	Carrying costs on Credit Facilities	30.8	0.1	30.9
5c.	Carrying costs on Other Loans	14.2	0.0	14.2
6	Cineplex's transaction expenses	5.5	0.0	5.6
	Benefits obtained by Cineworld			
7a.	1. Avoided loss on the Cineplex shares	806.2	5.2	811.4
7b.	2. Avoided transaction costs	178.4	1.2	179.6
7c.	3. Avoided carrying costs of debt	124.5	0.3	124.8

²¹ Cineworld submits that Cineplex did not tell Cineworld that the nature of the relief the consortium was seeking from the government was a loan. The proposal was actually both an abatement from landlords and a loan from the government to pay the balance of the rent owed by retailers. In any event, the proposal did not succeed, and the issue is moot.

²² In the alternative, Cineplex argues that even if it breached the Arrangement Agreement, Cineworld was not entitled to terminate the agreement because it acted dishonestly in exercising its termination rights. Since I have found that Cineplex did not breach the Arrangement Agreement, there is no need to address Cineplex's alternative argument.

[154] Mr. Rosen testified that measures 1, 2, and 3 in this chart are independent of one another and to an extent duplicative, so only one of these measures could be awarded to Cineplex. Mr. Rosen further testified that measures 4, 5a, 5b, 5c, and 6 could all be awarded in tandem or independently in any combination and could be awarded in combination with measure 3 (Synergies) but not measures 1 and 2. He testified that measures 7a, 7b, and 7c together reflect a disgorgement amount for the benefits obtained by Cineworld as an alternative to the other measures of damages.

[155] Cineworld disputes all of these measures of damages, except for #6. It accepts that Cineplex would be entitled to recover its transaction expenses of \$5.5 million as reliance damages. It does not accept that expectation damages are recoverable in this case.

[156] With respect to Mr. Rosen's damage calculations, Mr. Carlucci disagreed with some of the methodologies and assumptions used by Mr. Rosen but did not put forward any alternative calculations.

[157] The usual measure of damages in a contract case is expectation damages. The plaintiff is entitled to the value of the promised performance: *Bank of America Canada v. Mutual Trust Co.*, 2002 SCC 43, [2002] 2 S.C.R. 601, at para. 26, citing S.M. Waddams, *The Law of Damages*, 3rd ed. (Toronto: Canada Law Book, 1997), at p. 267. A party who sustains a loss by reason of a breach of contract is, "so far as money can do it, to be placed in the same situation, with respect to damages, as if the contract had been performed": *Bank of America*, at para. 27. There is no reason that Cineplex should not be entitled to recover expectation damages for breach of contract in this case.

[158] Cineworld argues that Cineplex is not entitled to expectation damages as it could have sought specific performance of the Arrangement Agreement. I disagree. Prior to Cineworld's termination on June 12, Cineworld's position was that it had every intention of completing the Transaction. There was no basis for Cineplex to have sought specific performance prior to June 12. On June 12, Cineworld issued the notice of termination and advised the Agencies that it was withdrawing its application for ICA Approval. By doing so, it precluded Cineplex from seeking specific performance. I do not accept Cineworld's argument that an order for specific performance requiring Cineworld to use its best efforts to seek ICA Approval from the Agencies, after it withdrew its application following an extended negotiation process, would have been an appropriate remedy.

[159] I have reviewed the various alternatives proposed by Cineplex. In order to decide the issue of damages, I consider it necessary to address only two of them. As explained below, I do not consider #1; loss of consideration to shareholders, to be an appropriate measure of damages. However, I agree that damages can and should be awarded on the basis of #3, loss of synergies to Cineplex. In addition, Cineplex is entitled to recover its transaction costs, as provided for in s. 2.10(2) of the Arrangement Agreement and as conceded by Cineworld.

Loss of Consideration to Shareholders

[160] Cineplex submits that it should be entitled to recover the value of the consideration that would have been payable to its shareholders had the Transaction been completed, less the residual value of the shares on the termination date.

[161] This measure of damages cannot succeed. Quite simply, the losses that Cineplex seeks to recover are those of the shareholders, not Cineplex. Under the terms of the Arrangement Agreement, if the Transaction was completed, the purchase price for the shares was payable to the shareholders. There is nothing in the agreement that entitled Cineplex, as the contracting party, to recover the loss of the consideration to shareholders if the Transaction was not completed.

[162] Under s. 8.10 of the Arrangement Agreement, the shareholders are third-party beneficiaries of the contract and have limited rights as set out therein (my emphasis added):

- (1) Except as provided in Section 2.14, Section 4.4, Section 4.12 and Section 8.20 which, without limiting their terms, are intended as stipulations for the benefit of the third Persons mentioned in such provisions (such third Persons referred to in this Section 8.10 as the "Third Party Beneficiaries") and except for the rights of the Affected Securityholders to receive the applicable consideration following the Effective Time pursuant to the Arrangement (for which purpose the Company hereby confirms that it is acting as agent on behalf of the Affected Securityholders), the Parties intend that this Agreement will not benefit or create any right or cause of action in favour of any Person, other than the Parties and that no Person, other than the Parties, shall be entitled to rely on the provisions of this Agreement in any action, suit, proceeding, hearing or other forum.
- (2) Despite the foregoing, the Parties acknowledge to each of the Third Party Beneficiaries their direct rights against the applicable Party under Section 2.14, Section 4.4, Section 4.12 and Section 8.20, which are intended for the benefit of, and shall be enforceable by, each Third Party Beneficiary, his or her heirs and his or her legal representatives. For the purposes of Section 2.14, Section 4.4 and Section 4.12, the Company confirms that it is acting as agent on behalf of the Third Party Beneficiaries under those sections, and agrees to enforce such provisions on behalf of such Third Party Beneficiaries.

[163] I make two observations about this section. First, the only right that the shareholders had was to receive the consideration if the Transaction closed. They did not have any rights, as third-party beneficiaries, to enforce the agreement or to sue Cineworld for any breach. This is to be contrasted with the third-party beneficiaries who were entitled to assert their rights directly against Cineworld for breach of Sections 2.14, 4.4, 4.12 and 8.20 (none of which are for the protection of the shareholders).²³

²³ Section 2.14 is Incentive Plan Matters; s. 4.4 is Cooperation Regarding Reorganization; s. 4.12 is Insurance and Indemnification; and s. 8.20 is Financing Sources Related Parties.

[164] Second, Cineplex was appointed as the agent for the shareholders only for the purpose of collecting the consideration if the Transaction closed. It was not appointed as agent for the purpose of enforcing their rights against Cineworld if it failed to close. This is to be contrasted with Cineplex's role as agent for the third-party beneficiaries in enforcing their rights under the sections referred to above. If the parties had wanted to appoint Cineplex as the shareholders' agent to enforce their rights on Cineworld's failure to close, they could have done so.

[165] Cineplex submits that because the Transaction was structured as a plan of arrangement, this changes the analysis. It argues that in order to obtain court approval for an arrangement, the company must establish that the transaction is fair and reasonable. That looks at whether the plan has a valid business purpose and a positive value to the corporation: *BCE Inc. v. 1976 Debentureholders*, 2008 SCC 69, [2008] 3 S.C.R. 560, at p. 567. While I agree that this is the test for court approval, it does not change the fact that under the arrangement, the consideration was always payable to the shareholders, not to Cineplex. I do not agree that the structure of the Transaction as a plan of arrangement entitles Cineplex to collect the consideration that would otherwise have been paid to the shareholders.

[166] The parties made submissions about the debate in the U.S. jurisprudence and commentary relating to the case of *Consolidated Edison Inc. v. Northeast Utilities*, 426 F.3d 524 (2d Cir 2005), and whether that caselaw precludes a target company from recovering the consideration payable to its shareholders in a failed merger transaction. It is not for this court to resolve the debate in that jurisdiction.

[167] Cineplex argues that this measure of damages is supported by the U.K. caselaw on the principle of "transferred loss": *Lowick Rose LLP v. Swynson Ltd.*, [2017] UKSC 32. The principle of transferred loss may be invoked where "the known object of a transaction is to benefit a third party or a class of persons to which a third party belongs, and the anticipated effect of a breach of duty will be to cause loss to that third party": *Swynson*, at para. 14.

[168] This principle does not assist Cineplex. It has been narrowly construed and recognized only in cases where the third party suffers loss as the transferee of the property affected by the breach: *Swynson*, at paras. 14, 102. That is not the case here. In any event, there is no basis to apply that principle when the parties expressly defined the rights of third parties in s. 8.10 as set out above.

[169] In my view, the only damages recoverable by Cineplex are the losses sustained by Cineplex, not its shareholders.

Loss of Synergies

[170] Cineworld was a strategic buyer. As Mr. Mooky Greidinger testified, the rationale for the Transaction was to combine the operations of Cineplex and Regal and achieve substantial synergies through that combination. He testified that based on its previous acquisition experience, Cineworld was confident that the synergies could be achieved. He said that "the only thing that

justified – or part of the justification for the price we paid was the synergies that we were estimating that we could do. And this was very important for the deal as one of the basis [*sic*] for the deal.” In this case, there was an advantage because there was already a very big office for Regal in Knoxville, Tennessee.

[171] Prior to entering into the Arrangement Agreement, Cineworld engaged Ernst & Young to prepare a synergies report (the “**EY Report**”). That report estimated \$163.5 million in annualized combination benefits to Cineplex, comprised of cost synergies (\$88 million), revenue synergies (\$72 million) and efficiency synergies (\$3.5 million) that would result from the combination with Cineworld. The cost savings to Cineplex resulted from, among other things, removal of the Cineplex board, headcount rationalizations, and spending reductions on the operational side. The increased revenues to Cineplex included additional fees from film studios to play trailers during pre-show time, additional online booking fees, and increased concession spend at theatres.

[172] Mr. Rosen calculated that the present value of those synergies that were lost to Cineplex when Cineworld terminated the Arrangement Agreement was \$1.2366 billion (before pre-judgment interest). His methodology was as follows:

- he identified the synergies using the EY Report;
- he utilized only those synergies that would have been realized by the corporate entity Cineplex and excluded those that would have been realized by Cineworld or Regal. He said that of the \$176 million in total synergies projected in the EY Report, \$163.5 million was expected to be realized by Cineplex;
- he discounted the expected benefits to account for the delayed realization due to COVID-19; and
- he discounted the future cash flows to a present value as of the date of breach.

[173] Mr. Carlucci did not dispute Mr. Rosen’s methodology or calculations. His criticism was that these synergies only would have been achieved if the two businesses were combined and that they would have accrued to Cineworld as the buyer. He further testified that a discount should apply to account for the probability of Cineplex achieving these synergies.

[174] I consider the lost synergies to be an appropriate measure of damages and I accept Mr. Rosen’s calculations. This is a proper measure of damages because, unlike the consideration payable to shareholders, the lost synergies are Cineplex’s own losses as a result of Cineworld’s termination. Based on the evidence of Mr. Rosen (relying on the EY Report), these are synergies that would have been realized by Cineplex had the Transaction been completed. An award of damages on this basis would therefore put Cineplex in the position that it would have been in if Cineworld had not terminated the Arrangement Agreement and had closed the Transaction.

[175] As noted above, to obtain court approval for a plan of arrangement, a company must establish that the arrangement has a valid business purpose and a positive value to the corporation: *BCE*, at p. 567. In *Re Rapier Gold Inc.*, 2018 BCSC 539, at para. 99, the court considered the anticipated synergies that would be realized by the company as a benefit in approving the plan of

the arrangement. In the case at bar, Mr. Mooky Greidinger's evidence is that the purchase price payable to shareholders was reflective of the expected synergies set out in the EY Report. The synergies were one of the benefits to Cineplex of entering into the plan of arrangement.

[176] Although the ultimate benefit of the synergies would have accrued to Cineworld as the shareholder of Cineplex (as with any corporate benefit, which ultimately accrues to the shareholders of the corporation), it does not change the fact that these synergies would have been realized by the corporate entity, Cineplex.

[177] Mr. Rosen based his calculations on the analysis of Cineworld's own advisors in the EY Report. He focused only on the synergies that would have been realized by Cineplex, not by Cineworld or Regal – \$163.5 million out of \$176 million. As he explained in his report, this “included the removal of redundancies, consolidation of Cineplex's functions into Cineworld's existing operations, reduction in costs due to economies of scale, and increase in revenue from the introduction of new business initiatives. The remaining \$13 million was expected to be realized by Regal as it entailed revenue synergies from the introduction of Cineplex's business practices at the Regal theatres.” Mr. Rosen excluded the \$13 million from his calculation.

[178] Mr. Rosen chose the most probable outcome with respect to the synergies, noting that Cineworld had been successful in achieving expected synergies in the Regal transaction. He also applied a discount to take into account the impact of COVID-19 on the realization of synergies.

[179] Cineworld argued in its oral submissions that I cannot take into account the expected synergies without also accounting for the additional debt that the combined entity would have had after closing. Cineworld refers to the Third Amendment to Credit Agreement dated February 13, 2020 that it says would have permitted the banks to place over \$2 billion of Cineworld debt at the Cineplex level and Mr. Israel Greidinger's evidence that Cineworld planned to do so after closing. This evidence was vague and uncertain. It is not clear to me what the timing of these post-closing plans were nor is there any evidence of the financial impact that this would have had on Cineplex (such as the amount of the debt service cost that would have been borne by Cineplex as opposed to the other Cineworld borrowers under the credit facility). The evidence is insufficient for me to apply any discount to the amount of the lost synergies that Mr. Rosen calculated.

[180] Cineworld also submits that the synergies should be discounted to reflect the uncertainty of Cineworld obtaining ICA Approval. I am not prepared to do so. Mr. Mooky Greidinger's own testimony is that by June, Cineworld was “very close” with the government. The ICA experts both testified that there was sufficient time for Cineworld to have obtained ICA Approval by the outside closing date. The documentary evidence indicates that the Agencies were working closely and cooperatively with Cineworld to provide ICA Approval. They were available and responsive to Cineworld throughout the process. They indicated they wanted to get it done as quickly as possible.

[181] Once the pandemic was declared, the Agencies were amenable to and working with Cineworld on undertakings that would reflect the economic and operational uncertainties of

COVID-19. On June 2 and 10, the Agencies invited Cineworld to submit signed undertakings for the Ministers' approval. I am satisfied, on a balance of probabilities, that ICA Approval would have been forthcoming if Cineworld had not withdrawn its application on June 12. In the alternative, Cineworld's actions deprived Cineplex of the very real chance to see whether ICA Approval could be obtained prior to the outside closing date and on the evidence before me, there was a very high percentage likelihood that ICA Approval would have been obtained: *Berry v. Pulley*, 2015 ONCA 449, [2015] O.J. No. 3298, at paras. 70-72. There is no reason to discount Mr. Rosen's calculations for lost synergies on this basis.

[182] I award damages to Cineplex of \$1.2366 billion on account of the lost synergies. In addition, I award Cineplex its transaction costs of \$5.5 million. Both amounts are exclusive of pre-judgment interest.²⁴

CINEWORLD'S COUNTERCLAIM

[183] Cineworld has not established any breach by Cineplex. Its counterclaim for its transaction costs of £32 million is dismissed. In any event, I find that the largest component of that amount is the foreign exchange fees of £21.6 million that Cineworld agreed to assume for Goldman Sachs to participate in the RCF increase. That cost relates to Cineworld's operational financing, not to the Transaction. Further, Mr. Rosen raised numerous issues with the professional fees claimed by Cineworld that were not addressed by its witnesses. He calculated Cineworld's transaction costs to be £8.4 million. If I had awarded damages on the counterclaim, I would have fixed the amount at £8.4 million.²⁵

SUMMARY AND JUDGMENT

[184] The parties have put before me an extensive record of witness testimony, contemporaneous documents, and expert evidence. While it is not possible for me to review all of the evidence in these Reasons, I have considered the record in its entirety. Based on my review of the record, a clear picture of what transpired has emerged.

[185] The parties entered into the Arrangement Agreement. Cineworld agreed that it would not be able to exit the Transaction if a pandemic occurred. It did not negotiate a break fee to allow it to walk away from the Transaction.

[186] The pandemic was declared in March. By April 24, Cineworld no longer intended to close the Transaction at \$34 per share. It knew that its exit strategy was through the control of the ICA

²⁴ Cineplex asked for punitive damages in its written submissions but did not pursue it in oral argument. I see no basis to award punitive damages on top of this award. Cineplex has not persuaded me that measures 4 and 5 (that Mr. Rosen said "could" be awarded with measure 3 although not with measures 1 and 2) should be awarded in addition to lost synergies and transaction costs. Further, since I have accepted measure 3 as an appropriate measure of damages, there is no need to consider measures 2 or 7.

²⁵ He noted that only £266,696 were incurred by the plaintiffs and the rest by other entities in the Cineworld group. I would not reduce the transaction costs on that basis as the costs were incurred by the Cineworld group as a whole.

Approval process and the \$725M Debt Condition. It expected and hoped that Cineplex would not be able to meet that condition before ICA Approval was granted.

[187] Cineworld continued the ICA Approval process. When it appeared in June that ICA Approval was imminent and the closing date was approaching, Cineworld saw that Cineplex was still under the \$725M Debt Condition. Cineworld could not refuse to close on this basis nor could it walk away on account of the pandemic since that was excluded from the definition of Company Material Adverse Effect.

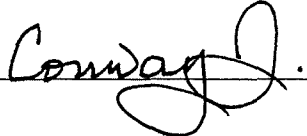
[188] Cineworld took a different course. It made wide-ranging allegations that Cineplex breached various covenants in the Arrangement Agreement. Although it knew of the payment deferrals by April, it waited until June to treat these as a default and took the position that the defaults were incurable. It then terminated the Arrangement Agreement on June 12 and pulled its application for ICA Approval. It precluded Cineplex from seeking specific performance.

[189] I have reviewed the alleged breaches carefully and have found that Cineplex did not breach the covenants in the Arrangement Agreement. It did not fail to comply with the Operating Covenant. It did not breach any of the other covenants during the Interim Period. Cineworld had no basis for terminating the Arrangement Agreement. Its June 12 notice was a repudiation of the agreement.

[190] Cineplex has proven its damages for Cineworld's breach of contract in an amount equal to the present value of the synergies that Cineplex would have realized had the Transaction closed. It is also entitled to recover its transaction costs.

[191] I grant judgment to Cineplex and award damages for \$1.2366 billion on account of lost synergies and \$5.5 million on account of transaction costs, both exclusive of pre-judgment interest.

[192] If the parties are unable to agree on costs, I will receive written submissions (no longer than ten pages double spaced, exclusive of bill of costs). Cineplex's costs submissions shall be delivered within 21 days and Cineworld's costs submissions within 21 days thereafter. Cineplex may file reply submissions of not more than five pages within seven days thereafter.



Conway J.

Released: December 14, 2021

CITATION: Cineplex v. Cineworld, 2021 ONSC 8016
COURT FILE NO.: CV-20-00643387-00CL
DATE: 20211214

ONTARIO
SUPERIOR COURT OF JUSTICE
(COMMERCIAL LIST)

CINEPLEX INC.

Plaintiff
Defendant to the Counterclaim

– and –

CINEWORLD GROUP PLC and 1232743 B.C. LTD.

Defendants
Plaintiffs by Counterclaim

REASONS FOR JUDGMENT

Conway J.

Released: December 14, 2021