

**Public Document**

**IN THE MATTER OF AN ARBITRATION UNDER CHAPTER ELEVEN OF THE  
NORTH AMERICAN FREE TRADE AGREEMENT AND THE 1976 UNCITRAL  
ARBITRATION RULES**

**BETWEEN:**

**WESTMORELAND MINING HOLDINGS LLC**

**Claimant**

**AND**

**GOVERNMENT OF CANADA**

**Respondent**

**(ICSID Case No. UNCT/20/3)**

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**GOVERNMENT OF CANADA**

**Second Expert Report of Kathryn A. Coleman**

**April 9, 2021**

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## I. PURPOSE AND SCOPE OF REPORT

1. The Government of Canada (“Canada”) asked me to address certain issues and questions of U.S. law raised by Westmoreland Mining Holdings LLC (“WMH”) in its Counter-Memorial on Jurisdiction and accompanying documents (the “Counter-Memorial on Jurisdiction”), filed on February 26, 2021, in the NAFTA Chapter Eleven matter captioned *Westmoreland Mining Holdings LLC v. Government of Canada* (ICSID Case No. UNCT/20/3) (the “Arbitration Proceeding”).<sup>1</sup> In particular, this report will address WMH’s arguments with respect to: (1) the sale transaction in which Westmoreland Coal Company (“WCC”) sold its interests in the Canadian companies now owned by WMH (the “Canadian Entities”); (2) the nature of the relationship between the First Lien Lenders<sup>2</sup> and WCC, specifically whether the First Lien Lenders exercised “control” over, or had “beneficial ownership” in, WCC and its assets (including WCC’s equity interest in the Canadian Entities) under U.S. law; and (3) other relevant concepts of U.S. law.

## II. EXECUTIVE SUMMARY

2. WMH suggests that the transaction by which WCC’s assets, including its equity interests in the Canadian Entities, were transferred to WMH was a mere reshuffling of assets among members of a corporate family. As detailed in my First Expert Report, that is not the case. WMH was created as a new entity by the First Lien Lenders shortly before the transaction to serve as the purchaser of WCC’s assets. The effect of the multi-step transaction was to transfer WCC’s assets to WMH, the First Lien Lenders’ designee, in partial satisfaction of WCC’s debt to the First Lien Lenders. WMH is not an affiliate of WCC, nor is it an “associated company.” The relationship between the two companies was that of a buyer and seller. WMH and WCC were legally adverse in interest

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<sup>1</sup> Capitalized terms used but not defined herein shall have the meaning ascribed to them in **RER**-Coleman-Bankruptcy-Memorial on Jurisdiction (referred to in this report as the “First Expert Report”).

<sup>2</sup> In its Counter-Memorial on Jurisdiction, WMH uses the term “Secured Creditors” to refer to the lenders under the Senior Secured Note and Term Loan Facility (as defined in ¶ 21 below). *See* Counter-Memorial on Jurisdiction, Appendix A, ¶ 6. In my First Expert Report and in this report, I use the term “First Lien Lenders” to refer to the same population. I use the term “First Lien Lenders” to distinguish between the lenders under the instruments secured by a first-lien security interest on substantially all of the WLB Debtors’ U.S. assets (including the equity of Westmoreland Canadian Investments, LP) and other creditors whose debt might be secured by a different lien. *See R-049*, Westmoreland Coal Company, et al., *Declaration of Jeffrey S. Stein, Chief Restructuring Officer of Westmoreland Coal Company, in Support of Chapter 11 Petitions and First Day Pleadings* [Court Docket, Doc. 54], 9 October 2018 [Excerpt of Declaration] (“Stein First Day Declaration”), ¶¶ 29-31.

and were represented by separate counsel. The U.S. bankruptcy court that managed the process made a specific finding that WMH and WCC were transacting at arm's-length.

3. WMH also posits that its owners (*i.e.*, the entities that hold the equity interests in WMH)—namely, the First Lien Lenders—“controlled” WCC from the day they first extended credit to WCC. This notion is inaccurate. Under U.S. law, a business entity, whether it be a corporation, an LLC, or a partnership, is controlled by its owners (and the management they appoint), not by its creditors. Debt instruments and equity interests have radically different characteristics, notwithstanding that extending secured credit to a borrower and buying an equity stake in a company may both sometimes colloquially be referred to as making an “investment” in that company. A secured lender enters into a contractual relationship with the borrower to lend the borrower money, with the expectation of repayment in full, and has rights vis-à-vis the borrower's assets if the money is not repaid. Unlike an equity holder, a secured lender does not assume enterprise risk, nor is it entitled to participate in the borrower's overall success. In the context of a U.S. bankruptcy, the distinction between debt and equity is foundational and cannot be disregarded. The First Lien Lenders were creditors of WCC, not owners, and therefore they did not “control” WCC, its assets, or its bankruptcy process.

### **III. WCC'S BANKRUPTCY PROCESS AND THE SALE TRANSACTION BETWEEN WCC AND WMH**

4. I have been asked to comment on the following statements that WMH has made in characterizing WCC's bankruptcy process and the sale of the Canadian Entities to WMH:

- “To effectuate this transfer [of assets] through the bankruptcy process, WMH was created as a wholly-owned subsidiary of WCC”<sup>3</sup>; and
- “WCC's transfer of Prairie and the associated NAFTA claim to WMH similarly was between associated companies,”<sup>4</sup> and, more specifically, that the Canadian Entities were

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<sup>3</sup> Counter-Memorial on Jurisdiction, ¶ 74; *see also e.g.*, Counter-Memorial on Jurisdiction, ¶¶ 2, 11, and 23; Counter-Memorial on Jurisdiction, Appendix A, ¶¶ 1 and 39; CER-Paulsson-International Law-Counter-Memorial on Jurisdiction, ¶ 23 (each incorrectly stating that WMH was created as a wholly-owned subsidiary of WCC).

<sup>4</sup> Counter-Memorial on Jurisdiction, ¶ 63.

“transferred through bankruptcy from a parent company to another wholly-owned subsidiary.”<sup>5</sup>

5. These statements are inaccurate. First, WMH was not created as a wholly-owned subsidiary of WCC. As I explained in my First Expert Report, WMH was formed on behalf of the First Lien Lenders.<sup>6</sup> WMH’s formation documents confirm that it was formed by Thomas Moers Mayer,<sup>7</sup> a bankruptcy partner at Kramer Levin Naftalis & Frankel LLP (“Kramer Levin”)<sup>8</sup>—the law firm that represented the First Lien Lenders and WMH in the WCC Bankruptcy Proceeding.<sup>9</sup> Due to conflict of interest rules under the rules of professional conduct, Mr. Mayer could not have represented or acted on behalf of WCC while representing the First Lien Lenders and WMH.

6. Second, under U.S law, the term “associated companies” has no legal significance; rather, members of a corporate family, and companies with some level of common ownership, are referred to as “affiliated companies.”<sup>10</sup> WCC and WMH were not affiliated companies<sup>11</sup> because there was

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<sup>5</sup> Counter-Memorial on Jurisdiction, ¶ 17.

<sup>6</sup> See **RER-Coleman-Bankruptcy-Memorial on Jurisdiction** [First Report], ¶¶ 64 and 70.

<sup>7</sup> **R-081**, Westmoreland Mining Holdings LLC, “Limited Liability Company Agreement of Westmoreland Mining Holdings LLC”, 31 January 2019 (“Original LLC Agreement”) (signed by Thomas Moers Mayer). In addition, the Certificate of Formation was signed and filed by Ilya Kontorovich, an associate at Kramer Levin, as authorized person. **R-082**, Westmoreland Mining Holdings LLC, Certificate of Formation, 31 January 2019 (“Certificate of Formation”). The Original LLC Agreement confirms my reading, based on my years of experience, of documents filed before the WCC Bankruptcy Court indicating that WMH was *not* formed as a subsidiary of WCC. See **RER-Coleman-Bankruptcy-Memorial on Jurisdiction** [First Report], note 82.

<sup>8</sup> **R-083**, Kramer Levin, “Kramer Levin Represents Secured Lenders in Acquisition of Westmoreland Coal’s Assets Under Chapter 11 Plan”, 15 March 2019, <<https://www.kramerlevin.com/en/perspectives-search/kramer-levin-represents-secured-lenders-in-acquisition-of-westmoreland-coals-assets-under-chapter-11-plan.html>> (accessed March 25, 2021).

<sup>9</sup> See **RER-Coleman-Bankruptcy-Memorial on Jurisdiction** [First Report], note 83 (discussing Kramer Levin’s representation of the First Lien Lenders and WMH); see also **R-061**, Kramer Levin Naftalis & Frankel LLP & Porter Hedges LLP, *Verified Statement of Kramer Levin Naftalis & Frankel LLP and Porter Hedges LLP Pursuant to Federal Rule of Bankruptcy Procedure 2019*, [Court Docket, Doc. 496], 14 November 2018 (including Thomas Moers Mayer on the signature block of the firm representing the First Lien Lenders); **R-053**, Westmoreland Coal Company, et al., *Stalking Horse Purchase Agreement, Exhibit H-6 to Notice of Sixth Amendment to the Plan Supplement* [Court Docket, Doc. 1621], 15 March 2019, § 12.01 (directing attention to Thomas Moers Mayer as a notice party on behalf of WML as “Buyer”); **R-062**, Westmoreland Coal Company, et al., *Notice of Seventh Amendment to the Plan Supplement* [Court Docket, Doc. 1849], 17 May 2019, § 15.3 (directing attention to Thomas Moers Mayer as a notice party on behalf of WMH).

<sup>10</sup> The amount of equity ownership deemed to create “affiliate” status varies across different areas of U.S. law, and may also be specified by contract.

<sup>11</sup> See **RER-Coleman-Bankruptcy-Memorial on Jurisdiction** [First Report], note 103 (reciting the Bankruptcy Code definition of “affiliate”).

no common equity ownership between WCC and WMH prior to or following the transaction. Prior to the transaction, WCC was a public company with widely distributed shares, whereas WMH's equity was owned by the First Lien Lenders' nominee.<sup>12</sup> Following the transaction, WCC was (and still is<sup>13</sup>) a debtor in bankruptcy, while WMH's equity remained held by the First Lien Lenders.<sup>14</sup> The argument that, despite the lack of common ownership, WMH is an affiliate of, or "associated" with, WCC because the First Lien Lenders, who own the equity of WMH, previously lent money to WCC is contrary to U.S. law. Under that theory, every bank and hedge fund would be "associated" with every company to which it loaned money, dissolving any distinction between virtually every sophisticated company on the planet.

7. While one step of the multistep transaction through which WMH purchased assets from WCC involved WCC momentarily holding the equity of WMH,<sup>15</sup> to say that WCC and WMH were "associated"<sup>16</sup> or that WCC was the parent of WMH<sup>17</sup> because of that brief moment in time<sup>18</sup> entirely disregards the WCC Bankruptcy Court's finding that the sale transaction between WCC and WMH was conducted at arm's-length and was not subject to the higher scrutiny applied to insider transactions.<sup>19</sup> As I explained in my First Expert Report, these sale transaction steps

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<sup>12</sup> **R-081**, Original LLC Agreement, § 6(a) ("The Company initially shall be wholly owned by the Member.").

<sup>13</sup> See **R-084**, Westmoreland Coal Company, *Chapter 11 Post-Confirmation Report for the Quarter Ending December 31, 2020*, [Court Docket, Doc. No. 3221], 3 February 2021.

<sup>14</sup> **RER-Coleman-Bankruptcy-Memorial on Jurisdiction** [First Report], ¶ 80.

<sup>15</sup> **RER-Coleman-Bankruptcy-Memorial on Jurisdiction** [First Report], ¶¶ 76-80; see also **RER-Coleman-Bankruptcy-Memorial on Jurisdiction** [First Report], ¶ 82.

<sup>16</sup> See Counter-Memorial on Jurisdiction, ¶ 63.

<sup>17</sup> See e.g., Counter-Memorial on Jurisdiction, ¶¶ 17 and 23.

<sup>18</sup> WMH was formed by the First Lien Lenders' nominee on January 31, 2019, **R-082**, Certificate of Formation, and the sale closed on March 15, 2019, **R-080**, Westmoreland Coal Company, et al., *Notice of (I) Entry of Order Confirming the Amended Joint Chapter 11 Plan of Westmoreland Coal Company and Certain of Its Debtor Affiliates and (II) Occurrence of the Plan Effective Date* [Court Docket, Doc. 1608], 15 March 2019.

<sup>19</sup> **RER-Coleman-Bankruptcy-Memorial on Jurisdiction** [First Report], ¶ 72(c). In order to make this finding, the WCC Bankruptcy Court was required to determine that WMH was not an "insider" of WCC. As I discussed in my First Expert Report, the Bankruptcy Code definition of "insider" encompasses "affiliates" of the debtor. See **RER-Coleman-Bankruptcy-Memorial on Jurisdiction** [First Report], note 103. Therefore, the WCC Bankruptcy Court effectively determined that WMH was not an "affiliate" of WCC, as that term is defined in the Bankruptcy Code (which is to say, that WMH did not own or control WCC, that WCC did not own or control WMH, and that WMH was not owned or controlled by an entity that also owned or controlled WCC). As discussed in my First Expert Report, I consider the WCC Plan Confirmation Order to apply equally to WMH and WML as "Purchaser." See **RER-Coleman-Bankruptcy-Memorial on Jurisdiction** [First Report], note 81. See also generally **RER-Coleman-Bankruptcy-Memorial on Jurisdiction** [First Report], ¶ 72.

occurred virtually simultaneously,<sup>20</sup> and the transaction both began and ended with the First Lien Lenders (or their nominee) owning WMH.<sup>21</sup> WCC's only meaningful action with respect to its ownership of WMH was to transfer the purchased assets to it and then immediately relinquish its ownership stake to the First Lien Lenders as part of the overarching sale transaction. At no point did WCC have a meaningful role or relationship with respect to the management or operations of WMH that would lead to a different conclusion than the one at which the WCC Bankruptcy Court arrived.

8. Although WMH asserts that the Canadian Entities were “transferred through bankruptcy from a parent company to another wholly-owned subsidiary,”<sup>22</sup> the equity in the Canadian Entities was not transferred as a mere reshuffling of equity interests among members of a corporate family. Instead, and as I discussed in my First Expert Report, WCC transferred its assets, including its ownership interest in the Canadian Entities, to an unaffiliated third party, WMH, in satisfaction of debt.<sup>23</sup> WMH was formed as a new entity on behalf of the First Lien Lenders before the transaction for the purpose of taking ownership of the WLB Debtors’<sup>24</sup> assets, including the equity in the Canadian Entities, in satisfaction of the WLB Debtors’ outstanding debt obligations owed to the First Lien Lenders.<sup>25</sup> WMH was the vehicle through which the First Lien Lenders purchased the WLB Debtors’ assets in several simultaneous steps: (i) certain subsidiary WLB Debtors transferred ownership of the purchased assets to WMH in exchange for equity interests in WMH; (ii) the subsidiary WLB Debtors passed their equity interests in WMH up the corporate chain to WCC as a dividend; and (iii) WCC distributed the equity interests in WMH right back to the First Lien Lenders through the WCC Plan.<sup>26</sup> The fact that the sale transaction took place in the context of the WCC Bankruptcy Proceeding only inured to the benefit of WMH (and by extension the First Lien Lenders) because WMH was able to obtain the protections offered by the WCC Bankruptcy

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<sup>20</sup> **RER-Coleman-Bankruptcy-Memorial on Jurisdiction** [First Report], ¶ 75.

<sup>21</sup> **RER-Coleman-Bankruptcy-Memorial on Jurisdiction** [First Report], ¶¶ 73, 80, and 82.

<sup>22</sup> **Counter-Memorial on Jurisdiction**, ¶ 17.

<sup>23</sup> **RER-Coleman-Bankruptcy-Memorial on Jurisdiction** [First Report], ¶¶ 73-83 and 89-90.

<sup>24</sup> *See* **RER-Coleman-Bankruptcy-Memorial on Jurisdiction** [First Report], ¶ 8 and note 6 (defining “WLB Debtors”).

<sup>25</sup> **RER-Coleman-Bankruptcy-Memorial on Jurisdiction** [First Report], ¶¶ 70, 80, and 83.

<sup>26</sup> **RER-Coleman-Bankruptcy-Memorial on Jurisdiction** [First Report], ¶¶ 73-80.

Court's findings that the sale was free and clear, made in good faith, conducted at arm's-length, and that WMH would not face any successor liability.<sup>27</sup>

#### **IV. THE RELATIONSHIP BETWEEN THE FIRST LIEN LENDERS AND WCC**

9. I have also been asked to provide my views on the nature of the relationship between the First Lien Lenders and WCC, and, in particular, on whether the First Lien Lenders exercised "control" over, or had "beneficial ownership" interests in, WCC or its assets at any time. At the heart of these questions lies the basic distinction between debt and equity under U.S. law in general, and in bankruptcy law in particular. I discuss these principles below, before assessing the relationship between the First Lien Lenders and WCC.

##### **A. The Distinction Between Debt and Equity Under U.S. Law**

###### **1. General Principles**

10. Under U.S. law, a company can raise money in the capital markets in one of two principal ways: by offering equity (or ownership interests in the company) or by incurring debt. When a company offers equity in exchange for an infusion of funds, it is offering a stake in the future financial success of the company to investors in return for immediate access to capital. The investor has a right to share in the company's profits and enterprise value (referred to as "earning dividends"), but only when the company is able to satisfy its obligations to creditors as well. The equity holder also has the right to participate in controlling the company's actions by virtue of electing the company's board of directors.

11. By contrast, when a company raises money by incurring debt, the borrower is receiving immediate access to funds in exchange for a promise to repay the money to the lender at some future point (almost invariably with interest, to compensate the lender for use of its funds). Very often the borrower must give the lender additional protection by granting liens or security interests on the borrower's property ("collateral"), thereby affording the lender direct access to the borrower's property in the event of nonpayment.<sup>28</sup> Lenders are inherently adverse to their

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<sup>27</sup> **RER-Coleman-Bankruptcy-Memorial on Jurisdiction** [First Report], ¶ 72.

<sup>28</sup> Broadly speaking, debt financing can take two forms: debt securities or loans. A debt security is an instrument that evidences a debt and is traded in the capital markets. The company issues the debt security by selling the security to



borrowers and have no ownership rights in the borrower entity. Thus, for example, they have no right to participate in electing the board of directors of the company.

## 2. The Concept of “Control” As It Relates to Debt Versus Equity

12. In its Counter-Memorial on Jurisdiction, WMH refers to an undefined concept of “control,” asserting that the First Lien Lenders “controlled” WCC (by virtue of the loan documents) and the WCC Bankruptcy Proceeding (by virtue of the WCC RSA).<sup>29</sup> Under U.S. law, the concept of “control” is used in different legal contexts and has different consequences depending on the situation.<sup>30</sup> Generally, “control” of a corporation like WCC is deemed to reside in those who have the power to direct management and the company’s policies, including majority shareholders (who can vote on the appointment of directors and to approve certain transaction), officers of the company (who manage the day-to-day operations of the company), directors of the company (who appoint officers and set higher-level strategy for the company),<sup>31</sup> and, in rarer cases, minority shareholders who have agreed to act in concert to create a voting majority.

13. Lenders and other creditors do not typically fall within the scope of persons who can exercise control,<sup>32</sup> and loan covenants, which are contractual provisions often contained in debt instruments by which the borrower agrees to take or refrain from taking specified actions, do not meet the

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lenders in exchange for the promise of repayment at a time certain. A loan is similarly an instrument that evidences a debt, but it is not traded in the same way as debt securities.

<sup>29</sup> See e.g., Counter-Memorial on Jurisdiction, Appendix A, ¶¶ 11, 13, 15, and 22; see also Counter-Memorial on Jurisdiction, ¶ 71.

<sup>30</sup> For example, in the equity securities context, the U.S. Securities and Exchange Commission has defined control as “the possession, direct or indirect, of the power to direct or cause the direction of the management and policies of a person, whether through the ownership of voting securities, by contract [governing intra-shareholder relations], or otherwise.” **R-085**, Title 17 of the U.S. Code of Federal Regulations – Chapter II, Securities & Exchange Commission [Excerpts] (“17 C.F.R.”), § 230.405.

<sup>31</sup> The board cannot delegate its authority to any person or entity outside of the board. See **R-086**, *Obeid v. Hogan*, No. CV 11900-VCL, 2016 WL 3356851, at \*15 (Del. Ch. June 10, 2016).

<sup>32</sup> In very rare cases, a business entity with no equity ownership may be alleged to have dominated or controlled another entity’s business to such a great extent that the “dominant” business should be liable to third parties for certain of the “subservient” business’s obligations. **R-087**, *Krivo Indus. Supply Co. v. Nat’l Distillers & Chem. Corp.*, 483 F.2d 1098, 1101 (5th Cir. 1973). However, the quantum of control necessary to establish liability where there is no equity ownership is high. **R-088**, *James E. McFadden, Inc. v. Baltimore Contractors, Inc.*, 609 F. Supp. 1102, 1105 (E.D. Pa. 1985). Merely loaning money and taking steps to monitor the credit of the borrower is not sufficient. **R-087**, *Krivo Indus. Supply Co. v. Nat’l Distillers & Chem. Corp.*, 483 F.2d 1098, 1105 (5th Cir. 1973).

above-described threshold for control.<sup>33</sup> These covenants are designed to maximize the probability that the lenders will be paid in full, to assure that collateral value is maintained, and to provide lenders with sufficient information to monitor the borrower’s compliance with loan obligations. The idea behind such covenants is to ensure that the risk of nonpayment does not increase after the loan is extended. Before making funds available, lenders perform diligence and price the loan according to the lenders’ assessment of risk. Loan covenants are designed to prevent that risk from changing. Covenants in debt instruments are merely contractual undertakings which the borrower has both the right and the power to disregard.

14. Accordingly, the existence of loan covenants can further distinguish between debt and equity. The hallmark of equity is the ability to vote on corporate governance issues, and thereby directly participate in controlling the company’s actions. Lenders do not have this right. While debt instruments may contain covenants meant to induce or disincentivize certain behavior, they do not confer a right of control; the borrower maintains the authority to operate the business—either in accordance with the covenants or not. If a borrower chooses to breach a covenant, the lender may have certain rights to increased interest or to access its collateral. But the lender never gets the right to change the borrower’s corporate decisions.

### **3. The Concept of “Beneficial Ownership” Is Distinct from a Security Interest**

15. Throughout its Counter-Memorial on Jurisdiction, WMH posits that there is a continuity of “beneficial interest” or “beneficial ownership” between WCC and WMH.<sup>34</sup> However, WMH improperly equates the First Lien Lenders’ security interest in the WLB Debtors’ assets to a “beneficial interest” in, or “beneficial ownership” of, the WLB Debtors and their assets.

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<sup>33</sup> **R-087**, *Krivo Indus. Supply Co. v. Nat'l Distillers & Chem. Corp.*, 483 F.2d 1098, 1105 (5th Cir. 1973) (discussing *Chicago Mill & Lumber Co. v. Boatmen's Bank*, 234 F. 41 (8th Cir. 1916), wherein the Eighth Circuit refused to find a bank liable for the debts of to a mill and land company, notwithstanding the large sums of money the company owed the bank, because the bank’s conduct was “easily and naturally referable to a legitimate and customary practice of keeping an oversight by a creditor over the business, management, and operations of a debtor of doubtful solvency. All the facts of the this case and all the reasonable inferences deducible from them would not, in our opinion, have warranted a jury in finding . . . that the [bank] was carrying on the business of the [company] as part of its own. . . .”) (alterations in original).

<sup>34</sup> See generally Counter-Memorial on Jurisdiction, § III.C.3; CER-Paulsson-International Law-Counter-Memorial on Jurisdiction, ¶ 70 (referring to “beneficial as opposed to formal ownership”).

16. Under U.S. securities law, the concept of “beneficial ownership” refers to who holds the true economic interest in an equity security, regardless of the name in which the interest is held.<sup>35</sup> The beneficial owner has voting power over the security and/or the decision-making authority regarding the disposition of the security, irrespective of the nominal holder’s identity.

17. A lender taking a security interest in property of its borrower to assure repayment of its loan does not “beneficially own” the debtor or the debtor’s assets. A security interest affords lenders direct property rights in the assets the borrower has pledged to support the lender’s right of repayment if the borrower defaults on its obligations to the lender. Until the lender exercises its rights vis-à-vis the collateral, the collateral remains under the ownership and control of the titleholder—the borrower.

#### 4. Treatment of Debt and Equity in the U.S. Bankruptcy Process

18. As I mentioned in my First Expert Report, debt is treated differently from equity in the U.S. bankruptcy process.<sup>36</sup> The reason for the different treatment is that debt instruments document contractual arrangements for the extension and repayment of credit—between counterparties who are inherently adverse to each other—whereas equity interests are not contractual undertakings and exist to evidence ownership of a portion of an enterprise. The U.S. Bankruptcy Code prioritizes repayment of debt over returns to equity holders, such that all debt must be paid in full before there can be any value distributed to equity.<sup>37</sup>

19. The U.S. bankruptcy process provides a single forum for a distressed company to address all of its prepetition liabilities and obligations, including those owed to creditors (who have extended credit to the company and are entitled to repayment) and equity holders (who have purchased

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<sup>35</sup> See **R-085**, 17 C.F.R., § 240.13d-3(a) (“For the purposes of sections 13(d) and 13(g) of the [Securities Exchange Act of 1934] a beneficial owner of a security includes any person who, directly or indirectly, . . . has or shares: (1) voting power which includes the power to vote, or to direct the voting of, such security; and/or (2) investment power which includes the power to dispose, or to direct the disposition of, such security.”). Furthermore, the rule explicitly excludes a holder of a security interest, or a pledgee, in securities “shall not be deemed to be the beneficial owner of such pledged securities until the pledgee has taken all formal steps necessary which are required to declare a default and determines that the power to vote or to direct the vote or to dispose or to direct the disposition of such pledged securities will be exercised,” subject to certain requirements. **R-085**, 17 C.F.R., § 240.13d-3(d)(3).

<sup>36</sup> Cf. **RER**-Coleman-Bankruptcy-Memorial on Jurisdiction [First Report], ¶ 30 and note 11.

<sup>37</sup> See **R-045**, Title 11 of the U.S. Code - Bankruptcy, 11 U.S.C §§ 101 et seq. (“11 U.S.C.”) [Updated Excerpts], 11 U.S.C. § 1129(b)(2).

ownership stakes in the company and have no rights or remedies if that ownership decreases in value).<sup>38</sup> A debtor in chapter 11 is inherently adverse to its creditors, who have rights to the value of its assets and remedies they can exercise, but not to its shareholders, who have neither.

## **B. The First Lien Lenders Did Not “Control” WCC or WCC’s Assets By Virtue of Loan Covenants**

20. WCC is a corporation organized under the laws of Delaware and headquartered in Englewood, Colorado.<sup>39</sup> As a corporation, WCC’s business was managed by its board of directors,<sup>40</sup> and, prior to its Bankruptcy Proceedings, WCC was a publicly-held company, which was formerly traded on the NASDAQ Global Market.<sup>41</sup>

21. On December 16, 2014, WCC obtained approximately \$700 million of debt financing—through debt instruments in the form of both notes and loans—from the First Lien Lenders. On December 16, 2014, WCC issued senior secured notes in an aggregate principal amount of \$350 million, due in 2022 (the “Senior Secured Notes”).<sup>42</sup> On the same date, WCC also entered into a \$350 million secured term loan facility (the “Term Loan Facility”).<sup>43</sup> The Senior Secured Notes and the Term Loan Facility were secured by liens on substantially all of the WLB Debtors’ U.S. assets, including 65% of the equity interests of Westmoreland Canadian Investments, LP.<sup>44</sup> On May 21, 2018, WCC, Westmoreland San Juan Holdings, Inc, and Prairie jointly borrowed an

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<sup>38</sup> **RER-Coleman-Bankruptcy-Memorial** on Jurisdiction [First Report], ¶ 25.

<sup>39</sup> **R-049**, Stein First Day Declaration, ¶ 8.

<sup>40</sup> WCC’s board of directors was dissolved on the Plan Effective Date, which occurred on March 15, 2019. See **R-042**, Westmoreland Coal Company, et al., *Amended Joint Chapter 11 Plan of Westmoreland Coal Company and Certain of Its Debtor Affiliates*, Exhibit A to United States Bankruptcy Court, *Order Confirming the Amended Joint Chapter 11 Plan of Westmoreland Coal Company and Certain of Its Debtor Affiliates* [Court Docket, Doc. 1561], 1 March 2019 [Excerpt] (“WCC Plan”), Art IV.O.

<sup>41</sup> **R-049**, Stein First Day Declaration, ¶ 32.

<sup>42</sup> **R-049**, Stein First Day Declaration, ¶ 31; see also **C-032**, Westmoreland Coal Company, Current Report (Form 8-K), 16 December 2014.

<sup>43</sup> **R-049**, Stein First Day Declaration, ¶ 30; see also **C-032**, Westmoreland Coal Company, Current Report (Form 8-K), 16 December 2014. Under U.S. law, only the Senior Secured Notes would be considered “debt securities.” Cf. Counter-Memorial on Jurisdiction, Appendix A, ¶ 1; see also **R-089**, *Kirschner v. JPMorgan Chase Bank, N.A.*, No. 17 Civ. 6334 (PGG), 2020 WL 2614765 (S.D.N.Y. May 22, 2020) (holding that syndicated bank loans are not securities).

<sup>44</sup> **R-049**, Stein First Day Declaration, ¶¶ 30-31; see also **C-036**, Guaranty and Collateral Agreement between WCC and Bank of Montreal, 16 December 2014, § 3, Schedule 3.03; **C-037**, Collateral Agreement between WCC and U.S. Bank Nat’l Assn., 16 December 2014 § 3, Schedule 3.03.

additional \$90 million under a \$110 million bridge loan facility (the “Bridge Loan Facility”) from certain of the First Lien Lenders.<sup>45</sup> The Bridge Loan Facility was secured by liens on substantially all of the WLB Debtors’ Canadian assets, in addition to the WLB Debtors’ U.S. assets that were not previously encumbered.<sup>46</sup> On November 15, 2018, the WCC Bankruptcy Court approved an additional \$110 million Senior Secured Debtor-in-Possession term loan facility (the “DIP Facility”), provided by certain of the First Lien Lenders, under which WCC, Westmoreland San Juan Holdings, Inc, and Prairie were again borrowers. The DIP Facility was secured by liens on substantially all of the WLB Debtors’ U.S. and Canadian assets.<sup>47</sup>

22. In connection with the financing arrangements, WCC agreed to certain covenants and restrictions in exchange for access to the financing provided by the Senior Secured Notes, the Term Loan Facility and the Bridge Loan Facility. For example, the credit agreement governing the Term Loan Facility contains WCC’s undertaking to provide the First Lien Lenders with financial statements, access to the WLB Debtors’ books and records, and to maintain insurance on its property.<sup>48</sup> In the indenture governing the Senior Secured Notes, WCC promised, among other things, not to incur certain types of additional debt or sell assets unless certain conditions were

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<sup>45</sup> **R-049**, Stein First Day Declaration, ¶ 29; *see also* **C-039**, Westmoreland Coal Company, Current Report (Form 8-K), 21 May 2018. Prior to the Bridge Loan Facility, Prairie was not a borrower or a guarantor of the Senior Secured Notes or the Term Loan Facility. As such, the First Lien Lenders did not have a direct security interest in Prairie’s assets. However, once Prairie became a borrower under the Bridge Loan Facility, its assets became the First Lien Lenders’ collateral. Although I cannot opine as to Prairie’s actual rationale for becoming a borrower under the Bridge Loan Facility, one possible explanation for Prairie’s sudden involvement in the WCC-First Lien Lender relationship is that the First Lien Lenders were unwilling to loan additional funds to the WLB Debtors without additional collateral.

<sup>46</sup> **R-049**, Stein First Day Declaration, ¶ 29; *see also* **C-039**, Westmoreland Coal Company, Current Report (Form 8-K), 21 May 2018 (stating that the Bridge Loan Facility was “secured by a first lien on substantially all U.S. and Canadian assets, including 35% of the equity in the holding company for the Company’s Canadian business not previously securing the Existing Secured Debt, and guaranteed by all of the Company’s material U.S. and Canadian subsidiaries.”).

<sup>47</sup> **C-040**, United States Bankruptcy Court, *Final Order (I) Authorizing Westmoreland Coal Company and Certain of Its Affiliates to Obtain Postpetition Secured Financing, (II) Granting Liens and Providing Superpriority Administrative Expense Claims, (III) Authorizing the Use of Cash Collateral, (IV) Granting Adequate Protection, (V) Modifying the Automatic Stay, and (VI) Granting Related Relief* [Court Docket, Doc. 520], 15 November 2018 (the “Final DIP Order”), ¶ 3.

<sup>48</sup> *See* **C-032**, Westmoreland Coal Company, Current Report (Form 8-K), 16 December 2014, Ex. 4.3 §§ 9.01-9.03. In its S.E.C. filing, WCC described the agreement as containing “customary affirmative covenants, negative covenants, including financial covenants, and events of default.” *See* **C-032**, Westmoreland Coal Company, Current Report (Form 8-K), 16 December 2014. The agreement governing the Bridge Loan Facility contains similar covenants. *See* **C-039**, Westmoreland Coal Company, Current Report (Form 8-K), 21 May 2018, Ex. 10.1 § 9.

satisfied.<sup>49</sup> WMH suggests that these covenants indicate that the First Lien Lenders exercised control over WCC and its assets.<sup>50</sup>

23. Based upon my review of these covenants, the covenants described above are standard in transactions of the sort between sophisticated, third-party lenders and their commercial clients. While these covenants may have been intended to induce or disincentivize certain behavior from WCC, they did not confer upon the First Lien Lenders the ability to manage, or “control”, the operations of WCC and its affiliates or their assets. The First Lien Lenders’ remedies for a breach of these covenants include the ability to charge more interest<sup>51</sup> and the ability to seek to access the value of the collateral. Those remedies do not include the right or the power to take over WCC’s business or to change its corporate decisions.

### **C. The First Lien Lenders Themselves Characterized the Financings as Arm’s-Length**

24. My conclusion is confirmed by the First Lien Lenders’ own characterization of the financings. Specifically, the First Lien Lenders explicitly claimed that they were at arm’s-length to the WLB Debtors, and disclaimed “control” over the WLB Debtors through the financing arrangements. For example, the credit agreement governing the Term Loan Facility specifically states that:

The Borrower acknowledges and agrees that . . . the transactions contemplated by this Agreement and the other Credit Documents (including the exercise of rights and remedies hereunder and thereunder) are arm’s-length commercial transactions between the Lender Parties, on the one hand, and the Borrower, on the other.<sup>52</sup>

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<sup>49</sup> See **C-032**, Westmoreland Coal Company, Current Report (Form 8-K), 16 December 2014, Ex. 4.1 §§ 4.09-4.10.

<sup>50</sup> See *e.g.*, Counter-Memorial on Jurisdiction, ¶¶ 70-71; *see also generally* Counter-Memorial on Jurisdiction, Appendix A.

<sup>51</sup> See **C-032**, Westmoreland Coal Company, Current Report (Form 8-K), 16 December 2014, Ex. 4.3 § 2.08(b).

<sup>52</sup> **C-032**, Westmoreland Coal Company, Current Report (Form 8-K), 16 December 2014, Ex. 4.3 § 13.20 (where the Borrower refers to WCC and the Lender Parties refer to the First Lien Lenders and their affiliates); *see also* **C-039**, Westmoreland Coal Company, Current Report (Form 8-K), 21 May 2018, Ex. 10.1 § 13.20 (similar, but referring to WCC, Westmoreland San Juan Holdings, Inc, and Prairie as “each Borrower” and only a subset of the First Lien Lenders and their affiliates as Lender Parties).

25. The final order of the WCC Bankruptcy Court approving the DIP Facility further provides that:

None of the DIP Facility Agent, the DIP Lenders, or the Prepetition Secured Parties [i.e., the First Lien Lenders] controls the Debtors or their properties or operations, has authority to determine the manner in which any of the Debtors' operations are conducted or is a control person or insider of the Debtors or any of their affiliates by virtue of any of the actions taken with respect to, in connection with, related to, or arising from the Interim Order or this Final Order, the DIP Facility, the DIP Loan Documents, the Prepetition Facilities, and/or the Prepetition Financing Documents.<sup>53</sup>

26. Accordingly, the First Lien Lenders did not exercise "control" over the WLB Debtors in connection with the financing arrangements, and did not have any equity-type rights or any say in the day-to-day operations of the WLB Debtors, or Prairie in particular.

#### **D. The First Lien Lenders Did Not "Control" the WCC Bankruptcy Proceeding**

27. WMH also suggests that the WCC RSA "gave the Secured Creditors an effective right to control the bankruptcy process."<sup>54</sup> Parties to a restructuring support agreement (an "RSA") (other than the debtor) do not "control" the bankruptcy process. Indeed, the practice of entering into RSAs has developed precisely because the debtor-in-possession has exclusive control over the bankruptcy process.<sup>55</sup> As stated in the First Expert Report, an RSA is a contractual arrangement among the debtor and key creditors whereby the debtor agrees to use its control over the process in a specified way.<sup>56</sup> However, the debtor also has a fiduciary duty to maximize the value of its estate for the benefit of all stakeholders.<sup>57</sup> If someone offers the debtor a more advantageous path forward than the path agreed upon under the RSA, the debtor has a fiduciary duty to pursue the

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<sup>53</sup> **C-040**, Final DIP Order ¶ E(viii). The "Prepetition Facilities" include both of the financing arrangements signed on December 16, 2014, as well as the May 21, 2018 Bridge Loan Facility. **C-040**, Final DIP Order, ¶ E(iii) (defining "Prepetition Facilities" to include the Bridge Loan Facility, the Term Loan Facility and the Senior Secured Notes).

<sup>54</sup> See e.g., Counter-Memorial on Jurisdiction, Appendix A, ¶ 15.

<sup>55</sup> See **R-045**, 11 U.S.C., § 1107(a). Pursuant to section 1121(b) of the Bankruptcy Code, a chapter 11 debtor has the exclusive right to file a chapter 11 plan for the first 120 days after the commencement of the case. **R-045**, 11 U.S.C., § 1121(b).

<sup>56</sup> **RER-Coleman-Bankruptcy-Memorial on Jurisdiction** [First Report], ¶ 37.

<sup>57</sup> See **RER-Coleman-Bankruptcy-Memorial on Jurisdiction** [First Report], note 11 (defining "stakeholder" as "anyone with an interest or concern in the debtor's business, generally. Practically speaking, it means both a debtor's creditors and its shareholders.").

better deal. For this reason, virtually all RSAs contain a “fiduciary out” provision that permits the debtor to terminate the RSA in favor of the better alternative.<sup>58</sup> Thus, regardless of whether it has signed an RSA, the debtor retains ultimate decision-making authority over its bankruptcy process, subject to bankruptcy court approval. I therefore disagree with WMH’s suggestion that the First Lien Lenders “controlled” the WCC Bankruptcy Proceeding.

#### **E. The First Lien Lenders Did Not “Beneficially Own” WCC or WCC’s Assets**

28. Finally, WMH suggests this is a case where there is “no question as to beneficial as opposed to formal ownership.”<sup>59</sup> While WMH does not distinguish as to whether the First Lien Lenders purport to have held a “beneficial ownership” in WCC itself, or in the WLB Debtors’ assets, I address both propositions.

29. First, the mere fact that the First Lien Lenders lent WCC money is not equivalent to owning WCC. As discussed above, the concept underlying “beneficial ownership” is that, although someone else might own an asset, or more specifically an equity interest, in name, the true party in interest is someone else entirely, from whom all decision-making authority flows.<sup>60</sup> The First Lien Lenders were not entitled to step into the position of WCC’s public shareholders by virtue of providing debt financing to WCC. Thus, it is inaccurate to conclude that the First Lien Lenders “beneficially owned” WCC.

30. In addition, the First Lien Lenders’ security interest in substantially all of the assets of the WLB Debtors—including the equity interests in the Canadian Entities—granted in connection with the various financing arrangements did not amount to “beneficial ownership” of such assets (including the Canadian Entities). Rather, the First Lien Lenders’ lien merely afforded them the ability to foreclose on the assets—a right that is only exercisable in the event of an uncured breach of the obligations under the financing documents.<sup>61</sup> The First Lien Lenders’ status as lenders, not

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<sup>58</sup> See e.g., **R-050**, Westmoreland Coal Company, et al., Restructuring Support Agreement, Exhibit A to *Declaration of Jeffrey S. Stein in Support of Chapter 11 Petitions and First Day Pleadings* [Court Docket, Doc. 54], 9 October 2018 [Excerpt], §§ 8.01, 13.02(b).

<sup>59</sup> **CER-Paulsson-International Law-Counter-Memorial on Jurisdiction**, ¶ 70.

<sup>60</sup> See Section IV.A.3 above.

<sup>61</sup> Once the WLB Debtors commenced the WCC Bankruptcy Proceeding, the First Lien Lenders could not exercise their foreclosure right without first seeking leave of the WCC Bankruptcy Court due to the imposition of the automatic stay. See **RER-Coleman-Bankruptcy-Memorial on Jurisdiction** [First Report], ¶ 18.



owners, is underscored by the provisions of the WCC RSA setting up a sale of the collateral, with the First Lien Lenders as the stalking horse bidder, as part of the WCC Plan. Had the First Lien Lenders had ownership rights already as a result of their security interests, the sale process would have been unnecessary because the First Lien Lenders would already have owned the assets.

## V. OTHER U.S. LAW CONCEPTS

### A. Claims Trading

31. I was also asked to review WMH's statement that, "[i]t is common for U.S. bankruptcy courts to approve claims trading as a matter of U.S. bankruptcy law," and the cases it cites in support thereof.<sup>62</sup> WMH's discussion of "claims trading" is inapposite to the matter at hand. The first line of the decision cited in *ReGen Capital I, Inc. v. UAL Corp. (In re UAL Corp.)*, 635 F.3d 312 (7th Cir. 2010) states, "A claims trader buys claims *against bankruptcy debtors from creditors* at a discount."<sup>63</sup> The "NAFTA Claim," as defined in the Stalking Horse Purchase Agreement,<sup>64</sup> is not a claim *against* WCC and it was not purchased *from* the First Lien Lenders. In fact, the opposite is true: the "NAFTA Claim" was a WCC asset included in WCC's sale of assets to the First Lien Lenders in partial satisfaction of their outstanding debt.<sup>65</sup>

32. The other cases cited by WMH are similarly irrelevant. *ReGen Capital I, Inc. v. Halperin (In re U.S. Wireless Data, Inc.)*, 547 F.3d 484 (2d Cir. 2008) discusses a creditor's ability to file a claim against a debtor after missing applicable bar dates and failing to challenge the debtor's proposed cure amounts.<sup>66</sup> *Dorr Pump & Mfg. Co. v. Heath (In re Dorr Pump & Mfg. Co.)*, 125 F.2d 610 (7th Cir. 1942), in addition to being almost eighty years old and decided decades before the currently-effective Bankruptcy Code was enacted, holds that certain "wage earners" were

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<sup>62</sup> Counter-Memorial on Jurisdiction, note 110.

<sup>63</sup> See **CLA-024**, *ReGen Capital I, Inc. v. UAL Corp. (In re UAL Corp.)*, 635 F.3d 312, 314 (7th Cir. 2011) (emphasis added).

<sup>64</sup> See **RER-Coleman-Bankruptcy-Memorial on Jurisdiction [First Report]**, ¶ 68; **R-053**, Stalking Horse Purchase Agreement § 1 (defining the "NAFTA Claim" as "that certain claim filed with the Office of the Deputy Attorney General of Canada on November 19, 2018 by Westmoreland on its own behalf and on behalf of its Canadian Subsidiary Prairie Mines & Royalty ULC against the Government of Canada pursuant to chapter 11 of the North American Free Trade Agreement (as such claim may be amended).").

<sup>65</sup> See **RER-Coleman-Bankruptcy-Memorial on Jurisdiction [First Report]**, ¶ 68.

<sup>66</sup> See **CLA-025**, *ReGen Capital I, Inc. v. Halperin (In re U.S. Wireless Data, Inc.)*, 547 F.3d 484, 492-96 (2d Cir. 2008).

permitted to assign their claims for wages against the debtor company to third parties, namely, certain stockholders of the bankrupt company.<sup>67</sup> None of these cases speaks to a debtor's ability to transfer its own claims to third parties. However, as stated in the First Expert Report, a debtor in bankruptcy is permitted to assign, or sell, its legal rights to increase value for creditors, *so long as the assignment is permitted under applicable non-bankruptcy law*.<sup>68</sup>

## **B. Type G Reorganizations**

33. Finally, I was asked to comment on the following sentence from WMH's Counter-Memorial on Jurisdiction: "The transaction was structured in this way to qualify as a 'Type G' reorganization, by which an entity may restructure tax-free."<sup>69</sup> I do not opine as to what tax advantages would or would not be gained from structuring the transaction as outlined in my First Expert Report.<sup>70</sup> However, I note that the determination of whether WMH may qualify for certain tax benefits vis-à-vis its acquisition of WCC's assets is a distinct inquiry from a determination of whether WMH was an unrelated, third-party purchaser of WCC's assets, as the WCC Bankruptcy Court found in the WCC Plan Confirmation Order.<sup>71</sup>

## **VI. RESERVATION OF RIGHTS**

34. My opinions herein are based solely on the information available and work performed through the date of this report. I reserve the right to supplement my opinion should further information be produced, and to respond to any expert opinions offered by, or on behalf of, the parties to this matter. My testimony may also supplement this report. This report is therefore subject to change or modification and should additional relevant information become available that bears on the analyses, opinions, or conclusions contained herein.

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<sup>67</sup> See **CLA-026**, *Dorr Pump & Mfg. Co. v. Heath (In re Dorr Pump & Mfg. Co.)*, 125 F.2d 610, 611 (7th Cir. 1942).

<sup>68</sup> See **RER-Coleman-Bankruptcy-Memorial on Jurisdiction** [First Report], ¶¶ 86-88.

<sup>69</sup> Counter-Memorial on Jurisdiction, Appendix A, ¶ 41.

<sup>70</sup> See **RER-Coleman-Bankruptcy-Memorial on Jurisdiction** [First Report], ¶¶ 73-82.

<sup>71</sup> See **RER-Coleman-Bankruptcy-Memorial on Jurisdiction** [First Report], ¶ 72(c).

I declare that the statements and opinions contained in this report are true and correct to the best of my knowledge and belief.

Dated: April 9, 2021  
New York, New York



Kathryn A. Coleman