

CANADA / JUDGMENT

Francisco Gold Corp. (Re)

2002 BCSC 1054

COURT

Supreme Court of British Columbia

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2002BCSC1054

Citation: Francisco Gold Corp. (Re)

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2002 BCSC 1054Docket: L021464
Registry: Vancouver
IN THE SUPREME COURT OF BRITISH COLUMBIA
IN THE MATTER OF SECTION 252 OF THE BRITISH COLUMBIA COMPANY ACT,
R.S.B.C. 1996, CHAPTER 62, AS AMENDEDAND: IN THE MATTER OF AN ARRANGEMENT BETWEEN FRANCISCO GOLD CORP.
AND ITS SHAREHOLDERS

REASONS FOR JUDGMENT

OF THE

HONOURABLE MADAM JUSTICE H. HOLMES

Counsel for Francisco Gold Corp.:

Michael P. Carroll, Q.C.

K. Michael Stephens

S. Cramer

Counsel for John Halagan:

Rose-Mary Liu Basham, Q.C.

Karen Thompson

Counsel for Randy Reifel:

D. Burnett

Counsel for Glamis Gold Ltd.:

Michael Tourigny

Date and Place of Hearing:

June 20-21, 2002

Vancouver, BC

INTRODUCTION

- [1] The petitioner Francisco Gold Corp. seeks the final approval in a "fairness hearing" under s.252 of the B.C. Company Act of a plan of arrangement with Glamis Gold Ltd.
- [2] The respondent John Halagan, a minority shareholder and former director of Francisco, opposes the Arrangement and seeks an adjournment of the hearing of the petition. He also seeks various orders for cross examination of Francisco's directors and others, production of documents, and the appointment of independent counsel to investigate the fairness of the Arrangement.
- [3] Counsel agreed that the question whether the hearing of the petition should be adjourned necessarily involves consideration of the bases upon which Mr. Halagan objects to approval of the Arrangement. By agreement, the adjournment application and the application seeking final approval of the Arrangement under s.252 were therefore argued together.

BACKGROUND

The Parties and their Relationship

- [4] Francisco is a B.C. company trading on the TSX Venture Exchange (previously the Vancouver Stock Exchange). It is engaged in gold mining exploration and development in Mexico and Central America.
- [5] Glamis is a B.C. company trading on the Toronto and New York stock exchanges. Glamis is also engaged in the exploration, mining, and extraction of precious metals.
- [6] On April 30, 2002, Francisco and Glamis (together with a subsidiary of Francisco called Chesapeake Gold Ltd.) entered into an agreement to effect a business combination between these companies. Chesapeake is currently a shell company without assets, essentially waited to be activated by the transactions involved in the Arrangement.
- [7] Mr. Halagan was a director of Francisco until 1993. Since then, his role has been as a minority shareholder. He owns 375,000 escrow shares, comprising approximately 2% of the total outstanding shares of Francisco. By their nature, the shares cannot be traded unless they are freed from escrow.

- [8] The beneficial ownership of these escrow shares was the subject of a protracted dispute between Mr. Halagan and Randy Reifel, Francisco's president and director. After a lengthy and hard-fought trial over 34 days between November 1997 and July 1998, Satanove J. held in October 1998 that the escrow shares in Mr. Halagan's name were beneficially his and not, as asserted by Mr. Reifel, held for whomever Francisco's board of directors may identify as suitable: *Halagan v. Reifel*, [1998] B.C.J. No. 2301 (Q.L.)(S.C.). The Court of Appeal upheld that decision: (2001), 90 B.C.L.R. (3d) 146 (C.A.). Leave to appeal to the Supreme Court of Canada was denied on June 6, 2002: [2001] S.C.C.A. No. 469 (Q.L.).
- [9] The shares were also the subject of regulatory proceedings, which are still under appeal. After Satanove J.'s decision that he owned the shares, Mr. Halagan applied to the Vancouver Stock Exchange for their release from escrow. Francisco opposed the application. The VSE authorized the release of Mr. Halagan's shares but the B.C. Securities Commission reversed that decision on appeal. The key issues before the Commission were whether Francisco had achieved success in Venezuela and, if so, whether Mr. Halagan was entitled to rely solely on Mr Reifel's contribution to that success as a basis for the release of his own shares from escrow. Mr. Halagan has been given leave to appeal the Commission's decision to the Court of Appeal.

The Plan of Arrangement

- [10] The Arrangement contemplates a share exchange transaction valued in the range of \$350 million.
- [11] Under the Arrangement Glamis will acquire all of the outstanding common shares of Francisco, and Francisco will become a wholly-owned subsidiary of Glamis.
- [12] Francisco will also transfer to Chesapeake the shares of other wholly or partially-owned companies (which own, among other things, Francisco's exploration properties and assets in Nicaragua) together with a 2% net smelter return royalty on certain mineral properties located in Guatemala, and \$1.50 from Francisco's treasury for each issued share of Chesapeake. The net effect of these transactions is the transfer from Francisco to Chesapeake of a significant portion of Francisco's assets and \$25 million in cash.
- [13] The Arrangement provides that Francisco shareholders will receive for each Francisco share:
- (a) 1.55 common shares of Glamis
 - (b) 1 Chesapeake share and
 - (c) 1 "Glamis Right".

Analagous rights are provided for holders of Francisco options.

- [14] The "Glamis Right" was created to address the uncertain situation regarding Mr. Halagan's 375,000 escrow shares. It provides essentially that if Mr. Halagan is successful in his appeal to the Court of Appeal and the VSE decision is reinstated, he will be entitled to the release of the escrow shares and will be treated under the Arrangement in the same fashion as the other Francisco shareholders. If, on the other hand, Mr. Halagan is unsuccessful in his appeal, Francisco will apply to the Securities Commission to cancel the escrow shares. If the shares are cancelled, then by a formula more complicated than requires repetition here each Francisco shareholder will be entitled to an additional pro rata portion of a Glamis share.

Communication of the Arrangement

- [15] A press release announced the Arrangement in early March 2002. Articles appeared in The Vancouver Sun, The National Post, and The Globe and Mail.
- [16] On May 10, 2002, Francisco obtained a without notice order providing for the mailing to Francisco shareholders of an information circular concerning the Arrangement and allowing Francisco to hold an extraordinary general meeting of shareholders on June 12, 2002 to consider and vote on the Arrangement.
- [17] The Information Circular was mailed to Francisco shareholders, including Mr. Halagan, on May 15, 2002. On June 7, 2002, Mr. Halagan's counsel wrote expressing Mr. Halagan's opposition to the Arrangement. Ms. Basham explained that Mr. Halagan, a man of 85 years of age who lives in Nevada, U.S.A., did not become aware of the Arrangement until June 5, 2002.

Shareholder Approval

- [18] At the June 12, 2002, extraordinary general meeting, Francisco shareholders voted 94.9% in favour of the Arrangement. In total, 7,745,298 shares were voted at the meeting, representing 64.05% of the 16,585,425 outstanding shares. Of the 388,400 shares voted against approval, 375,000 represented Mr. Halagan's escrow shares. Mr. Halagan is thus the principal opponent to the Arrangement.
- [19] It is to be noted that Francisco shares are fairly widely-held. Francisco's directors and other officers together own approximately 14% of the outstanding shares.

Other Endorsement

- [20] Macquarie North America Ltd., a Canadian investment banking firm, provided an opinion dated April 30, 2002 that the Arrangement is fair, from a financial point of view, to the security holders of Francisco.

[21] The market has reacted very positively to the proposed Arrangement, showing an increase in trading price from \$8.50 to \$12.80 with the public announcement of the Arrangement on March 6, 2002. Since the announcement, Francisco shares have traded as high as \$24.61. The most recent trading date in evidence was June 14, 2002, when the price was \$21.40.

THE POSITIONS OF THE PARTIES

[22] Mr. Halagan's objections to the Arrangement and the process by which it was achieved and disclosed to Francisco's shareholders are extensive but can in my view be summarized as follows. He submits that:

- (a) numerous instances of inadequate disclosure to Francisco's shareholders cast the shareholders' approval of the Arrangement into serious doubt and call the fairness of the Arrangement into question
- (b) key among these is the inadequate disclosure of Francisco's improper payment of Mr. Reifel's personal legal fees in respect of the litigation with Mr. Halagan
- (c) Mr. Reifel's undisclosed purchase of Francisco shares in a 1993 private placement has a potential effect on the value of Francisco's assets and therefore in turn on the reliability of the Francisco-Glamis share ratio which constitutes a significant component of the Arrangement
- (d) the negotiation of the Arrangement and its presentation to Francisco shareholders failed to comply with numerous statutory and regulatory requirements concerned with conflict of interest and disclosure of the personal interests of directors and officers; these violations all affect the fairness of the Arrangement, and some of them are fatal to the Arrangement, because by s. 252(3) of the Act, approval is given only when "every requirement of this Act related to the proposed . . . arrangement has been complied with", and
- (e) the hearing should be adjourned to permit the further exploration of these many issues before the fairness of the Arrangement is determined.

[23] Francisco says that Mr. Halagan's assertion that the background to and the fairness of the Arrangement require further investigation is nothing but a proposal for a fishing expedition into irrelevant and undefined complaints. Francisco contends that Mr. Halagan's position, insofar as it seeks to delay court approval of the Arrangement, is fundamentally a bad faith effort to lever a deal by which either Francisco or Glamis will agree to buy out his minority, non-trading share position.

THE LEGAL FRAMEWORK

Section 252 of the B.C. Company Act

[24] Francisco seeks approval of the Arrangement under s.252 of the Act, which provides:

252 (1) Subject to subsections (6) and (7), if a compromise or arrangement is proposed between . . . a company and its members or any class of them, then, despite any other provision of this Act, if a majority in number representing . . . 3/4 of the votes of those members or that class of members, who are present and vote either in person or by proxy at a meeting convened in accordance with an order of the court under subsection (2), agree to a compromise or arrangement, the compromise or arrangement, if approved by the court and accepted for filing by the registrar, is binding on every creditor or member, as the case may be, and on the company.

...

- (3) No compromise or arrangement under this section takes effect until every requirement of this Act relating to the proposed compromise or arrangement has been complied with and a certified copy of the court order has been accepted for filing by the registrar.

[25] As Neilson J. noted in *Pacifica Papers Inc. (Re)* (2001), 17 B.L.R. (3d) 92 at para. 36; 2001 BCSC 701 ("Pacifica No. 1"); leave to appeal to B.C.C.A. refused (2001), 90 B.C.L.R. (3d) 94; 2001 BCCA 363, in relation to analogous provisions in the Canada Business Corporations Act, the approval of a plan of arrangement is a three step process:

The application for an interim order . . . for directions related to calling a shareholders' meeting is characteristically the first of three steps required to approve an arrangement under the Act. It usually proceeds *ex parte*, due to the administrative burden of notifying all shareholders of the application. The second step is the meeting of shareholders, where the arrangement is debated and must be approved by a majority of two-thirds [75%, in the case of the B.C. Company Act] to proceed further. The third step is a further application to the Court under the Act for a final order approving the arrangement. This is referred to as the fairness hearing, and all interested parties receive notice of it and may appear to contest the final order on the basis of its substantive fairness.

[26] The first and second steps took effect in this court's order pursuant to s.252(2) for the calling of a meeting of security holders, and the ensuing June 12, 2002 meeting mentioned above. No issue is taken in relation to either of those steps except in that Mr. Halogan objects to the adequacy of the disclosure provided to the shareholders in advance of the meeting.

[27] The third step is Francisco's present application seeking final approval of the Arrangement on the ground that it is fair and reasonable to its shareholders.

The Test for Final Approval Under s. 252

[28] In the leading case of *Gold Texas Resources Ltd. (Re)*, [1989] B.C.J. No. 167 (Q.L.)(S.C.), Chief Justice McLachlin (then Chief Justice of this Court) set out the test to be applied on an application for court approval of an arrangement:

Before the Court sanctions a scheme or arrangement, four requirements must be met: Palmer's Company Law 24th ed., p. 79:

1. The statutory provisions must have been complied with;
2. The class must have been fairly represented;
3. The arrangement must be such as a man of business would reasonably approve; and
4. The arrangement must be compatible with the section under [which] the arrangement is to be approved.

[29] I note that no issue is taken here in relation to the second requirement that the majority vote be bona fide.

[30] In making the determination whether the arrangement is one that a business person would reasonably approve, the court will pay deference to the business judgment of the majority: *Re Gold Texas Resources Ltd.*, supra; *Pacifica Papers Inc. (Re)* (2001), 92 B.C.L.R. (3d) 158, at paras. 23, 84-85; 2001 BCSC 1069 ("Pacifica No. 2"); *Trizec Corp. (Re)* (1994), 20 B.L.R. (2d) 202 at para. 31 (Alta. Q.B.).

[31] In *Re St. Lawrence & Hudson Railway Co.*, [1998] O.J. No. 3934 at para. 27 (Q.L.)(Gen. Div.), Blair J. stated:

What better litmus test . . . for assessing whether in the circumstances of a given arrangement "an intelligent and honest business person, as a member of the class concerned and acting in his or her own interest, might reasonably approve of the plan", than the votes of those whose interests are actually at stake? The votes of security holders at meetings to consider a proposed Plan are not conclusive, but a substantial vote in favour of the proposed plan of arrangement by the security holders affected is an important factor in the court's considerations. The "business judgment" of the security holders in determining their own interests is to be given great weight

(See also: *Canadian Pacific Ltd. (Re)* (1996), 30 O.R. (3d) 110 at 132 (Gen. Div.)).

[32] Ms. Basham for Mr. Halagan properly observes that the persuasive power of a shareholder vote of approval is seriously undermined if there is inadequate disclosure regarding the proposed arrangement. I will address in detail later in these reasons the areas in which she submits the disclosure to the shareholders to have been inadequate here.

[33] It is not the task of the court on a fairness hearing to enter into a searching enquiry as to whether the proposed arrangement is perfect; it need only be fair to the shareholders to be approved. As the Ontario Court of Appeal observed in *Maple Leaf Foods Inc. v. Schneider Corp.* (1998), 42 O.R. (3d) 177 at 192 (C.A.):

. . . the court must be satisfied that the directors have acted reasonably and fairly. The court looks to see that the directors made a reasonable decision not a perfect decision

[emphasis in original]

- [34] McLachlin C.J. in *Gold Texas Resources Ltd.*, supra, noted similarly that the court will not itself judge upon the commercial merits of a plan of arrangement.

DISCUSSION

- [35] I turn now to consider in turn each of Mr. Halagan's areas of objection to the Arrangement, as I have summarized them above.

(a) THE ADEQUACY OF DISCLOSURE

- [36] Mr. Halagan argues that the disclosure to shareholders in the Information Circular was inadequate to enable them to make an informed decision whether or not to support the Arrangement. The areas of inadequate disclosure he asserts include: the interests of management (particularly Mr. Reifel) in the Arrangement (including by way of severance pay, appointment to the Glamis board of directors with remuneration, Mr. Reifel's management of Chesapeake for a fee, and the immediate release to Mr. Reifel of escrow shares held in the name of Beggar Pacific) and the value of those various benefits and its impact on the consideration offered to Francisco shareholders under the Arrangement; details of the negotiations leading to the Arrangement; an explanation of Francisco's payment of Mr. Reifel's legal fees; and the fact and effect of Mr. Reifel's undisclosed participation in a private placement of Francisco shares in 1993.
- [37] I will address the adequacy of disclosure in the latter two of these areas (concerning Mr. Reifel's legal fees and the 1993 private placement) later in these reasons in connection with other or more specific bases on which Mr. Halagan opposes the approval of the Arrangement and asserts a lack of fairness requiring further investigation.
- [38] I note also that in relation to the 1993 private placement Mr. Halagan asserts a complete lack of disclosure, whereas in the other areas he argues that the information disclosed is inadequate for the shareholders' assessment of the Arrangement. For example, although the Information Circular clearly sets out a schedule of persons to receive severance payments and the amounts of the payments, Mr. Halagan objects that the underlying reasoning behind each of these does not appear. In further example, although the Information Circular sets out the post-Arrangement directors and officers (including Reifel) of Chesapeake, it does not disclose their remuneration.
- [39] A circular is deficient when it contains an untrue statement of a material fact or omits a statement of material fact in a manner which is misleading. A fact is material if there is a substantial likelihood that a reasonable shareholder would consider it important in deciding how to vote: *Pacifica No. 1*, at paras. 40-46. As Blair J. noted in *First Marathon Inc.*, [1999] O.J. No. 2805 at para. 17 (Q.L.) (S.C.J.), an information circular is not required to anticipate and answer every conceivable inquiry that may arise:

The question is not whether the Information Circular contains information answering every conceivable query, and follow-up query, that an inquisitive minded shareholder (or shareholder's advisor) can pose. The requirement is that the substance of the pertinent matter be set out "in

sufficient detail to permit shareholders to form a reasoned judgement concerning the matter": OBCA Regulation, s. 30, item 31. This standard, it seems to me, is not dissimilar to the frequent declaration that shareholders are entitled to "full, fair and plain disclosure": see, for example, Imperial Trust Company, *supra*, at p. 393.

[40] Blair J. in *First Marathon* at para. 18 noted the difficulty of striking the right balance between over- and under-disclosure, and cautioned against quick judicial condemnation:

Those preparing Information Circulars in complex transactions have a difficult task. They must weigh an often uneasy balance between providing insufficient detail (which does not convey the substance and the material information to shareholders) and "[burying] the shareholder in an avalanche of trivial information", which creates its own kind of risks for intelligent and informed decision making: [citation]. The exercise requires business skill, expertise and acumen. Reasonable people can differ on what may be required. The courts should not be quick to interfere with such decisions, unless it is plain that there are good reasons to be concerned about the adequacy of the disclosure

[41] Having reviewed the impugned areas of the Information Circular, I am not satisfied that, in Blair J.'s words, "there are good reasons to be concerned about the adequacy of the disclosure". In my view, the Information Circular adequately states the material facts in each area, relating them to the effect of the Arrangement and any particular advantage to members of management. Potential conflicts of interest are conspicuously flagged by their simple statement. I do not consider it necessary for the disclosure material to enter into a discussion of their implications and ramifications.

[42] I note in this regard that an information circular need not disclose in minute detail the differences between parties: *Pacifica No. 1*, at paras. 86-88; *Smith v. First Merchant Equities Inc.* (1988), 50 D.L.R. (4th) 369 (Sask Q.B.). As stated by Neilson J. in *Pacifica No. 1* at para. 86 "management's obligation is to disclose material facts, not opposing views and arguments". As Mr. Carroll noted in his submissions, some of Mr. Halagan's allegations against Mr. Reifel which he says should be extensively disclosed could well turn out to be actionable.

[43] A meeting was convened for the express purpose of considering and voting upon the Arrangement. There is no evidence to suggest that any shareholder, other than Mr. Halagan in connection with the present petition, has made any inquiry, let alone raised any concern, about any of the areas of potential conflict, or has asked for further detail as to any of the matters disclosed. I cannot accept Mr. Halagan's submission that disclosure was made in only its barest form but was insufficient for the shareholders' informed consideration of the Arrangement.

(b) Payment of Mr. Reifel's Legal Fees

[44] Mr. Halagan contends that the Information Circular ought to have disclosed to shareholders not only, as it did, the fact that Francisco paid Mr. Reifel's legal fees in respect of his litigation with Mr. Halagan but also the basis upon which it did so. He says that Francisco's

payment of Mr. Reifel's personal legal fees of approximately \$850,000 cries out for explanation, without which Francisco's shareholders were not in a position to make an informed decision as to whether to support the Arrangement. He describes Francisco's payment of Mr. Reifel's legal fees as "improper".

- [45] Disclosure as to this matter appears as Note 7 to the financial statements under the heading "Legal Matters - Escrow Shares" at p. F-13 of the Information Circular. The Note explains that "[t]he ownership of 375,000 escrow shares is in dispute", and that litigation continues "between the president on behalf of the Company and a former director of the Company". After a brief history of the legal proceedings between Halagan and Reifel and those in relation to the application for release of the shares (which is now under appeal to the Court of Appeal), the Information Circular states that:

The Company has agreed to pay the costs of the litigation and the escrow release application defence as it has a direct interest in the outcome of these matters. The Company has incurred legal costs to September 30, 2001 of approximately \$850,000 relating to these disputes.

- [46] Although the litigation was between Mr. Halagan and Mr. Reifel personally, it is clear that the outcome directly affected the company. At the outset of her judgment, Satanove J. stated the defendant Mr. Reifel's position as follows at paras. 2 and 4:

The defendant seeks a Declaration that the plaintiff [Mr. Halagan] has no beneficial interest in the Escrow Shares and that the defendant is authorized to transfer the Escrow Shares to anyone whom the board of directors of [Francisco] identifies as suitable.

...

The defendant says . . . [he] had paid for the Escrow Shares and the plaintiff was merely holding them as trustee until the board of directors of [Francisco] identified a suitable third party to whom they wished to transfer the Escrow Shares as an incentive to join the company.

- [47] At para. 62 Satanove J. noted that:

Providing incentive is a recognized purpose for the existence of Escrow Shares. Escrow Shares are described as "performance shares" because by their very nature they are intended to act as an incentive to the holders thereof to contribute to the success of the company.

- [48] The Information Circular clearly discloses the payment of \$850,000 in legal fees for Francisco's president in relation to litigation between him and "a former director", and explains that the company has a "direct interest in the outcome" of the litigation. The nature of Francisco's interest in the ownership and control of the shares is obvious, as inherent in the well-known use of escrow shares as a potential incentive to suitably capable and experienced individuals to work for a company's success. In my view the explanation in the Information Circular of the reason for the payment of Reifel's legal fees is entirely sufficient for the purposes of the shareholders' decision whether or not to approve the Arrangement.

- [49] I note also that there is no evidence that Mr. Halagan or any other shareholder has asked for additional detail or explanation of the payment. Mr. Halagan in his affidavit simply expresses his disapproval of the payment, a view which is hardly surprising given the history of litigation between him and Mr. Reifel and the company.
- [50] Mr. Halagan has to date made no demands on Francisco to initiate legal proceedings to recover the legal expenses paid on behalf of Mr. Reifel, and has taken no steps toward derivative proceedings under s. 201 of the Act in relation to those expenses.
- [51] I find that neither the fact of Francisco's payment of Mr. Reifel's legal expenses, nor the adequacy of disclosure of that fact in the Information Circular, is a matter which, if further investigated as proposed by Mr. Halagan, would assist the court's determination of the fairness of the present Arrangement.
- (c) The 1993 Private Placement
- [52] Mr. Halagan raises concerns about what he says was Mr. Reifel's undisclosed acquisition of approximately 700,000 Francisco shares and warrants through a private placement in 1993. He relates these concerns to several of the issues implicated in the fairness hearing, as well as to his application for an adjournment of the hearing.
- [53] First, he argues that Mr. Reifel's undisclosed participation in the 1993 private placement has a likely material effect on the current value of Francisco shares, and therefore ought to have been disclosed in the Information Circular. No information regarding the 1993 private placement appears in the Information Circular. Second, he argues that the likely effect of the private placement on Francisco's current share value also affects the adequacy of the consideration offered for Francisco shares under the Arrangement and therefore the very fairness of the Arrangement itself. Third, he argues that the Board's failures to investigate and disclose Reifel's conflict of interest in relation to the 1993 private placement and to recover unlawfully received profits from him should have been disclosed to shareholders as material background information relating to the character and diligence of those putting forward the Arrangement and participating under it. Finally, Mr. Halagan seeks the adjournment of the fairness hearing in large part on the basis of his asserted need for further investigation of these various aspects of Mr. Reifel's participation in and possible profit from the private placement, of the conduct of other board members who knew or ought to have known about his participation, and of the effect of his participation and the current value of Francisco shares and therefore on the fairness of the Arrangement.
- [54] As to the effect of Mr. Reifel's participation in the 1993 private placement upon Francisco's current share value, Mr. Halagan's reasoning proceeds as follows. He asserts that Mr. Reifel's failure, as a key insider of Francisco, to disclose his interest in the placees subscribing to Francisco shares, put him in breach of his fiduciary and director's duty to Francisco as well as various regulatory requirements applicable to the private placement. Mr. Halagan then reasons that Mr. Reifel is liable to account to Francisco for any profit he has made as a result of the private placement, by virtue of the breach of his fiduciary duty to Francisco and as a

result of ss. 120 and 121 of the Act. He argues that an accounting to Francisco of Reifel's profit on the private placement shares would necessarily increase the company's assets. An increase to Francisco's asset base would in turn logically increase the trading price of its shares. Mr. Halagan reasons that since the Arrangement includes a share-exchange ratio based on market prices for Francisco and Glamis shares respectively, but without reflecting the increase to the value of Francisco shares which could be expected to flow from an accounting for Reifel's profits from the private placement, it is therefore likely unfair to the Francisco shareholders.

[55] Mr. Halagan relies on the principles expressed in *Fraser River Helicopters Inc. v. Pemberton Helicopter Services Ltd.*, [1994] B.C.J. No. 1229 (Q.L.)(S.C.) and *MacMillan Bloedel Ltd. v. Binstead* (1983), 22 B.L.R. 255 (B.C.S.C.), and also on ss. 120 and 121 of the Act. Those provisions read as follows:

120(1) Every director of a company who, in any way, directly or indirectly, is interested in a proposed contract or transaction with the company must disclose the nature and extent of the director's interest at a meeting of the directors.

...

121(1) Every director referred to in section 120(1) must account to the company for any profit made as a consequence of the company entering into or performing the proposed contract or transaction, unless

- (a) he or she discloses his or her interest as required by section 120,
 - (b) after his or her disclosure the proposed contract or transaction is approved by the directors, and
 - (c) he or she abstains from voting on the approval of the proposed contract or transaction
- or unless
- (d) the contract or transaction was reasonable and fair to the company at the time it was entered into, and
 - (e) after full disclosure of the nature and extent of his or her interest, it is approved by special resolution.

[56] Mr. Carroll argues for Francisco that any profit Mr. Reifel may have enjoyed in respect of shares taken in the 1993 private placement is outside the contemplation of the common law duty to account and the duty expressed in s. 121 of the Act. He reasons that if Mr. Reifel took an undisclosed interest in the private placement in breach of regulatory requirements and profited from the appreciation of the shares' value, his profit was nonetheless not an opportunity which Francisco could otherwise have enjoyed. A private placement by its nature involves a company issuing shares to placees (or purchasers) in order to raise new capital, \$250,000 in new funds here. Mr. Carroll speaks of the absurdity of objecting to the

loss to Francisco of a corporate opportunity consisting in the investment of money in Francisco in return for Francisco shares.

- [57] The difficulty with this submission is that it does not address the situation where, for example, a company may issue shares to an undisclosed insider in a private placement at an artificially low price, and the insider-subscriber realizes a substantial profit on re-sale of the shares. The company's lost opportunity is not the opportunity to invest as subscriber but rather the opportunity to have issued the shares at a higher price. Such a situation is unlikely to occur, given the requirements of Exchange approval of the terms, including price, of the private placement. However, in my view it serves to demonstrate the potential for a breach of fiduciary duty and the appropriate application of s. 121(1) of the Act in the context of a private placement in which the company would not, logically, participate as subscriber.
- [58] Nonetheless, I cannot accept Mr. Halagan's submissions in this area. In my view, the details and implications of Mr. Reifel's participation in the 1993 private placement are too remote, in time and causal connection, from the issues in the fairness hearing to be of assistance in the determination of the fairness of the Arrangement. At best, Francisco may have a cause of action against Mr. Reifel for the recovery of profits he may have enjoyed in respect of the private placement shares. Assuming, and there is no evidence of this, a sale of all Mr. Reifel's private placement shares at the height of the market (which I note, ironically, followed after the public announcement of the Arrangement), the profit in question would amount to approximately 5% of the value of the Arrangement to Francisco shareholders (or 10% if one also assumes that Mr. Reifel exercised the private placement warrants and realized the maximum available profit on the resulting shares too). One seriously doubts that a shareholder would reject the present Arrangement in the hope of improving the consideration for his or her shares by at most 5% (or even 10%) as a result of proposed litigation with the company's key insider in relation to events some nine years earlier.
- [59] Mr. Halagan's reasoning essentially treats a breach of Mr. Reifel's duty to Francisco or a violation of ss. 120 and 121 as effecting an automatic increase to the asset column of Francisco's balance sheet, and ultimately to the market price of Francisco's shares. It is to be noted, however, that proof of Mr. Halagan's allegations of impropriety and resulting profit would entail considerable uncertainty and cost to the company. Recovery from Mr. Reifel may also be an issue. Finally, negative market reaction to the simple fact of Francisco suing its key insider for acts amounting to failure in his duties to the company may well counteract any increase in share value effected by the line of reasoning Mr. Halagan proposes. As Mr. Burnett bluntly put the matter, Mr. Halagan's asking questions about the propriety of the private placement is a long leap from adding to Francisco's asset base and share value.

- [60] I conclude that even assuming the facts necessary to establish a breach of Mr. Reifel's duties to Francisco arising from common law or statute, and assuming the maximum profit conceivable on those facts, the resulting effect on the fairness of the Arrangement is not, in all the circumstances, material.
- [61] I note also that Mr. Halagan has known since the trial before Satanove J. in 1997 and 1998 of Mr. Reifel's participation in the 1993 private placement and has taken no steps calling for an accounting of any profits to Francisco. In my view this application to consider the fairness of an arrangement conceived and concluded years after the private placement is not the appropriate tool for the historical dig he now suggests.
- (d) COMPLIANCE WITH STATUTORY REQUIREMENTS
- [62] Mr. Halagan submits that the conflicts arising from benefits to Mr. Reifel under the Arrangement required each of the following:
- (i) that the conflicts be disclosed to the shareholders in accordance with s. 253(1) of the Act
 - (ii) that Mr. Reifel abstain from further negotiating or approving the Arrangement
 - (iii) that the directors appoint an independent committee of directors to safeguard against the potential unfair advantage to Mr. Reifel as an interested party, and
 - (iv) that, as a "related transaction" within the meaning of OSC Rule 61-501, the Arrangement be subject to related party disclosure and an independent valuation as required by the Ontario Rule.
- (i) Alleged Breach of Company Act s. 253(1)(a)
- [63] I have already addressed and rejected Mr. Halagan's contention that the disclosure in the Information Circular of material matters, including potential conflicts of interest or benefits to Mr. Reifel and other directors, was inadequate to permit shareholders to reach an informed decision whether or not to approve the Arrangement. Mr. Halagan's objections to the adequacy of disclosure also relate to his submission that the lack of compliance with various statutory provisions is fatal to the approval of the Arrangement under s. 252 of the Act.
- [64] Section 253(1)(a) of the Act requires that:
- (1) If a meeting [of shareholders] is convened under section 252, the company must include in any notice of the meeting
 - (a) that is sent to a creditor or member of a company, a statement, which may be included in the information circular of a reporting company, explaining the effect of the compromise or arrangement and in particular stating
 - (i) any material interest of every director and officer, whether as director, officer, member or creditor of the company, or otherwise, and

(ii) the effect of the compromise or arrangement on those persons in so far as it is different from the effect on the similar interests of other persons.

[65] Mr. Halagan refers to the various personal benefits flowing to Mr. Reifel under the Arrangement, which I have discussed above in relation to the general adequacy of disclosure of the Information Circular.

[66] My conclusion above that the Information Circular makes adequate disclosure of these matters leads inevitably to the conclusion also that there is no violation of s. 253(1) in respect of them. I note also that s. 253(1)(a) requires only that a notice to shareholders "stat[e]" any material interest of a director [officer, etc.] and its effect on the director as it is different from the effect on similar interests of other persons. This requirement to "state" these matters stands in contrast to the section's requirement to "explain" the effect of the compromise or arrangement, and in my view indicates a more limited scope to what is required to be disclosed.

[67] The areas of material interest are plainly stated in the Information Circular. The material interest in question is in each case clearly described in a fashion that conveys its unique effect on the particular director (usually Mr. Reifel). I find that s. 253(1) does not require a further explanation or discussion. The policy underlying the section is satisfied in the clear bringing to shareholders' attention of the various potential personal benefits to the company insiders seeking their approval of the Arrangement.

(ii) Mr. Reifel's Failure To Abstain from Voting or Taking Part in Negotiations

[68] Mr. Halagan submits also that the potential conflicts required that Mr. Reifel (and, in relation to some items, other directors) abstain from voting, and that his failure to do so breached the rules of good corporate governance and his duty to Francisco as well as the Ontario Securities Commission Rule dealing with "related transactions" and ss. 120 and 121 of the Act.

[69] Conflict allegations were made against Board members voting in favour of the arrangement under consideration in the Pacifica Papers litigation. There, the Board split 5-1 as to whether to proceed with the transaction. On the application for the interim order (Pacifica No. 1), Neilson J. held that a conflict of interest would not invalidate a vote taken, and declined to look further into the specific allegations of conflict. Similarly, on the fairness hearing (Pacifica No. 2), Lowry J. stated at para. 62 that "[w]here a director is shown to have acted within his authority but contrary to his fiduciary obligations in casting his vote as a member of the corporation's board, his act may give rise to a claim against him for damages, but it would not normally appear to invalidate his vote". See Pacifica No. 1 at paras. 26-35, and Pacifica No. 2 at paras. 62-73.

[70] Here, Mr. Reifel voted as only one of five board members unanimously in favour of the Arrangement. His abstention would not have affected the Board's approval. As I have noted elsewhere, his areas of potential conflict of interest were disclosed in the Information

Circular, and the shareholders nonetheless voted overwhelmingly in favour of the Arrangement. In those circumstances, I cannot conclude that his failure to abstain and remove himself from participation in the process indicated or caused unfairness to those shareholders.

- [71] Mr. Halagan argues also that Mr. Reifel's failure to abstain from voting on the Arrangement in any event violates s. 120(1) of the Act and therefore precludes the Arrangement's approval under s. 252. Section 121(1), which is quoted earlier in these reasons, requires a director to account for his or her profit from a contract or transaction with the company unless certain steps are taken, including the director's abstention from voting on the contract or transaction. Section 252(3) is also quoted earlier and provides that "[n]o compromise or arrangement . . . takes effect until every requirement of this Act relating to the proposed compromise or arrangement has been complied with . . .".
- [72] It is first to noted that s. 121(1) does not mandate abstention. Rather, it provides that in the absence of abstention and other procedural steps, the director must account to the company for his or her profit.
- [73] Second, even if Mr. Halagan is correct in his position that Mr. Reifel has violated s. 121(1) by failing to abstain from the vote and the negotiations, in my view that failure does not constitute a lack of compliance within the contemplation of s. 252(3). Section 252(3) refers to compliance with requirements under the Act "relating to the compromise or arrangement". The provision falls among a series of procedural requirements relating to the process for bringing the proposed arrangement under the review of the shareholders, creditors and other interested parties, and the court. It is inconsistent with the language and context of s. 252(3), as well as with the perceived scope of the s. 252 fairness hearing, to conclude that it requires compliance with every provision of the Act that may conceivably relate to the arrangement, before the arrangement may be approved as fair to the shareholders. Otherwise, a fairness hearing would be at risk of becoming a full-scale inquiry into every step in the company's history that may be seen as directly or indirectly connected to the proposed arrangement in question. I conclude instead that s. 252(3) refers to the Act's procedural requirements directed specifically to company compromises or arrangements, and not to its requirements of companies and corporate behaviour generally.
- [74] I conclude that Mr. Reifel's failure to abstain from voting on the Arrangement is immaterial to the considerations under s. 252(3).
- [75] I will address the effect of the OSC Rule regarding "related transactions" later in these reasons in relation to Mr. Halagan's submission that Francisco should have obtained an independent valuation of the Arrangement.

(iii) Failure to Appoint An Independent Board Committee

- [76] Mr. Halagan does not suggest that there exists a statutory or other requirement that the board of directors appoint an independent committee to review the proposed Arrangement. While the appointment of such a committee may have been a step open to the board if they considered it useful or appropriate, I cannot conclude that it was a necessary step or that without it the fairness of the Arrangement is in doubt.
- (iv) Failure to Obtain an Independent Valuation for a "Related Transaction"
- [77] Mr. Halagan submits that the Arrangement is a "related transaction" within the meaning of OSC Rule 61-501, and that therefore an independent valuation is required.
- [78] As a member of the TSX Venture Exchange, Francisco is a reporting issuer in Ontario and therefore subject to the Ontario Securities Commission Rules. OSC Rule 61-501 deals comprehensively with insider bids, issuer bids, going private transactions, and related party transactions, and sets out extensive requirements directed ultimately at the integrity of the particular transaction. Certain exemptions are available on satisfaction of stipulated disclosure requirements.
- [79] Mr. Halagan contends that Francisco is a "related party" to Glamis and that therefore the Arrangement must comply with the detailed requirements of the Rule, including that the Arrangement be subject to an independent valuation. It appeared initially to be Mr. Halagan's position that a failure to comply with the OSC Rule was of itself fatal to the Arrangement, by virtue of s. 252(3) of the Act or in violation of the requirements stated by McLachlin C.J. in *Gold Texas Resources*. However, it became clear during oral submissions that his position in this area related rather to the inherent fairness of the Arrangement. I would indeed have difficulty finding a violation of the OSC Rule to be automatically fatal to the approval of the Arrangement under s. 252 of the Act.
- [80] Francisco strenuously disputes the assertion that the Arrangement in any way involves a "related party transaction" within the meaning of the OSC Rule.
- [81] The reasoning supporting Mr. Halagan's position that Francisco is a "related party" to Glamis involves reliance on the proposition that Mr. Reifel and the other directors who agreed to support the Arrangement thereby acted "jointly or in concert" with Glamis in putting the Arrangement to the shareholders for their consideration.
- [82] The main difficulty with Mr. Halagan's reasoning in this area is that it rests on the existence of the support agreements (between Francisco directors and Glamis) as bringing the Arrangement within the "related party" rule, when those support agreements may be seen as an integral part of the Arrangement itself, among otherwise unrelated parties. This recognition appears to underlie the Ontario Securities Commission's direction that "an ordinary lock-up agreement with an identically treated shareholder should not in and of itself generally result in arm's length parties being seen to be acting jointly or in concert": Companion Policy to OSC Rule 61-501, s. 2.3(2).

- [83] In my view it is unnecessary to definitively resolve the unlikely proposition that the Arrangement falls within the OSC Rule. Even if it does, I cannot conclude that Francisco's failure to obtain an independent valuation of the Arrangement calls into question the fairness of the Arrangement in the context of all the other circumstances and indicators that it is fair, indeed beneficial, to Francisco shareholders.
- [84] For similar reasons I conclude that Mr. Reifel's failure to abstain from voting on or taking part in the negotiation of the Arrangement, even if a violation of the OSC Rule, is not material to the assessment of the Arrangement's fairness.
- (e) MR. HALAGAN'S APPLICATIONS FOR ADJOURNMENT AND PRE-HEARING PROCEDURES
- [85] As indicated above, Mr. Halagan seeks the adjournment of the fairness hearing and various orders for pre-hearing procedures in the interim.
- [86] Francisco takes the position that Mr. Halagan is not entitled to document production, but it has nonetheless substantially complied with his numerous requests, with the exception of those documents which by their terms prohibit disclosure. During submissions Ms. Basham fairly indicated that Mr. Halagan does not seek the production of these documents, although he indicated that he may wish to test the issue of confidentiality on cross examination. It is therefore now unnecessary to deal with the application for an order for production of documents.
- [87] As to Mr. Halagan's other applications, Ms. Basham submits that the balance should weigh in favour of a brief adjournment of the fairness hearing. Although Mr. Halagan's motion suggests a panoply of extensive procedural steps before a five-day fairness hearing, she suggested in final submissions that an adjournment of even one week would permit a focussed cross examination of key individuals to illuminate the issues of concern to Mr. Halagan.
- [88] In *Gold Texas Resources Ltd.*, a minority shareholder opposing the arrangement sought to examine parties on their affidavits in support of the petition for approval. McLachlin C.J. dismissed the motion to cross examine, holding as follows:

The onus is on the applicant to show that cross-examination of the affidavits is necessary in that it is likely to produce evidence which will aid in the applicant's case or advance the proceedings; an adjournment for the purpose of cross-examining, will be granted only if this is the case - mere speculation will not suffice: [citation].

... I am not convinced that further exploration of the view of one dissentient in the majority camp or any other of the cross-examination proposed would materially advance [the opposing minority shareholder's] case.

- [89] Having reviewed above the nature of Mr. Halagan's concerns about the fairness of the Arrangement, I am unable to conclude that the cross examinations he proposes would advance the proceedings. The areas he proposes for further exploration are not -- for the reasons I have set out above -- material to the considerations affecting whether or not the Arrangement should be approved under s. 252.
- [90] In addition, the litigation history involving the key players and the controversy among them indicates a strong potential of significant delay that would work to the grave detriment of the shareholders, who overwhelmingly wish the Arrangement to advance.
- [91] Early in her judgment at para. 6, Satanove J. said this:
- The parties' relationship spanned 12 years but the circumstances surrounding what, if any agreement, was made between the parties with respect to the Escrow Shares took place in the early 1980s. Nonetheless, both counsel saw fit to drag in evidence of other business arrangements between the parties which existed both before and after the events concerning the Escrow Shares. Some of this evidence purportedly related to the nature of the parties' relationship and was proffered as an explanation for conduct on both their parts which seemed to be inconsistent with their positions. Most of this other evidence was tendered to destroy each other's credibility and prove that each was trying to "shake down" the other.
- [92] The "drop dead" date for the approval of the Arrangement is July 31, 2002. After that date either party is free to walk away from the deal. Francisco submits that any delay in approval even before July 31 may send a negative signal to the trading market and could seriously jeopardize the interests of Francisco shareholders.
- [93] As Neilson J. noted at para. 42 in *Pacifica No. 1*, courts asked to make a determination under s. 252 of the Act must "recognize the tight time requirements generally characteristic of such transactions". This is not to say that ominous references to imminent deadlines and massive potential financial gains or losses should deflect courts from a careful determination of whether or not the proposed arrangement is fair. Here, I have the additional task of considering essentially whether sufficient evidence for that determination is now before the court, or, rather, whether further investigative steps should first be taken to explore Mr. Halagan's various concerns.
- [94] In my view, Mr. Halagan has failed to establish any basis for delaying the fairness hearing to permit the various forms of further inquiry he wishes pursued. I am satisfied that the Information Circular disclosed to shareholders the material facts relating to the Arrangement and those promoting it and standing to benefit from it. Mr. Halagan's numerous concerns about the propriety of certain past actions taken by Francisco and its directors, Mr. Reifel in particular, do not in my view establish a basis for the adjournment of the present fairness hearing. Even assuming that the suggested pre-hearing procedures would generate supporting evidence of the facts Mr. Halagan alleges, I am unable to conclude that that evidence would assist a determination of whether the present Arrangement is fair.

- [95] Mr. Halagan's own good faith is not assisted by his failure to take steps to challenge any of these actions until now. What he proposes is essentially an inquiry into the propriety of Francisco's corporate governance (with particular regard to Mr. Reifel's role) over its history since his departure from the board. Whether or not his concerns are well-founded, their exploration and resolution is well beyond the scope of a hearing pursuant to s. 252.
- [96] As noted above, I am not persuaded that Mr. Halagan has offered a tenable basis for adjourning the fairness hearing. Were I so persuaded, I would not be confident that any of the investigative steps or inquiries he proposes would be capable of completion in a manner satisfactory to him and fair to the others concerned within the reasonably foreseeable future. In my view, this fact underlines the folly of unduly enlarging the scope of the court's task under s. 252 of the Act beyond the terms and effect of the immediate proposed arrangement.
- [97] This approach seems in accord with the guidance given in the two majority judgements of the Court of Appeal in *Samos Investments Inc. v. Pattison* (2002), 77 B.C.L.R. (3d) 97 (B.C.C.A.). The issue before the Court was whether the plaintiff shareholder's action in relation to breach of fiduciary duty and other alleged wrongdoing in the running of the company's affairs should be stayed as amounting to a collateral attack on an order under s. 252 approving a plan of arrangement for the company made by Cohen J. in earlier proceedings. Rowles J.A. and Mackenzie J.A. in separate judgments concluded that the plaintiff's claims did not amount to such a collateral attack and could proceed, because the hearing under s. 252 had not passed on the merits of those claims.
- [98] It is to be noted that in *Samos* the s. 252 hearing had on the facts been of limited scope. It is possible therefore to read the justices' comments as descriptive of the particular summary hearing and its effect, rather than prescriptive of the scope of future s. 252 hearings. Nonetheless, their discussion of the appropriate scope of s. 252 hearings is instructive and, in my view, of particular application to the situation now before me.
- [99] Rowles J.A. at para. 63 firmly rejected the defendant's view that a s. 252 hearing should consider prior conduct that may give rise to far reaching inquiries, and warned of the ease with which the hearing may be expanded beyond its proper scope:

It seems to me that certainty and efficiency in corporate affairs would not be fostered by adopting the defendants' expansive view of the scope or effect of an order approving a plan of arrangement made under s. 252 of the Company Act. An inquiry into the substantive fairness of a plan of arrangement, having regard to the prior conduct that might be relevant to the terms of the plan, would mandate inquiries of a far reaching nature even though the court has no jurisdiction under s. 252 to provide a remedy for such alleged wrongful acts. It is not difficult to conceive of past actionable wrongs that could have had an adverse impact on a company's equity and hence its share value. [emphasis added]

[100] Mackenzie J.A. spoke at paras. 86-7 of problematic consequences that could have ensued, had Cohen J. elected to hold the extensive s. 252 hearing sought by the plaintiff shareholder at the time:

The complexities of the corporate reorganization over the years leading up to the arrangement would have required an in-depth examination of the earlier steps in the reorganization and, in terms of the allegations of unlawful acts and conspiracy, the circumstances surrounding the various steps. It was impractical for the complaints raised in this litigation to have been adequately examined in the summary process of this s. 252(1) petition.

At most, Cohen J. could have adjourned the hearing for an in depth inquiry. There are obvious disadvantages to such a course. First, the petition would be delayed, perhaps indefinitely given the sweep of the allegations that were unproven and incapable on the material of even a preliminary assessment of the merits. Second, any credence given by the chambers judge to the allegations would have been unfair to the [company] majority interests in the absence of a rigorous examination of the facts which could not have been addressed in any meaningful manner on the arrangement petition. . . .

[101] In my view, the course suggested by Mr. Halagan carries obvious disadvantages similar to those of which Mackenzie J.A. warns.

[102] It follows from my decision not to adjourn the fairness hearing above that I also decline to order the appointment of independent counsel to investigate the fairness of the Arrangement, or to convert the petition into an action.

APPROVAL of the Arrangement

[103] The evidence before me indicates that the Arrangement is seen as advantageous to Francisco for bringing to Francisco Glamis' financial resources and strong management to develop the existing discoveries on Francisco's mineral properties. Francisco is said to lack the necessary financial resources, personnel, and experience to develop the discoveries and prosper as an independent mining company. Those promoting the Arrangement speak of the obvious synergy between the two companies, which is likely reflected in the increase in Francisco's share price since the announcement of the Arrangement. The evidence to this effect is not disputed.

[104] The Arrangement is said to be designed to give Francisco shareholders the ability to participate through their new ownership of Glamis shares in the mining development commenced by Francisco. It is structured so as to allow existing Francisco shareholders to participate in future exploration activities through their proposed share ownership of Chesapeake, which will hold a substantial portion of Francisco's current cash assets and certain mineral exploration properties.

- [105] The listing of Glamis shares on the Toronto and New York stock exchanges can be expected to provide greater liquidity to shareholders than is available to Francisco shareholders on the TSX Venture Exchange only.
- [106] The Arrangement has the unanimous support of the Francisco board of directors and the endorsement of an overwhelming majority of the shareholders who voted on the proposal. The market reaction appears to be strongly in favour. There is no evidence of any shareholder, including Mr. Halagan, exercising their right of dissent to effectively remove their shareholdings from the Arrangement.
- [107] Most of Mr. Halagan's concerns refer to the propriety of the process by which the Arrangement was reached and the adequacy of its disclosure to the shareholders. Few of his concerns (with the notable exception of those relating to the 1993 private placement) in any fashion relate to the substance of the Arrangement. Nothing in the evidence suggests that the Arrangement is other than beneficial to Francisco's shareholders. With the exception of Mr. Halagan's concern that the share exchange ratio fails to reflect an accounting of Mr. Reifel's possible profits from the private placement (an effect I consider too remote to be material), no weakness is identified in the advantages the Arrangement offers to Francisco shareholders and no superior alternative is suggested.
- [108] I have no difficulty concluding that the Arrangement is in all respects fair and reasonable, and one that a Francisco shareholder, acting in his or her own interest as an intelligent and honest business person, might reasonably approve.
- [109] It follows from my reasons given in response to Mr. Halagan's various objections to the Arrangement that I also conclude that the other prerequisites to approval, as stated by McLachlin C.J. in *Gold Texas Resources*, *supra*, are satisfied.

Conclusion

- [110] I conclude that the determination as to approval of the Arrangement should be made at this time and not adjourned, and that the Arrangement is fair to the shareholders of Francisco and should be approved under s. 252 of the Company Act.
- [111] I make the order in the form sought by counsel.

"H. Holmes, J."

The Honourable Madam Justice H. Holmes

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