Court File No. CV-16-11257-00CL

ONTARIO
SUPERIOR COURT OF JUSTICE
(COMMERCIAL LIST)

IN THE MATTER OF THE *COMPANIES' CREDITORS ARRANGEMENT ACT*, R.S.C. 1985, C. C-36, AS AMENDED

AND IN THE MATTER OF A PLAN OF COMPROMISE OR ARRANGMENT OF PRIMUS TELECOMMUNICATIONS CANADA INC., PRIMUS TELECOMMUNICATIONS, INC. AND LINGO, INC.

BOOK OF AUTHORITIES OF THE PURCHASER (BIRCH COMMUNICATIONS INC.)

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DEBTORS AND CREDITORS SHARING THE BURDEN:

A Review of the *Bankruptcy and Insolvency Act* and the *Companies' Creditors Arrangement Act*

Report of the Standing Senate
Committee on Banking, Trade and Commerce

Chair
The Honourable Richard H. Kroft

Deputy Chair
The Honourable David Tkachuk

November 2003

J. Executory Contracts

Executory contracts are contracts under which something remains to be done by one or more of the parties to the contract. In essence, it is a contract where there are obligations yet to be completed. Examples include leases, intellectual property rights and employment contracts, among others. Neither the BIA nor the CCAA uses the expression "executory contract."

... the existence of [executory] these contracts in a situation of insolvency raises the question of the extent to which these private contracts – negotiated in good faith and with due consideration of risk – should be altered or terminated, under what circumstances and by whom.

Nevertheless, the existence of these contracts in a situation of insolvency raises the question of the extent to which these private contracts – negotiated in good faith and with due consideration of risk – should be altered or terminated, under what circumstances and by whom. Alteration or termination of contractual rights change expectations, reduce predictability in contracting and increase risks, which will have negative implications. As well, both contracting parties may experience harm, since the continuation of a contract may be in the best interest of both parties.

Canadian legislation in this area has existed for some time. The *Bankruptcy Act* passed in 1949 contained few restraints on completed contracts; as well, it explicitly recognized the applicability of provincial/territorial law to real estate leases. Various omnibus bills in the 1970s and 1980s, all of which died on the Order Paper, proposed that an insolvent person who wished to make a proposal could disclaim any executory contract, and the co-contracting party would have the right to file a claim in the proposal for damages; the insolvent company could continue as a going concern, while the co-contracting party to the disclaimed contract would be no worse off than if a bankruptcy had occurred.

Amendments to the BIA in 1992 provide that, after a reorganization begins, secured creditors cannot exercise their security; the termination of a lease, licensing agreement or public utility because of default was also prevented. Debtors, however, were given the ability to disclaim leases on real property.

Witnesses presented the Committee with divergent opinions on whether disclaimer of executory contracts should be allowed, with the Court's permission, by insolvency practitioners or by co-contracting parties. Some witnesses told us that a company involved in a reorganization should be permitted to renounce such contracts. This view was held, for example, by Mr. Mendelsohn, who told the Committee – in reference to the CCAA – that "reorganizing entities [do and should] have the ability to renounce executory contracts, ... with appropriate judicial supervision." After noting that, under the BIA, only commercial leases of real estate where the reorganizing entity is the lessee can be renounced, he argued that a coherent system of restructuring must permit the entity to renounce other executory contracts as well. He informed us that "[i]f executory contracts have to be renounced, they have to be renounced whether .... [the] company [is big or small]."

Mr. Mendelsohn also shared the view that a bankruptcy trustee should be able to assign and transfer executory contracts to third parties, including licensing arrangements and leases of premises. He believed that "a trustee in bankruptcy should be given the right to realize, for the benefit of creditors, whatever economic value resides in the assets, including executory contract assets."

The Joint Task Force on Business Insolvency Law Reform also spoke about the ability to disclaim executory contracts and assignment to third parties. In the Joint Task Force's opinion, "[t]here should be a general right to disclaim (reject) executory contracts (including real property leases) in all bankruptcy and reorganization proceedings." Although it does not believe that insolvent organizations or the trustee in bankruptcy should require Court approval in order to disclaim these contracts existing at the date of commencement of proceedings, the Joint Task Force argued that "the legislation could impose some pre-conditions to the exercise of the disclaimer power either generally, or with respect to certain types of contracts."

Regarding the ability to assign executory contracts, the Joint Task Force informed the Committee that "trustees in

bankruptcy and court-appointed receivers should have the power to assign executory contacts (not including eligible financial contracts) both in connection with going concern transactions and on a liquidation basis," subject to a number of limitations. It went on to note, however, that "[t]here should be provision for the court to prohibit an assignment if [the non-bankrupt party to the contract] establishes that the proposed assignee does not meet, in a material way, criteria reasonably applied by [it] before entering into similar agreements ... or the proposed assignee is less creditworthy than [the bankrupt] was when the executory contract was entered into and reasonable assurances of payment have not been provided with respect to any credit required to be extended to the assignee by [the non-bankrupt party] under the executory contract after the assignment."

The Canadian Bankers Association, however, told the Committee that "[i]nsolvency law constraints on contracts can affect pre-insolvency contracting behaviour and may reduce credit availability. The new economy dictates that companies must be innovative and dynamic. In order to finance such new enterprises, financiers must be able to rely on the negotiated terms of their contracts."

A particular executory contract – a collective agreement – was discussed by several witnesses, including representatives of organized labour. In general, their view is that the Court should not be able to terminate a collective agreement, in whole or in part. The CAW-Canada told the Committee that "the CCAA offers no authority to a Court to abrogate a collective agreement. Nor should it do so. Still, some counsel and commentators believe that Superior Courts in Canada have an 'inherent jurisdiction' to issue an order pursuant to the CCAA which suspends or temporarily cancels one or more terms of a collective agreement. We fundamentally disagree."

A particular executory contract – a collective agreement – was discussed by several witnesses, including representatives of organized labour.

In the union's opinion, "[t]here can be no dispute that if the preservation of the status quo is a key objective of the CCAA, then the terms and conditions of employment defined in a collective agreement at the time of the issuance of a CCAA order must be maintained subject to the parties' mutual authority to negotiate changes." From this perspective, the

CAW-Canada told the Committee that "[t]he CCAA should … make clear that it is not open to a Court, in exercising its 'inherent jurisdiction' to alter, waive, or override the provisions of a collective agreement without the consent of the employer and the relevant trade union."

A similar view was presented to the Committee by the United Steelworkers of America, which told us that "the Courts should not be entitled, under the guise of a CCAA proceeding, to interfere with the operation of freely negotiated collective agreements which affect the rights of many workers. … [U]nions have demonstrated, in times of legitimate economic crisis, that they are capable of acting responsibly and in the best interests of their membership to agree to amendments to a collective agreement which may be necessary to enable the employer to survive. This cooperative approach is to be preferred to an approach which would eliminate workers (sic) rights with the stroke of a pen and subvert the primacy of collective bargaining."

Moreover, the Canadian Labour Congress differentiated collective agreements from other executory contracts, and indicated to the Committee that "[j]ust as employees are not like other creditors, collective agreements are not like other contracts. … [T]he bankruptcy and CCAA courts should not be accorded any jurisdiction over collective bargaining agreements. … Unlike other creditors, workers are not in a position to negotiate the terms upon which they may become creditors of their employer. Unlike other creditors, they are not in a position to assess the risks that they are required to bear. Unlike other creditors, they are not able to guarantee their employer's obligation by way of a secured charge. And unlike senior executives, they are not in a position to have their termination entitlements, including golden parachutes, set aside in trust accounts and thereby protected from bankruptcy proceedings."

The labour federation also informed the Committee that it does not support disclaimer of collective agreements. In its view, "[t]he debtor company and the union are in the best

position to evaluate the needs of the company and are also the parties with the greatest interest in preserving the company as a going concern; they are, therefore, the appropriate parties to determine any changes to the collective agreement. The key incentive for the parties to reach an agreement is the threat that a failure to do so will lead to the bankruptcy of the debtor. ... Neither the courts nor the monitor or receiver should have the power to vacate or amend a collective bargaining agreement that was arrived at within the provincial or federal statutory framework." The Canadian Labour Congress, however, went farther, and argued that "the value of each concession should be assigned unsecured creditor status with no less priority of valuation than any other unsecured creditor."

In support of the views of organized labour, Professor Sara commented that "treating collective agreements as commercial executory contracts that can be unilaterally set aside ... is highly problematic."

From the perspective of intellectual property rights, the Intellectual Property Institute of Canada indicated its preference for an approach that would limit the right of disclaimer to "unprofitable," rather than "executory," contracts, since there is "too much uncertainty as to what types of agreements would be found to be 'executory'." The Institute also made other suggestions for change.

[The Committee received testimony] with respect to patents, trademarks and trade secrets.

For example, the Institute recommended that: the time limit for the exercise of the right of disclaimer be three months; the Court have the discretion to maintain the contract if the disclaimer would cause undue hardship not compensable in damages; the Court be permitted to make an order discharging the agreement and ordering payment for damages for non-performance by the trustee; aggrieved persons be given the status of a creditor of the bankrupt, to the extent of any loss suffered by reason of the disclaimer; and, where the bankrupt is a licensor of intellectual property rights, the licensee have the right to elect – within one month after receipt of the notice of disclaimer – to retain the licence. Recommendations were also made by it with respect to patents, trademarks and trade secrets.

... we urge relevant parties to engage in the discussion needed to ensure a satisfactory resolution to the full range of issues identified to us by the Intellectual Property Institute of Canada.

Similarly, Mr. Baird, Q.C., spoke to the Committee about intellectual property issues and noted the debate that has existed for some years about "whether a trustee in bankruptcy or a bankrupt licensor or a debtor under the protection of the CCAA has the right to repudiate licences issued by the bankrupt or the insolvent debtor." In supporting a recommendation made by the Insolvency Institute of Canada, he said that "the BIA and the CCAA [should] be amended to provide protection for a licensee of a right to intellectual property similar to that provided in the United States."

The Writers' Union of Canada also commented on copyright, noting the absence of copyright issues in the CCAA and the extent to which "the *Bankruptcy and Insolvency Act* less frequently applies – or doesn't apply initially. ... When [it] does apply, it provides writers with very limited protection and often too late. A receiver or trustee in bankruptcy may already have assigned his or her rights and sold the inventory, short circuiting a possible statutory reversion of rights, depriving the author of possible revenues from sales by the trustee, and interfering with the author's future opportunities for republication." It also recommended that a trustee not be permitted to transfer or assign the copyright, or any interest in it, since the relationship between a writer and his or her publisher is personal; the writer should be permitted to make any alternative arrangements in the event of his or her publisher's insolvency. Finally, the Union commented that there is a lack of clarity about whether a publishing agreement is a partial assignment of copyright or a licensing agreement under which the author retains the copyright.

While we believe that there are a variety of unresolved issues related to the insolvency of a licensor or a licensee in the context of an intellectual property licence, intellectual property law is a highly specialized area and we feel that the limited examination given by the Committee to this particular aspect of insolvency does not enable us to make any meaningful recommendations for change. Nevertheless, we urge relevant parties to engage in the discussion needed to ensure a satisfactory resolution to the full range of issues identified to us by the Intellectual Property Institute of Canada.

More generally, the Committee supports the concept of permitting disclaimer of all executory contracts, since we believe that the flexibility to take this action increases the probability of successful reorganization and thereby – in some sense – a fresher, if not fresh, start for the business. We also feel, however, that the parties to executory contracts should meet in good faith with a view to negotiating mutually acceptable changes to their contract that would enable them to meet their goals and permit the contract to continue, albeit in a changed form. We strongly believe that, in most cases, the parties will be able to come to a successful resolution; however, it is likely that situations will arise in which the parties cannot reach agreement, and in these cases we believe that disclaimer should be permitted by the Court. Nevertheless, disclaimer should only be allowed where certain conditions are met, including good faith attempts to negotiate mutually acceptable changes to the contract and serious hardship in restructuring without the disclaimer. Believing that this approach would enhance fairness, predictability and effectiveness, the Committee recommends that:

... the Committee supports the concept of permitting disclaimer of all executory contracts, since we believe that the flexibility to take this action increases the probability of successful reorganization and thereby – in some sense – a fresh, if not fresher, start for the business.

The *Bankruptcy and Insolvency Act* and the *Companies' Creditors Arrangement Act* be amended to permit disclaimer of executory contracts in existence on the date of commencement of proceedings under the Acts. This disclaimer should apply to all executory contracts, provided a number of conditions are met. In particular: the debtor should be obliged to establish inability or serious hardship in restructuring the enterprise without the disclaimer; the co-contracting party should be permitted to file a claim in damages in the restructuring; and, where a collective agreement is being disclaimed, the debtor should also have the burden of establishing that post-filing negotiations have been carried on, in good faith, for relief of too onerous aspects of the collective agreement and should establish in Court that the disclaimer is necessary in order to allow for a viable restructuring.

Moreover, the Committee is of the view that trustees, Court-appointed receivers and monitors should be able to assign executory contracts where doing so would enhance the value of the assets and, thereby, moneys available for

distribution to creditors. We recognize that while this circumstance would not permit the co-contracting party to choose its commercial partner, we feel that if the co-contracting party is no worse off financially, it would suffer no prejudice. As well, efficiency and effectiveness – two principles that we believe should characterize our insolvency system – would be enhanced. From this perspective, the Committee recommends that:

The *Bankruptcy and Insolvency Act* and the *Companies' Creditors Arrangement Act* be amended to permit trustees, Court-appointed receivers and monitors, if authorized by judgment, to assign executory contracts when appropriate, in connection with going concern transactions and on a liquidation basis, provided that two conditions are met: the proposed assignee is at least as credit worthy as the debtor was at the time the contract was entered into; and the proposed assignee agrees to compensate the other party for pecuniary loss resulting from the default by the debtor or give adequate assurance of prompt compensation.

2

Case Name:

Extreme Retail (Canada) Inc. v. Bank of Montreal

IN THE MATTER OF the Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36, as amended
IN THE MATTER OF a Plan of Compromise or Arrangement of Denninghouse Inc. and the Other Companies listed in Schedule "A" (Applicants)
RE: Extreme Retail (Canada) Inc. and Buck or Two (2004) Inc. (Moving Parties), and
Bank of Montreal (Responding Parties)

[2007] O.J. No. 3304

37 C.B.R. (5th) 90

2007 CarswellOnt 5520

12 P.P.S.A.C. (3d) 26

Court File No. 04-CL-005523

Ontario Superior Court of Justice
Commercial List

D.G. Stinson J.

Heard: August 3, 2007.
Judgment: September 5, 2007.

(23 paras.)

Corporations and associations law -- Conditions and warranties -- Purchaser of assets of insolvent corporation took assets free and clear of interests of Bank -- Bank participated in approval of purchase and provided letter of comfort to purchaser waiving its rights with respect to assets purchased.

Insolvency law -- Creditors -- Secured creditors -- Purchaser of assets of insolvent corporation took assets free and clear of interests of Bank -- Bank participated in approval of purchase and provided letter of comfort to purchaser waiving its rights with respect to assets purchased.

Insolvency law -- Proposals -- Court approval -- Purchaser of assets of insolvent corporation took assets free and clear of interests of Bank -- Bank participated in approval of purchase and provided letter of comfort to purchaser waiving its

rights with respect to assets purchased.

Motion by Extreme for interpretation of approval and vesting order -- Denninghouse and subsidiaries operated discount retail stores -- Most stores operated as franchises pursuant to agreements between subsidiary ABOT and franchisees -- ABOT had general security agreements over assets of franchisees -- Principal lender to group of companies was Bank of Montreal -- Bank also provided financing to franchisees, and also received general security agreements from franchisees -- Denninghouse provided Bank with Letter of Comfort and Inventory Buy-Back Agreements and Subordination Agreements with respect to each franchisee -- Under Subordinate Agreements, Denninghouse agreed to cause it subsidiaries, including ABOT, to subordinate their rights against assets of franchisees to rights of Bank -- Denninghouse failed to have ABOT execute such agreements -- Both Bank and ABOT registered their general security agreements -- Seven cases where ABOT did this first -- Denninghouse sought CCAA protection in August 2004 -- Monitor sought proposals for purchase of Denninghouse group assets, including franchise agreements and ABOT general security agreements -- Monitor and Denninghouse entered into agreement with Extreme for sale of these assets -- Sale approved by court and implemented in December 2004 -- Bank present in court when approval order issued -- Extreme paid consideration required and became owner of assets -- As part of closing, Bank provided Extreme with comfort letter, waiving rights against Denninghouse -- In 2006, two franchisees encountered financial problems and had assets liquidated -- Extreme and Bank disputed who was entitled to priority over proceeds of realization -- Both registrations of general security agreements by Bank in these cases came after ABOT general security agreement were registered -- Extreme claimed priority over Bank's position, because of date of registration of ABOT agreements and because ABOT never executed Subordination Agreements -- Argued it acquired agreements free and clear of prior rights, and argued Bank's comfort letter precluded Bank from disputing Extreme's priority -- Bank argued Denninghouse bound ABOT and signed Subordination Agreements as agent for ABOT, because Denninghouse owned 100 percent of ABOT -- Bank Alternatively asserted oral subordination agreement existed between ABOT and Bank -- Bank claimed approval order did not deprive Bank of priority in relation to Bank's general security agreements -- Claimed its comfort letter was not intended to waive Bank's rights under its separate security agreements -- HELD: Motion allowed -- Dispute governed by plain language of approval order -- Language made it clear Extreme acquired assets not subject to any higher rights -- Any interests of Bank deleted by order -- Bank had ample opportunity to raise issues of its priority over ABOT general security agreements prior to issuance of order -- Extreme had priority over Bank's general security agreements.

Statutes, Regulations and Rules Cited:

Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36

Counsel:

Robert C. Harason, for the moving parties.

Harvey G. Chaiton, for the responding parties.

ENDORSEMENT

1 D.G. STINSON J.:-- This motion involves a dispute concerning the effect of a vesting order made in connection with the sale of certain assets during the course of this CCAA proceeding.

2 Prior to this CCAA proceeding, Denninghouse Inc. and its subsidiaries (the "Denninghouse Group") were in the business of operating a cross-Canada chain of discount retail stores or so-called dollar stores, principally under the name

of "A Buck or Two" stores. The principal lender to Denninghouse Group was the Bank of Montreal ("BMO").

3 Most of the "Buck or Two" stores were operated by franchisees, pursuant to franchise agreements between ABOT Franchise Inc. ("ABOT") as franchisor and the individual store operators as franchisees. ABOT was a subsidiary of Denninghouse Inc. Among other things, ABOT supplied inventory to the franchisees on credit terms. To secure its position, ABOT sought and received general security agreements ("GSAs") over the franchisees' assets (the "ABOT GSAs").

4 In addition to providing financing to the Denninghouse Group, BMO also provided financing directly to individual "Buck or Two" franchisees, pursuant to a franchisee financing plan arranged with BMO by representatives of Denninghouse Group. Pursuant to that plan, BMO also was to receive GSAs from the franchisees, in order to secure its lending to them (the "BMO GSAs"). Also as part of the plan, Denninghouse Inc. (the parent company) provided to BMO two signed agreements in relation to each franchisee financed by BMO, being a Letter of Comfort and Inventory Buy-Back Agreement, and a Subordination Agreement.

5 Significantly, although ABOT was the corporation that had the direct franchisor-franchisee relationship with the franchisees, the Letters of Comfort and Inventory Buy-Back Agreements and the Subordination Agreements were in the name of and signed by Denninghouse Inc. alone. In those documents, Denninghouse Inc. agreed to postpone to BMO's security, all security or other interests that it had over the franchisees or their property. Moreover, in the Subordination Agreements, Denninghouse Inc. agreed to cause its subsidiaries (which included ABOT) to subordinate their rights against the assets of the franchisees, to the rights of BMO. As events unfolded, however, Denninghouse Inc. never caused ABOT to do so and no separate Letters of Comfort and Inventory Buy Back Agreements or Subordination Agreements were ever executed by ABOT in favour of BMO.

6 ABOT registered the ABOT GSAs under the relevant *Personal Property Security Act* ("PPSA") regimes in the provinces in which the franchisees' stores were located. BMO did the same. In a total of seven instances, ABOT's PPSA registrations for the ABOT GSAs of particular franchisees pre-dated those of the BMO GSAs for the same franchisees.

7 On August 16, 2004, the Denninghouse Group sought and obtained an order declaring themselves subject to the CCAA ("the Initial Order"). BMO was among the parties represented in court when the Initial Order was made. The Initial Order appointed RSM Richter Inc. to act as Monitor.

8 Following the Initial Order, proposals were sought for the purchase of various of the assets of the Denninghouse Group, including the franchise agreements and the ABOT GSAs. In due course, the Monitor and the Denninghouse Group entered into an agreement of purchase and sale with the moving parties, Extreme Retail (Canada) Inc. and Buck or Two (2004) Inc. ("Extreme"). The sale to Extreme was approved by the court and implemented by means of an order dated December 7, 2004 (the "Approval and Vesting Order"). Extreme paid the consideration contemplated by the agreement of purchase and sale and, pursuant to the Approval and Vesting Order, became the owner of the assets, including the franchise agreements and the ABOT GSAs.

9 Significantly, BMO was one of the parties represented in court when the Approval and Vesting Order was granted.

10 The operative provision of the Approval and Vesting Order that effected the conveyance and transfer of ownership to Extreme, provided that the assets (including the ABOT GSAs) "... are vested in Extreme ... absolutely and forever, free and clear of and from any and all right, title and interest of the applicants [the Denninghouse Group] and of any, security interests, charges, pledges, mortgages, ... adverse claims, ... disputes, ... limitations or restrictions, ... charges, encumbrances, or any other rights, ... whether contractual, statutory, by operation of law or otherwise, whether secured, unsecured or otherwise ..."

11 In addition, as part of the closing of the sale transaction, BMO provided to Extreme a comfort letter dated December 10, 2004, that provided as follows:

> ... please accept this letter as confirmation that [BMO] hereby waives any rights it may have to pursue [Extreme] for enforcement and collection of any monies arising from and pursuant to the terms of any inventory buy-back agreements, guarantees or security provided by and executed in favour of [BMO] by the Denninghouse Group given in respect of any indebtedness of a franchisee.

12 In 2006, well after the sale and the Approval and Vesting Order, two Buck or Two franchisees in the Province of Alberta encountered financial problems. Their assets were liquidated. A dispute then arose between Extreme and BMO as to which of them was entitled to priority over the proceeds of realization. The franchise agreements and ABOT GSAs for those franchisees were part of the assets purchased by Extreme from ABOT. BMO also held BMO GSAs in relation to the assets of these franchisees. The PPSA registrations of the BMO GSAs, however, were subsequent to the registrations of the ABOT GSAs. Both franchisees were indebted to each of Extreme and BMO. By agreement of the parties, the funds have been held in trust, to be released by agreement or by court determination as to which of Extreme or BMO is entitled thereto.

13 In addition to their dispute concerning the proceeds of realization of the two Alberta franchisees mentioned above, the parties have determined that there are five other franchisee relationships, some in Alberta and some in Ontario, in relation to which the ABOT GSAs in relation to those franchisees were registered under the relevant PPSA regime prior to the registration of the BMO GSAs for the same franchisees. Extreme has therefore asked the court to declare the rights of the parties in relation to those franchisee GSAs, as well as in relation to the proceeds of realization that remain held in trust.

14 Extreme claims priority over the position of BMO by reason of the fact that the ABOT GSAs acquired by it pursuant to the Approval and Vesting Order were registered in priority to the BMO GSAs given by the franchisees to BMO. Extreme argues that ABOT never agreed to subordinate its position nor did it enter into any Subordination Agreements with BMO. Extreme further argues that it acquired the GSAs free and clear of any prior rights, pursuant to the Approval and Vesting Order. Finally, Extreme argues that the comfort letter signed by BMO as part of the sale transaction precludes BMO from disputing Extreme's priority.

15 BMO argues that the agreements signed by Denninghouse Inc. with BMO bound ABOT, since Denninghouse Inc. was the 100 percent shareholder of ABOT. BMO further argues that Denninghouse Inc. signed the Subordination Agreements on behalf of ABOT as its agent. In the alternative, BMO asserts that there was an oral subordination agreement between ABOT and BMO. The end result, asserts BMO, is that the ABOT GSAs acquired by Extreme rank in priority after the BMO GSAs, despite their prior registrations under the relevant PPSAs. BMO further argues that the Approval and Vesting Order was never intended to deprive BMO of its priority in relation to the BMO GSAs obtained by it in exchange for financing the franchisees, which was a separate lending arrangement, independent of the financing provided by BMO to the Denninghouse Group. Those arrangements, BMO agrees, were not intended to be affected by the CCAA proceedings, or the Approval and Vesting Order. Lastly, BMO argues that the December 10, 2004 comfort letter provided by it was also not intended to waive any of BMO's rights under its separate security over the assets of the franchisees, but merely to assure Extreme that BMO would not enforce the inventory buy-back obligations of ABOT against Extreme.

16 In support of its position, BMO relies on the rule 39.03 examination of a former Denninghouse Group executive, William Thomas. On his examination, Mr. Thomas gave evidence about the history of the relationship between BMO and the Denninghouse Group, the franchisee financing plan, and the Letter of Comfort and Inventory Buy-Back Agreements and Subordination Agreements between BMO and Denninghouse Inc. Mr. Thomas also gave evidence about the intention of the parties to those agreements, to the effect that it was intended all along that the ABOT GSAs would be subordinated to the BMO GSAs. Counsel for Extreme objects to the admissibility of this evidence, arguing that it amounts to extrinsic evidence of intention, while the agreements themselves were unambiguous. By reason of the conclusion that I have reached as set out below, I find it unnecessary to deal with this argument. I also find it unnecessary to deal with the Extreme argument concerning the scope and intent of the December 10, 2004 BMO

comfort letter.

17 In my view, this dispute is governed by the plain language of the Approval and Vesting Order relating to the terms upon which Extreme acquired the assets that it purchased. I have earlier quoted the operative provision of that order. In my view, that language makes it plain that the assets that Extreme acquired were not subject to any higher rights. In this respect, the language of the order is unambiguous and far-reaching. Accordingly, assuming that there had existed an enforceable subordination agreement as between ABOT and BMO in relation to the ABOT GSAs, and assuming that BMO's rights ranked ahead of ABOT's rights, that higher BMO security interest was a right or encumbrance that was deleted by the Approval and Vesting Order.

18 As I have noted above, BMO argues that the Approval and Vesting Order was never intended to have such an effect. As I have also noted, however, BMO was a party to the proceedings, was represented in court when the Approval and Vesting Order was granted, and even provided a comfort letter in order to fulfill one of the conditions for the closing of the sale transaction. I also note that BMO was one of the parties that benefited from the completion of that transaction, as the principal secured creditor of the Denninghouse Group. BMO had ample opportunity to raise the issues of its claimed priority over the ABOT GSAs, and it could have sought to have a suitable limiting provision inserted in the Approval and Vesting Order. It failed to do so.

19 For its part, Extreme was a third party purchaser that was a stranger to the dealings between BMO and the Denninghouse Group. Counsel for BMO points out that Extreme has not taken the position that it was a *bona fide* purchaser for value without notice, and that Extreme had the opportunity to uncover the details of the Subordination Agreements between BMO and the Denninghouse Group prior to closing. Counsel for Extreme concedes that it may well be that the Subordination Agreements between Denninghouse Inc. and BMO were part of the documentation contained in the material made available to prospective purchasers of the assets of the Denninghouse Group. He notes, however, that there is no evidence that Extreme was actually aware of the alleged Subordination Agreements between ABOT and BMO. In any event, he argues, Extreme was entitled to rely on the unequivocal terms of the court order approving the transaction.

20 In my view, it is neither appropriate nor desirable to, in effect, open up and revisit the terms of a vesting order, especially one given two and a half years ago, and upon which parties have subsequently acted and conducted their affairs. It is impossible to say what would have occurred as the parties were negotiating the sale agreement, had the issue of BMO's claimed priority been raised at the time. I am not prepared to speculate that it would have been a matter of no moment: Extreme negotiated for and acquired the assets on the terms set out in the sale agreement and the Approval and Vesting Order. The assets were to be acquired free and clear. BMO was aware of this. BMO failed to protect its claimed position.

21 To paraphrase Cumming J. in *Air Canada Pilots Assn. v. Air Canada Ace Aviation Holdings Inc. et al.* (2007), 26 B.L.R. (4th) 124, [2007] O.J. No. 89 (S.C.J.), at para. 43, BMO is bound by the Approval and Vesting Order and cannot seek to vary or amend it. As Cumming J. went on to observe (at para. 44):

> The matters resolved by the CCAA Plan and Sanction Order are *res judicata* through issue and/or cause of action estoppel. The doctrine of *res judicata* prevents relitigation of matters which have already been determined by a court of competent jurisdiction.

In the present case, the Approval and Vesting Order was a final judicial determination of the rights of the parties represented in that proceeding in respect of the assets that were the subject of the sale. The CCAA objective of providing a mechanism for the efficient restructuring of corporations that encounter financial difficulty would be seriously undermined if parties who failed to assert or protect their rights at the time of the restructuring were permitted subsequently to return to court to undo past transactions. Such an approach should be discouraged.

22 I therefore conclude that, in relation to the seven ABOT GSAs that are the subject of this application, Extreme has

priority over the BMO GSAs.

23 In relation to costs, counsel have agreed that the successful party should be awarded $31,250. I therefore order BMO to pay that amount to Extreme.

D.G. STINSON J.

[Editor's note: Schedule "A" was not included in the copy received from the Court and therefore is not included in the judgment]

3

Case Name:

Allen-Vanguard Corp. (Re)

**IN THE MATTER OF the Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36, as amended
AND IN THE MATTER OF a Plan of Arrangement and Reorganization of Allen-Vanguard Corporation under the Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36, as amended and Section 186 of the Ontario Business Corporations Act., R.S.O. 1990, c. B.16, as amended, Applicants**

[2011] O.J. No. 3946

2011 ONSC 5017

81 C.B.R. (5th) 270

2011 CarswellOnt 8984

Court File No. CV-09-00008502-00CL

Ontario Superior Court of Justice
Commercial List

C.L. Campbell J.

Heard: November 16, 2010.
Judgment: August 25, 2011.

(113 paras.)

Bankruptcy and insolvency law -- Companies' Creditors Arrangement Act (CCAA) matters -- Compromises and arrangements -- Sanction by court -- Motions by directors, officers and underwriters to enjoin actions allowed -- Cross-motion by plaintiffs to vary Sanction Order dismissed -- Initial Order stayed Laneville action against corporation, which plaintiffs sought to continue against directors -- Love action against directors, officers and underwriters claimed negligence and failure to disclose transactions -- Sanction Order permitted only claims contemplated by s. 5.1(2) of CCAA, which these were not -- Plaintiffs could not claim against directors for acts undertaken in Corporation's name prior to initial order -- Release deprived underwriters of indemnity and plaintiffs never sought leave for derivative action -- Sanction Order was relied on by parties.

Bankruptcy and insolvency law -- Proceedings -- Practice and procedure -- Stays -- Of concurrent proceedings -- Motions by directors, officers and underwriters to enjoin actions allowed -- Cross-motion by plaintiffs to vary Sanction

Order dismissed -- Initial Order stayed Laneville action against corporation, which plaintiffs sought to continue against directors -- Love action against directors, officers and underwriters claimed negligence and failure to disclose transactions -- Sanction Order permitted only claims contemplated by s. 5.1(2) of CCAA, which these were not -- Plaintiffs could not claim against directors for acts undertaken in Corporation's name prior to initial order -- Release deprived underwriters of indemnity and plaintiffs never sought leave for derivative action -- Sanction Order was relied on by parties.

Corporations, partnerships and associations law -- Corporations -- Directors and officers -- Personal liability of directors to persons other than the corporation -- Joint and several liability -- Derivative actions -- Powers of court -- Conduct of the action -- Oppression remedy -- Stay, discontinuance, settlement or dismissal -- Motions by directors, officers and underwriters to enjoin actions allowed -- Cross-motion by plaintiffs to vary Sanction Order dismissed -- Initial Order stayed Laneville action against corporation, which plaintiffs sought to continue against directors -- Love action against directors, officers and underwriters claimed negligence and failure to disclose transactions -- Sanction Order permitted only claims contemplated by s. 5.1(2) of CCAA, which these were not -- Plaintiffs could not claim against directors for acts undertaken in Corporation's name prior to initial order -- Release deprived underwriters of indemnity and plaintiffs never sought leave for derivative action -- Sanction Order was relied on by parties.

Securities regulation -- Civil liability -- Misrepresentation in a prospectus -- Persons liable -- Underwriters -- Motions by directors, officers and underwriters to enjoin actions allowed -- Cross-motion by plaintiffs to vary Sanction Order dismissed -- Initial Order stayed Laneville action against corporation, which plaintiffs sought to continue against directors -- Love action against directors, officers and underwriters claimed negligence and failure to disclose transactions -- Sanction Order permitted only claims contemplated by s. 5.1(2) of CCAA, which these were not -- Plaintiffs could not claim against directors for acts undertaken in Corporation's name prior to initial order -- Release deprived underwriters of indemnity and plaintiffs never sought leave for derivative action -- Sanction Order was relied on by parties.

Motion by the former directors and officers of the Corporation to enforce the terms of the Sanction Order and enjoin the class actions against them. Motion by the underwriters to stay or dismiss the shareholder class action against them. Cross-motion by the plaintiffs to vary the Sanction Order to permit the proposed actions. The Initial Order was made in December 2009 and stayed the existing Laneville action against the corporation. 100 per cent of affected creditors voted in favour of the plan, which the Corporation would have been unable to carry on without, and the Sanction Order was made. In the Laneville action, the shareholders alleged the corporation, directors and officers were liable for negligence, misrepresentation and oppression. The plaintiffs sought to continue the Laneville action against the directors. After the Sanction Order was made, the Love action was commenced by shareholders against the directors, officers and Corporation's underwriters and claimed negligence and failure to disclose transactions.

HELD: Motions allowed. Cross-motion dismissed. The released contained in the Sanction Order clearly permitted only those claims against directors that were contemplated by s. 5.1(2). These claims were not the type of claims contemplated by s. 5.1(2). It would be inconsistent with the CCAA to allow the plaintiffs to proceed with their oppression claim against the directors for acts or omissions undertaken in the Corporation's name prior to the Initial Order being made. The plaintiffs did not oppose the Sanction Order, so took their chances that the order would permit their claim to proceed. Allowing the claim to proceed would permit an inappropriate sort of priority for unsecured creditors. The claims against the directors in both actions were enjoined. Protection for the underwriters was not discussed when the Sanction Order was approved, but s. 5.1(2) was to be read narrowly to ensure to objectives of the CCAA. Furthermore, s. 5.1(2) could not be used to create a cause of action that would otherwise require court approval and leave. The plaintiffs had plenty of opportunity to seek leave to commence a derivative action but never did. The terms of the release in the Sanction Order deprived the underwriters of any indemnity they would otherwise be entitled to from the Corporation. The claim against the underwriters was struck in negligence and misrepresentation. Had the plaintiffs claimed and provided full particulars of fraud, such a claim may have survived as the terms of the release did not extend to fraud. The plaintiffs' motion to vary the terms of the Sanction Order was dismissed. It would be

inappropriate to vary an order that was relied on by all parties and approved by all affected creditors.

Statutes, Regulations and Rules Cited:

Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36, s. 5.1(1), s. 5.1(2), s. 5.1(3)

Excise Tax Act, R.S.C. 1985, c. E-15,

Ontario Business Corporations Act, R.S.O. 1990, c. B.16, s. 131(1), s. 246(1)

Ontario Securities Act, s. 130, s. 138.3

Counsel:

Ronald G. Slaght, Q.C. and Eli S. Lederman for the Directors and Officers of Allen-Vanguard Corporation.

C. Scott Ritchie, Michael G. Robb and Daniel E.H. Bach for class action plaintiffs.

Alan L.W. D'Silva and Daniel S. Murdoch for Underwriters.

REASONS FOR DECISION

1 **C.L. CAMPBELL J.**:-- Two motions were heard together: the first by former directors and officers of Allen-Vanguard to enforce the terms of a Sanction Order, which the directors and officers say release them as well as Allen-Vanguard from all claims except those specifically provided for in section 5.1(2) of the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36, as amended (the "CCAA.") In addition, the former directors assert that the claims of the Plaintiffs in two proposed Class Actions are not sustainable against them in law under s. 5.1(2) of the CCAA.

2 The second motion by the Underwriters of Allen-Vanguard seeks to dismiss or stay the action brought against the Underwriters by shareholders in a proposed Class Action.

3 A cross-motion brought by Plaintiffs in the two proposed Class Actions seeks, if required, variation of the terms contained in the Sanction Order granted December 16, 2009, to permit the Class Actions to proceed.

4 By way of an endorsement dated February 9, 2011, the Court sought further information from the parties with respect to the factual circumstances that surrounded the agreement that was embodied in the terms of the Sanction Order. That information has been provided and will be referred to later in these Reasons.

5 The claims that the directors who are the moving parties seek to effectively enjoin are those brought in two Class Actions (hereinafter the "Laneville action" and the "Love action"), wherein former shareholders seek damages against directors, officers and Underwriters based on alleged misrepresentation to shareholders by the Defendants about the effect on Allen-Vanguard of its purchase of another company in 2007.

Background

6 As of December 2009, Allen-Vanguard was insolvent. An Application was made on December 9 for an Initial Order under the CCAA, appointment of a Monitor and a Plan Filing and Meeting Order. The effect of the Initial Order among other matters stayed the existing Class proceeding.

7 The circumstances that surrounded the Plan Filing/Meeting Order, the Court was advised, were necessary to avoid a bankruptcy. The subsequent vote on December 9, 2010 was approved in favour of the Plan by 100% of affected creditors.

8 The circumstances that surrounded the December 9, 2010 Application and Order were a variation on a CCAA process that has come to be known as a "pre-packaged" Application. The secured creditors agreed to a restructuring of their secured debt in circumstances involving a going concern sale of assets where, had a bankruptcy ensued, there would have been no recovery for creditors or shareholders beyond very incomplete recovery for those secured creditors.

9 The First Report of the then proposed Monitor, Deloitte and Touche, in support of the Initial Order, outlined the transaction that had been proposed to all creditors as early as September 2009, posted on SEDAR and to which (apart from the question of releases) no party was opposed on December 9.

10 The Plan provided for the Secured Lenders foregoing a portion of their existing debt and fees, converting the remainder of the existing debt into a multi-year restructured term loan with terms more favourable to the Company and a new revolving credit facility.

11 The Court accepted the opinion of Deloitte & Touche that without the proposed transaction, the Company would likely not be able to meet its financial obligations as they became due and would likely be unable to carry on the business beyond the very short-term, which would then necessitate liquidation.

12 The conclusion by Deloitte & Touche, accepted by the Court, was that the restructuring process in the Plan maximized the value of the Company for the benefit of all stakeholders and represented the best offer from that process.

13 The alternative faced by the Company was that of a forced liquidation, which as estimated by the Monitor would result in a shortfall to secured lenders in excess of $100 million.

The Laneville Action

14 The proposed Class Action Plaintiff in the Laneville action issued on October 9, 2009 a Statement of Claim dated November 26, 2009, which sought appointment on behalf of a Representative Plaintiff and for a class of Allen-Vanguard shareholders who allege that Allen-Vanguard Corporation and its directors and officers are liable for various misrepresentations, negligence and oppression.

15 The Statement of Claim detailed a transaction that occurred in 2007 for which the Class Plaintiffs claim the directors and officers failed to properly value and account for in the financial statements of Allen-Vanguard, when Allen-Vanguard purchased all of the shares of a private corporation called Mid-Eng Systems Inc.

16 In addition, the Class Plaintiff claims damages for negligent misrepresentation not only under the common law but as well under s. 138.3 of the *Ontario Securities Act* in connection with the same transaction.

17 The only creditor objection to the Plan taken at the time of the Initial Order was from counsel for the Proposed Class Plaintiff in the Laneville action, who sought an adjournment of the vote based on the wording of the proposed release terms.

18 The adjournment of the vote was not granted given the financial fragility of Allen-Vanguard, and the sanction hearing, which was to deal with the wording of the proposed release terms, was set for December 16, 2009.

19 The Second Report of the Monitor, dated December 10, 2010, advised the Court of the terms of the release and injunctions that had been negotiated, the terms of which were put forward for approval on an unopposed basis. No objection was taken at the sanction hearing by counsel for the Class Plaintiff and no amendment to the Release portion of the Sanction Order sought. Whatever had been negotiated between the parties came before the Court on an

unopposed basis. Counsel for the Class Action Plaintiffs and for the Defendant directors had input into and agreed to the wording.

20 The Court has been advised that by agreement of counsel, the wording of the Release was negotiated by the parties with the recognition that there would likely remain an issue on which the Court would have to rule. That issue is now the subject of the first motion and the cross motion. I have been advised as a result of the inquiry of February 9, 2011 and what is now obvious as a result of the recent correspondence (including an affidavit sworn June 30, 2011 and objected to) is that Plaintiffs' counsel in the Laneville action and counsel for the directors had quite different views in respect of the kinds of claims that could be included in s. 5.1(2).

21 As I now understand it, counsel for the Allen-Vanguard Corporation made no representation or agreement that the claims in the Laneville action were within those permitted by s. 5.1(2) of the CCAA.

22 Counsel for the Plaintiff in the Laneville action believe that the language in the Sanction Order preserves the claims in both the Laneville action and the Love action, including the claims against the Underwriters. It is submitted by the Plaintiff that the jurisprudence in respect of s. 5.1(2) permits not only claims against directors but as well officers to the extent there is insurance coverage, and that the Plaintiffs' position is consistent with the jurisprudence under s. 5.1(2).

23 Counsel for the Directors and for Underwriters submit that counsel for the Plaintiff knew or ought to have known at the time they agreed to the language of the Plan of Arrangement and the draft Sanction Order that the claims asserted against the Directors and Officers of Allen-Vanguard might nevertheless fail to meet one of the exceptions set out in s. 5.1(2) of the CCAA.

24 In the result, the issue of what was or was not agreed to as part of the Sanction Order comes down to the question of whether or not the wording of s. 5.1(2) of the CCAA, read in context of statutory interpretation, is sufficient to permit continuance of claims in the Laneville and Love actions.

25 As reported by the Monitor in the First Report, the Plan contemplated two releases: a General Release and an Equity Claims Release, both of which had been contemplated in the proposed Plan. Neither the Equity Claims Release nor the General Release was intended to release or deal with or affect in any respect claims under ss. 5.1(1), (2) and (3) of the CCAA, which read:

> 5.1(1) a compromise or arrangement made in respect of a debtor company may include in its terms provision for the compromise of claims against directors of the company that arose before the commencement of proceedings under this Act and that relate to the obligations of the company where the directors are by law liable in their capacity as directors for the payment of such obligations.
>
> 5.1(2) A provision for the compromise of claims against directors may not include claims that
>
> (a) relate to contractual rights of one or more creditors; or
> (b) are based on allegations of misrepresentations made by directors to creditors or of wrongful or oppressed conduct of directors.
>
> 5.1(3) the court may declare that a claim against directors shall not be compromised if it is satisfied that the compromise would not be fair and reasonable in the circumstances.

26 The Monitor in its Second Report remarked as follows:

28. The injunctions provided in the Plan are limited by section 5.1(2) of the CCAA. The injunctions barring any person from commencing, continuing or pursuing any proceeding on or after the Effective Time for a claim that such person may have against the Company or any current or former officer of the Company of the type referred to in subsection 5.1(2) of the CCAA ... but permit any such subsection 5.1(2) claim to proceed against a current or former director of the company except that any such claim against a current or former director of the company is permitted recourse, and sole recourse, to the Company's insurance policies in respect of its current and former directors. The estimated value of any coverage under such insurance is $30 million as per the Luxton Affidavit.

29. The Monitor is aware of at least one group of stakeholders affected and by the Supplemental Injunction, being a group of current and former shareholders of the Company that have served a Notice of Action and Statement of Claim on the Company seeking approximately $80 million in damages from the Company and its directors and officers, as further described in the monitors First Report. As stated above the terms of the Supplemental Injunction would permit this claim to survive against the current and former directors of the Company with recourse limited to the Companies insurance as referenced above."

27 The Releases and Sanctions are contained in the language of the Sanction Order. A summary of the provisions with paragraph references to the Sanction Order is as follows:

22. Releases are essential to the Plan

23. All Persons give full release to each of the Released Parties including contribution and indemnity but directors not released in respect of any claim of the kind referred to in section 5.1(2) of the CCAA.

24. Release of Applicant and current and former directors provided that nothing therein releases a director or current or former officer in respect of any claim of the kind referred to in section 5.1(2) of the CCAA.

25. All Persons enjoined and estopped from commencing or continuing actions with the exception of any claim against the directors of the kind referred to in section 5.1(2) of the CCAA..

26. Injunction and bar with respect to section 5.1(2) against the applicant ... and that the sole recourse for any claims against a current or former director or officer of the Applicant Limited to any recoveries from the Applicants insurance policies in respect of current or former directors and officers

27. Laneville Action dismissed as against the Applicant without prejudice to discovery rights against representative of the Applicant.

The Love Action

28 On February 8, 2010, after the Sanction Order had been made, another Proposed Representative Plaintiff, Gordon Love, commenced a second action and is represented by the same counsel as in the Laneville action. The Statement of Claim, dated March 10, 2010 against the directors and officers of Allen-Vanguard Corporation, includes claims against Cannacord Financial Ltd (and others collectively referred to as "Underwriters.")

29 An Amended Statement of Claim dated August 10, 2010 asserts in the Love action claims for negligence against directors, officers and Underwriters, all arising out of the transaction and alleged failure to properly disclose the transaction in the financial statements and transaction referred to in paragraph 15 above in respect of a 2007 acquisition.

Issues

1. Do the Laneville action and the Love action and their proposed class claims fall within those claims non-exempt under s. 5.1(2) of the CCAA?

2. Does the language of the Release contained in the Sanction Order apart from s. 5.1(2) permit either the Laneville or Love actions, including that against Underwriters, to continue?
3. Is there any basis on which the Court could or should vary the terms of the Release section of the Sanction Order?

30 Having reviewed the language of the Releases contained in the Sanction Order, I am satisfied that the only basis that the release language permits claims as against the directors is if they are those contemplated in s. 5.1(2) of the CCAA not to be released.

31 The object of the CCAA is to facilitate the restructuring of an insolvent corporation. In order to effect restructuring, a compromise of creditors' claims is almost inevitably an essential ingredient of a Plan under the CCAA.

32 The Plan, to be effective and to obtain Court approval, requires consensus and agreement by various classes of creditors. Many of the issues that arise before a Plan is approved by the Court involve a contestation between creditor groups as to how they should be classified and what extent of what group approval should be appropriately required. No motion was brought to seek to lift the stay in respect of actions provided for in the Initial Order.

33 In this case, no creditor came forward to oppose approval of the Plan, including the terms of the release language as set out in the Sanction Order. The effect of a Sanction Order is to create a contract between creditors. (See *Canadian Red Cross Society* (2002), 35 C.B.R. (4th) 43 (Ont. S.C.J.).

34 The most significant feature of the CCAA Applications that have come before the Court in the last two or three years is that the negotiation has taken place to achieve consensus among creditors often before the Initial Order under the statute.

35 One can rightly understand the reluctance on the part of a provider of interim financing to continue to do so on an indefinite basis, when the approval process may be dragged out for days, weeks or months.

36 All secured creditors whose security continues to deteriorate during the period of negotiation will seek an early determination of the consensus necessary for approval of a Plan; otherwise, liquidation may be preferable.

37 Such consensus requires agreement among many stakeholders, including not just creditors but as well current and former directors and officers, many of whose continued cooperation is necessary and integral to a Plan's success.

38 To avoid the inequity that would result from creditor claims that were outstanding as against directors at the time of a CCAA application, s. 5.1(2) was amended in 1997 to its present form. As Hart J. noted in *Re-Liberty Oil & Gas Ltd.* 2002 ABQB 949 at paragraph 4, before the enactment of this section, the legislation provided for compromises of claims only against the petitioning company. The new section extends relief against directors of the petitioning company subject to exceptions.

39 It is appropriate to approach statutory interpretation with the assumption that meaning is to be accorded to each of the words used in the provision within the overall purpose of the CCAA. The absence of other words can also be purposeful.

40 The CCAA has been said to be a skeletal statute designed to give flexibility and expediency in the ability of the company, with the concurrence of its creditors, to accomplish a restructuring of its debt in the avoidance of liquidation or bankruptcy, and does not contain a comprehensive code that lays out all that is permitted or barred. (See *ATB Financial v. Metcalfe & Mansfield Alternative Investments 11 Corp.*, 2008 ONCA 587 per Blair J.A. para. 44.)

41 Since the hearing in this matter, the Supreme Court of Canada has rendered a decision in *Century Services Inc. v. Canada (Attorney General)* 2010 SCC 60, which endorses the broad principles of the CCAA and the discretion granted

to the Court to effect a restructuring if possible or an orderly liquidation.

42 The case involved a contest between the deemed trust provisions of the *Excise Tax Act* and the CCAA. Madam Justice Deschamps, speaking for the majority, noted the need for clarity of the underlying purpose with respect to the CCAA.

43 Paragraphs 12 to 14, 17, 58-59 and 63 of that decision read as follows:

> 12. Insolvency is the factual situation that arises when a debtor is unable to pay creditors (see generally, R.J. Wood, *Bankruptcy and Insolvency Law* (2009), at p. 16). Certain legal proceedings become available upon insolvency, which typically allow a debtor to obtain a court order staying its creditors' enforcement actions and attempt to obtain a binding compromise with creditors to adjust the payment conditions to something more realistic. Alternatively, the debtor's assets may be liquidated and debts paid from the proceeds according to statutory priority rules. The former is usually referred to as reorganization or restructuring while the latter is termed liquidation.
>
> 13. Canadian commercial insolvency law is not codified in one exhaustive statute. Instead, Parliament has enacted multiple insolvency statutes, the main one being the *BIA*. The *BIA* offers a self-contained legal regime providing for both reorganization and liquidation. Although bankruptcy legislation has a long history, the *BIA* itself is a fairly recent statute -- it was enacted in 1992. It is characterized by a rules-based approach to proceedings. The *BIA* is available to insolvent debtors owing $1000 or more, regardless of whether they are natural or legal persons. It contains mechanisms for debtors to make proposals to their creditors for the adjustment of debts. If a proposal fails, the *BIA* contains a bridge to bankruptcy whereby the debtor's assets are liquidated and the proceeds paid to creditors in accordance with the statutory scheme of distribution.
>
> 14. Access to the *CCAA* is more restrictive. A debtor must be a company with liabilities in excess of $5 million. Unlike the *BIA*, the *CCAA* contains no provisions for liquidation of a debtor's assets if reorganization fails. There are three ways of exiting *CCAA* proceedings. The best outcome is achieved when the stay of proceedings provides the debtor with some breathing space during which solvency is restored and the *CCAA* process terminates without reorganization being needed. The second most desirable outcome occurs when the debtor's compromise or arrangement is accepted by its creditors and the reorganized company emerges from the *CCAA* proceedings as a going concern. Lastly, if the compromise or arrangement fails, either the company or its creditors usually seek to have the debtor's assets liquidated under the applicable provisions of the *BIA* or to place the debtor into receivership. As discussed in greater detail below, the key difference between the reorganization regimes under the *BIA* and the *CCAA* is that the latter offers a more flexible mechanism with greater judicial discretion, making it more responsive to complex reorganizations.
>
> ...
>
> 17. Parliament understood when adopting the *CCAA* that liquidation of an insolvent company was harmful for most of those it affected -- notably creditors and employees -- and that a workout which allowed the company to survive was optimal (Sarra, *Creditor Rights*, at pp. 13-15).
>
> ...

58. *CCAA* decisions are often based on discretionary grants of jurisdiction. The incremental exercise of judicial discretion in commercial courts under conditions one practitioner aptly describes as "the hothouse of real-time litigation" has been the primary method by which the *CCAA* has been adapted and has evolved to meet contemporary business and social needs (see Jones, at p. 484).

59. Judicial discretion must of course be exercised in furtherance of the *CCAA*'s purposes. The remedial purpose I referred to in the historical overview of the Act is recognized over and over again in the jurisprudence. To cite one early example:

> The legislation is remedial in the purest sense in that it provides a means whereby the devastating social and economic effects of bankruptcy or creditor initiated termination of ongoing business operations can be avoided while a court-supervised attempt to reorganize the financial affairs of the debtor company is made.
>
> *Elan Corp. v. Comiskey* reflex, (1990), 41 O.A.C. 282, at para. 57, *per* Doherty J.A., dissenting.)

...

63. Judicial innovation during *CCAA* proceedings has not been without controversy. At least two questions it raises are directly relevant to the case at bar: (1) what are the sources of a court's authority during *CCAA* proceedings? (2) what are the limits of this authority?

44 I have quoted from the above decision at length to stress the nature of the discretion that is inherent in the CCAA statute to allow the Court to fashion a structure or process to best benefit stakeholders. Consistent with that purpose and as a matter of statutory interpretation, it is appropriate to look at the interpretation of s. 5.1(1) and (2) of the CCAA. Section 5.1(1) deals with "obligations of the company where the directors are by law liable in their capacity as directors for the payment of such obligations."

45 A Plan can therefore provide for the compromise of claims against directors where a director may in law be liable for the payment of a company's obligation with the exceptions set out in s. 5.1(2).

46 In my view, the best that can be said of s. 5 is that it is not as clearly drafted as it might have been.

47 It is noteworthy that in the first line of s. 5.1(2), the only claims that may not be excluded in a compromise are those against "directors." Claims that can be excluded in a compromise include those against "officers" and the "company" itself. Why is this the case? One reason undoubtedly is the personal liability that directors face under both Federal and Provincial legislation, or the personal undertaking of a director to a creditor such as a personal guarantee. (See *C.I.T. Financial v Lambert* 2005 BCSC 1779.)

48 By way of example, s. 131(1) of the OBCA provides that directors are made personally liable for unpaid wages of the corporation's employees to a maximum of six months. Reading through s. 5.1(1) and (2), there is nothing in the wording that would prevent the compromise of such claims against officers or the company itself, but not as against directors. The CCAA does not contain a definition of the word "creditor" but does of the terms "secured creditor," "unsecured creditor" and "shareholder." It would seem that for the purposes of the CCAA and in particular s. 5.1(2), a creditor would include both a secured creditor and an unsecured creditor, but would not include a shareholder.

49 Section 5.1(2) refers only to creditors and not shareholders as prospective claimants, whether in contract, tort or statutory oppression.

50 In this case, the claims by the Class Action Plaintiffs are on behalf of shareholders against directors, since the effect of the CCAA stayed the action against the company Allen-Vanguard. The claims arise with respect to a 2007 transaction and the pre-filing financial statements, but the claims do not involve officers or the company, only directors.

51 While framed in negligence, the claims in these actions seek to involve the remedy of oppression under the OBCA to enlist the broad scope of remedy possible under that statute. However, it is only in respect of unpaid obligations of the company and other contract-type claims where the law imposes liability on the Defendant directors that invokes the exception in s. 5.1(2). It is noteworthy that the word "negligence" does not appear in the section at all.

52 In their essence, the claims in the two actions allege a failure on the part of the directors in 2007 and the company to enter into a provident transaction and the transaction represented a misrepresentation to shareholders of the value of the transaction causing a reduction in shareholder value. Such claims are not of the same kind as those contemplated in section 5.1(1). They do not relate to "obligations of the company where the directors are by law liable."

53 The claims relate to transactions that were well in advance of the Initial CCAA Order. In *Re Canadian Airlines Corp.* 2000 ABQB 442 (leave refused to ABCA, [2000] A.J. No. 1028, and to SCC, [2001] S.C.C.A. No. 60), it was held that claims against the directors should only be released if they arose prior to the date of the CCAA proceeding.

54 I agree that the oppression remedy is expansive in scope and empowers the Court to make determinations and orders that can have a direct and even a radical impact on the internal management and status of a corporation, including even an order winding up the corporation. (See *820099 Ontario Inc. v. Harold E. Ballard Ltd.* (1991), 3 B.L.R. (2d) 113 (Ont. Div. Ct.) and *Incorporated Broadcasters Ltd. v. CanWest Global*, [2001] O.J. No. 4882, 2001 CanLII 28395 (Ont. S.C.) at paragraphs 101-105.) Oppression as it occurs within s. 5.1(2) of the CCAA must be read within the context of the section itself.

55 The claims in the Love and Laneville actions are in negligence and no other remedy is sought apart from a claim for damages and access to whatever insurance may be available to respond to claims against directors and officers. There is nothing before the Court to suggest that the insurers, assuming there is a valid policy, are aware of the restriction on remedy.

56 I see no basis from the pleadings in this action for which it would be appropriate to consider the scope of relief that might otherwise apply under the oppression remedy section of the OBCA. Counsel for the Plaintiffs in the Proposed Class Actions cannot bolster their position by limiting recovery to the applicable Directors and Officers Insurance, when there is no basis for the claim at all, either under the language of the Release or the meaning to be accorded to s. 5.1(2).

57 In *BCE Inc. v. 1976 Debentureholders*, [2008] 3 S.C.R. 560, the Supreme Court of Canada commented on the expectations of stakeholders including but not limited to shareholders, in considering a Plan of Arrangement in the context of an oppression claim. Part of the test for "oppression" referred to in that decision is an expectation on the part of the claimant to be "treated in a certain way and that failure to meet the expectation involved unfair conduct."

58 I fail to understand how the expectation of one or more shareholder groups can be any different with respect to the impugned transaction than those of creditors or indeed the company itself vis-à-vis the directors, particularly since neither the officers nor the company itself is pursued.

59 The Sanction Order in this case by its terms provided release of the claims now sought to be pursued. By the terms of the Sanction Order, the only reasonable expectation of stakeholders would be that unless specifically authorized by the Order, any claim against directors would be barred. Potential claims against directors were not assigned to class plaintiffs nor was direction sought by any party about the effect of s. 5.1 prior to the issuance of the Order. Given the issue now before the Court and the disagreement of the parties, perhaps the better practice would have been to advise the Court of the issue and "carve" it out of the Plan.

60 The Court is put in a difficult position when asked in a very constrained timeframe to approve the restructuring with releases. It should certainly not be the expectation that in every instance, releases of the type here should be granted as a matter of course. Those with unpaid obligations of the company may assert that directors are liable if they fail to fulfill the company's obligation when they are legally bound to do so.

61 I am of the view that third-party releases in particular should be the exception rather than the rule. There may very well be instances in which the releases are not integral or necessary to the restructuring and should not be approved. That was not suggested in the approval process here. There was no evidence presented at the time of the granting of the Sanction Order to suggest that directors were not important to the restructuring. Indeed, the only evidence before the Court was to the contrary: that the directors were integral to the Plan's success.

62 In this case, the putative Plaintiffs did not oppose the granting of the Sanction Order and in effect took their chances that the Order might after the fact permit the limited claim referred to in the Monitor's Report.

63 All of the other stakeholders, including the secured creditors, directors, officers and the Applicant Company, approved the form of Order.

64 It is certainly speculative at this time to consider, had the form of Order proposed been objected to, to what extent the Court would have any jurisdiction to grant the language now sought by the Plaintiffs, without rejecting the Plan entirely.

65 The duty of directors is first and foremost to the company itself. The oppression remedy does not in my view permit one group (shareholders) to claim oppression when other stakeholders, for example employees or creditors or indeed the company itself, have allegedly suffered a loss that results in insolvency and are unable to seek redress and still preserve restructuring.

66 To vary or amend the Sanction Order now to permit the claims to continue might at the very least require the presence and concurrence of all of those who supported the form of Order in the first place.

67 Counsel for the proposed Plaintiffs refer to several decisions, which they urged support the proposition that shareholder actions for oppression against directors are permitted under s. 5.1(2) of the CCCA.

68 Each of those decisions, while fact-specific, in my view is consistent with a narrow range of actions warranted for a shareholder against the director under the exception to s. 5.1(2).

69 In *Re-Liberty Oil & Gas Ltd.*, 2002 ABQB 949, where the action did proceed, the allegation involved a personal representation, indeed a fraudulent one, by the defendant director to two individuals who happened to be shareholders. The complained acts were not those of the company (as here), but rather personal and direct as between the director and shareholder. In other words, there was the proximity that one would expect in a tort situation.

70 In *Worldwide Pork Corp.*, 2009 SKQB 414, the action was not permitted to proceed. At paragraphs 14 and 15 Justice Dawson said:

> It must be remembered that the oppression remedy is not designed to settle every dispute of a corporation but only those that involve and abuse of the corporate system and for which a common-law remedy does not exist.
>
> As well, the plaintiffs have pled that their claim is for damages, for loss of profits and loss of pay out dividends. There must be a causal connection between the alleged oppressive conduct and the loss claimed to be suffered by the plaintiffs. That is, there must be a causal nexus between the alleged conduct and the loss suffered by the plaintiffs. There is no pleading which sets out how

> the alleged loss of profit or dividends resulted from the conduct alleged to be oppressive. But in any event the losses claimed are losses as a result of Worldwide Pork not being profitable, that is, being unable to provide a return to shareholders for their investment. Such a loss cannot support an action for oppression since it comes with in the exception contained in section 5.1(2)(b) of the CCAA.

71 In *Re-Blue Star Battery Systems International Corp.* (2000), 10 B.L.R. (3d) 221, Farley J. of this Court dealt with a claim very much like that considered by the Supreme Court of Canada in *Century Services, supra,* as it involved G.S.T. At paragraph 12, he said

> Thus it appears to me that RevCan, not having put itself into position where it could (and did) perfect its derivative claims as set out in section 323(2)(a) of the *Excise Tax Act* never had a claim against the directors which could survive the sanction of the Plan vis-à-vis the Applicants. Nothing that this Court could do at the present time (that is, at the time when considering the CCAA sanctioned motion) could crystallize a RevCan claim against the directors. RevCan would have to take additional multiple steps over some period of time to establish a claim against the directors."

72 Farley J. went on to discuss the hypothetical of a claim in oppression against the directors as provided for in s. 5.1(2) in the context where the creditor had put the directors on notice of the promise of the company to pay the tax.

73 The argument of the Proposed Plaintiffs here is that "oppressive conduct" is not to be carved out, but that wrongful conduct that involves directors, even though the action as against the company cannot continue, it can continue against the directors.

74 What in my view is consistent with the decisions in the three cases mentioned and in the Québec case *Papiers Gaspésia* 2006 QCCS 1460 (CanLII) and with the interpretation of s. 5.1(2) is that the actions of the directors toward persons who may be regarded as creditors, and may in this context include a shareholder, are based on a direct relationship when a director takes on an obligation to make a payment that would otherwise be the obligation of the company and promises to do so or is obliged to do so by legislation. In most cases this will be a post-filing obligation. In other words, a promise by a director directly to a creditor stakeholder that is made following a CCAA Initial Order may attract liability to the director and should not be released.

75 It would be inconsistent with the scheme of the CCAA to allow all claims in which shareholders claim oppression to proceed against directors for acts or omissions that they did in the name of the company prior to the Initial Order. There would be little if any incentive to directors to pursue restructuring if they were going to be so exposed. On the other hand, personal undertakings or obligations of directors made during the CCAA process should not easily be released.

76 To permit the kind of claims as the Proposed Plaintiffs would see them would create a priority to that class of unsecured creditors that properly should belong to the creditors as a group. No leave to continue the Class action was sought before the Sanction Order was granted and even on this motion no submission was put forward for the exercise of discretion under section 5.1(3).

77 None of the cases referred to in argument dealing with s. 5.1(2) squarely deals with the issue raised here -- that the section was intended to related to post-filing claims or personal undertakings of directors to creditors in connection with the proposed plan prior to filing.

78 The final argument on behalf of Class Plaintiffs is that to deny the claim of shareholders as against directors would only benefit their insurers, since the Class Plaintiffs have agreed to limit any recovery to the amount of the insurance. I fail to see how this advances the position of the Proposed Plaintiffs. No information was put before the Court about the particulars of the insurance. The Court has no information to know whether or not the insurers even know of this issue.

79 If the claim does not lie as against the directors in the first place under s. 5.1(2), the limitation of the claim as against the potentially available insurance does not advance the case of the class of Plaintiffs.

80 There would be little meaning left to s. 5.1 if all claims of negligence and wrongful conduct against directors for pre-filing activity could not be released and no need for the discretion provided for in s. 5.1(3) for Court to override this compromise as not being fair or reasonable. As noted above in the passages from the *Century Services* case, the purpose of the CCAA and the discretion granted to the Court are to permit restructuring to work, not create new causes of action.

81 The concern of the Court, which necessitated the further inquiry, was that the language of the Sanction Order might imply on the part of the Applicant and directors who had knowledge of the particulars of the claim that the facts could give rise to a s. 5.1(2) claim. I am satisfied based on the further information provided that no such admission is to be implied.

82 The relief sought by the directors is therefore granted.

Underwriters

83 Underwriters acted on share and warrant offerings of Allen-Vanguard in September 2007 and certified a related prospectus. The Love Class Action was commenced in February 2010 and the proposed Representative Plaintiff claims damages against Underwriters under s. 130 of the *Securities Act (Ontario)* and also makes claims on the basis of negligence, unjust enrichment and waiver of tort.

84 Underwriters rely on the provisions of the releases granted by the Sanction Order and in particular the claims against the Applicant Company Allen-Vanguard. As well, Underwriters rely on the definition of "Equity Claims" in the Sanction Order and submit that because the provisions of the Order in paragraph 26(ii) bar certain claims against third parties who might claim contribution and indemnity against the restructured company, they should be entitled to the benefit of that provision.

85 The response of the proposed Class Plaintiffs in the Love litigation is that the claim against Underwriters is based on the negligence, fraud or wilful misconduct of Underwriters. It is submitted that Underwriters are not entitled to indemnity as against Allen-Vanguard for the several negligence of Underwriters, either at law or under s. 130 of the *Securities Act*.

86 The proposed Class Plaintiff submits that given the nature of the claim as against Underwriters, Underwriters would never have had a right to an indemnity for the claims asserted in the Love Action and therefore there were no such claims to be released.

87 It is submitted that Underwriters bargained any possible indemnity away by the terms of their contract with Allen-Vanguard in September 2007, and that even if they had the benefit of an indemnity, all that was required for the Plan's success was that Alan-Vanguard be protected from Underwriters, not that Mr. Love's claims against Underwriters be eliminated.

88 Counsel for the Plaintiff in the Love Action also urges that Underwriters did not have the right of indemnity as at the time of the Initial Order, and the Sanction Order bars any indemnity that they might otherwise have had and there is nothing in the language of either Order to preclude the claim of the Class Plaintiff against Underwriters limited to Underwriters' negligence.

89 Finally, it is submitted that since Underwriters did not "bring anything to the table" in respect of the restructuring, there is no basis on which the Court should vary the Sanction Order to now provide the indemnity that the Order fails to provide.

90 In the alternative, the Class Plaintiffs suggest that the Sanction Order be clarified, if necessary, to clearly provide the right of the Class Plaintiff to proceed against Underwriters.

91 In my view, there is a distinction to be made between the claim as against the directors and that against Underwriters, since in the case as against the directors, the parties appear to have bargained that if the claim could be brought under s. 5.1(2), it could proceed. That consideration was known to the parties who negotiated and agreed on the form of the Sanction Order and that was the only claim not otherwise covered by the Release terms.

92 In the case of Underwriters, there was nothing to suggest that any discussion or negotiation took place with respect to specific protection for Underwriters or the allowance of a claim against Underwriters at the time that the Sanction Order was approved.

93 This is another reason why in my view s. 5.1(2) of the CCAA should be read narrowly with respect to pre-filing claims or claims that relate to pre-filing activity.

94 The *Ontario Business Corporations Act*, R.S.O. 1990 c. B. 16 ("OBCA") contains a statutory process for that kind of action and remedy sought by the Class Plaintiffs in both actions. Section 246(1) reads as follows:

> **246.**(1) Subject to subsection (2), a complainant may apply to the court for leave to bring an action in the name and on behalf of a corporation or any of its subsidiaries, or intervene in an action to which any such body corporate is a party, for the purpose of prosecuting, defending or discontinuing the action on behalf of the body corporate.

95 The Supreme Court of Canada dealt with the issue of collective shareholder claims versus claims that are those of the corporation itself in *Hercules Management Ltd. et al. v. Ernst & Young*, 1997 CanLII 345, [1997] 2 S.C.R. 165. The case involved a claim by shareholders of the corporation against its auditors for an alleged negligence in preparation of financial statements of the corporation. Paragraph 48 of the reasons refers to and adopts a statement of Farley J. in *Roman Corp. v Peat Marwick Thorne* (1992), 11 O.R. (3d) 248 (Gen. Div.) at p. 260.

> As a matter of law the only purpose for which shareholders receive an auditor's report is to provide the shareholders with information for the purpose of overseeing the management and affairs of the corporation and not for the purpose of guiding personal investment decisions or personal speculation with a view to profit.

96 The plaintiffs in *Hercules* asserted reliance on financial statements in monitoring the value of their equity and then due to auditors' negligence, they failed to extract it before the financial demise of the company.

97 The Supreme Court, in assessing the claim, referred at paragraph 59 to the rule in *Foss v. Harbottle*, 67 E.R. 189:

> 59. The rule in *Foss v. Harbottle* provides that individual shareholders have no cause of action in law for any wrongs done to the corporation and that if an action is to be brought in respect of such losses, it must be brought either by the corporation itself (through management) or by way of a derivative action. The legal rationale behind the rule was eloquently set out by the English Court of Appeal in *Prudential Assurance Co. v. Newman Industries Ltd. (No. 2)*, [1982] 1 All E.R. 354, at p. 367, as follows:
>
>> The rule [in *Foss v. Harbottle*] is the consequence of the fact that a corporation is a separate legal entity. Other consequences are limited liability and limited rights. The company is liable for its contracts and torts; the shareholder has no such liability. The company acquires causes of action for breaches of contract and for torts which damage the company. No cause of action vests in the shareholder. When the shareholder acquires

> a share he accepts the fact that the value of his investment follows the fortunes of the company and that he can only exercise his influence over the fortunes of the company by the exercise of his voting rights in general meeting. The law confers on him the right to ensure that the company observes the limitations of its memorandum of association and the right to ensure that other shareholders observe the rule, imposed on them by the articles of association. If it is right that the law has conferred or should in certain restricted circumstances confer further rights on a shareholder the scope and consequences of such further rights require careful consideration.

To these lucid comments, I would respectfully add that the rule is also sound from a policy perspective, inasmuch as it avoids the procedural hassle of a multiplicity of actions.

60. The manner in which the rule in *Foss v. Harbottle*, *supra*, operates with respect to the appellants' claims can thus be demonstrated. As I have already explained, the appellants allege that they were prevented from properly overseeing the management of the audited corporations because the respondents' audit reports painted a misleading picture of their financial state. They allege further that had they known the true situation, they would have intervened to avoid the eventuality of the corporations' going into receivership and the consequent loss of their equity. The difficulty with this submission, I have suggested, is that it fails to recognize that in supervising management, the shareholders must be seen to be acting <u>as a body</u> in respect of the corporation's interests rather than as individuals in respect of their own ends. In a manner of speaking, the shareholders assume what may be seen to be a "managerial role" when, as a collectivity, they oversee the activities of the directors and officers through resolutions adopted at shareholder meetings. In this capacity, they cannot properly be understood to be acting simply as individual holders of equity. Rather, their collective decisions are made in respect of the corporation itself. Any duty owed by auditors in respect of this aspect of the shareholders' functions, then, would be owed not to shareholders *qua* individuals, but rather to all shareholders as a group, acting in the interests of the corporation. And if the decisions taken by the collectivity of shareholders are in respect of the corporation's affairs, then the shareholders' reliance on negligently prepared audit reports in taking such decisions will result in a wrong to the corporation for which the shareholders cannot, as individuals, recover.

61. This line of reasoning finds support in Lord Bridge's comments in *Caparo*, [1980] 1 All E.R. 568, *supra*, at p. 580:

> The shareholders of a company have a collective interest in the company's proper management and in so far as a negligent failure of the auditor to report accurately on the state of the company's finances deprives the shareholders of the opportunity to exercise their powers in general meeting to call the directors to book and to ensure that errors in management are corrected, the shareholders ought to be entitled to a remedy. <u>But in practice no problem arises in this regard since the interest of the shareholders in the proper management of the company's affairs is indistinguishable from the interest of the company itself and any loss suffered by the shareholders ... will be recouped by a claim against the auditor in the name of the company, not by individual shareholders</u>. [Emphasis in Supreme Court decision.]

It is also reflected in the decision of Farley J. in *Roman I*, *supra*, the facts of which were similar to those of the case at bar. In that case, the plaintiff shareholders brought an action against the

> defendant auditors alleging, *inter alia*, that the defendant's audit reports were negligently prepared. That negligence, the shareholders contended, prevented them from properly overseeing management which, in turn, led to the winding up of the corporation and a loss to the shareholders of their equity therein. Farley J. discussed the rule in *Foss v. Harbottle* and concluded that it operated so as to preclude the shareholders from bringing personal actions based on an alleged inability to supervise the conduct of management.
>
> 62. One final point should be made here. Referring to the case of *Goldex Mines Ltd. v. Revill* (1974), 7 O.R. (2d) 216 (C.A.), the appellants submit that where a shareholder has been directly and individually harmed, that shareholder may have a personal cause of action even though the corporation may also have a separate and distinct cause of action. Nothing in the foregoing paragraphs should be understood to detract from this principle. In finding that claims in respect of losses stemming from an alleged inability to oversee or supervise management are really derivative and not personal in nature, I have found only that shareholders cannot raise individual claims in respect of a wrong done to the corporation. Indeed, this is the limit of the rule in *Foss v. Harbottle*. Where, however, a separate and distinct claim (say, in tort) can be raised with respect to a wrong done to a shareholder *qua* individual, a personal action may well lie, assuming that all the requisite elements of a cause of action can be made out.

98 The policy of limiting indeterminate liability as in *Hercules* is consistent with the basis for the limitation of claims under s. 5.1(2) as set out above. In my view the words of s. 5.1(2) do not create a cause of action that would otherwise not exist except by leave of the Court. It simply provides an exception to what otherwise could be included in a release.

99 The release terms contained in the Sanction Order would deprive Underwriters from any claims for contribution or indemnity to which they would otherwise be entitled at law from the Company and its directors and officers should the actions of the Class Plaintiffs proceed.

100 This is just one further reason to support not just what is required for a derivative action but also what is required to be taken into consideration before the Court issues a Sanction Order in this case in effect on consent.

101 As noted above, what has come to be known as a "liquidating" CCAA application can provide problems not just for the parties but the Court itself. The presumption behind the timing of the Application in this case was that if not granted quickly, bankruptcy would have ensued with the inevitable loss of jobs, assets and creditor claims.

102 The Class Plaintiffs are taken to have known of the CCAA proposal as early as September 2009 and could have sought leave to commence a derivative action prior to or during the CCAA process. No such step was taken.

103 I am satisfied that it is appropriate in the circumstances to stay the claims as against Underwriters in negligence and misrepresentation.

104 The Claim against Underwriters also alleges fraud. If the only claim were in fraud and full particulars of alleged fraud were contained in the pleading, the claim might survive since the wording of the Release does not extend to fraud.

105 Apart from fraud, claims in negligence against Underwriters are caught by the terms of the Release. Arguably, the claims are those of the Company that are specifically released.

Variation of the Sanction Order

106 As noted above in reference to the decision in *Canadian Red Cross*, a Sanction Order in addition to being an Order of the Court and subject to the normal rules for variation thereof, represents an agreed contract between the creditors of an insolvent corporation.

107 The Class Plaintiffs in the Laneville action did not seek to lift the stay at the time of the Initial Order. The Class Plaintiff accepted the Release provisions which extend to Underwriters when the Sanctioned Order was granted.

108 Underwriters were released by the terms of the Sanction Order, and the Order, which was not appealed, represents a final determination of the rights of shareholders as against Underwriters.

109 As was mentioned above, in respect of the suggestion of variation of the Sanction Order to permit the claim as against the directors, I conclude that it is not appropriate to vary a Sanction Order after the fact. The reliance that parties place on the finality of a Sanction Order is such that it would only be in extraordinary circumstances of a clear mistake, operative misrepresentation or fraud that would permit variation without re-opening the whole process.

110 In *Extreme Retail (Canada) Inc. v. Bank of Montréal*, [2007] O.J. No. 3304 (Ont. S.J.) [Commercial List], Stinson J. held at paragraph 21 that an Approval and Vesting Order was a final determination of the rights of parties represented in that proceeding. Morawetz J. adopted those comments in *Royal Bank Body Blue Inc.*, [2008] O.J. No. 1628, 2008 CanLII 19227 [Ont. S.C.], to the same effect at paragraphs 19 and 20. In my view the same principle applies to a Sanction Order.

111 I see nothing in the requests of either Underwriters or the Class Plaintiffs that would be appropriate to permit variation of the Sanction Order as each of them have proposed.

112 Should the Class Plaintiff in the Laneville action seek to pursue a claim against Underwriters limited alone in fraud, the action should be permitted to proceed subject to the Plaintiff persuading a judge that such a limited claim should be certified.

<u>Conclusion</u>

113 For the above reasons the motion by the directors will succeed to enjoin the claims as against them in both the Love and Laneville actions. The motion of Underwriters to strike is granted, and motions for variation of the Sanction Order of both Underwriters and the Class Plaintiffs are dismissed. Counsel may make written submissions on the issue of costs.

C.L. CAMPBELL J.

cp/e/qlrxg/qlvxw/qlbdp/qlced/qlhcs

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Case Name:

Royal Bank of Canada v. Body Blue Inc.

**RE: Royal Bank of Canada, (Applicant), and
Body Blue Inc., (Respondent)**

[2008] O.J. No. 1628

13 P.P.S.A.C. (3d) 176

42 C.B.R. (5th) 125

2008 CanLII 19227

2008 CarswellOnt 2445

169 A.C.W.S. (3d) 703

Court File No.: 06-CL-6416

Ontario Superior Court of Justice
Commercial List

G.B. Morawetz J.

Heard: April 1, 2008.
Judgment: April 14, 2008.
Released: April 22, 2008.

(26 paras.)

Insolvency law -- Claims -- Property claims -- Motion by Body Blue for an Order declaring that title to certain intellectual property was conveyed to Body Blue by Court Order allowed -- In exchange for a payment to the Receiver, title in the intellectual property was transferred to Body Blue -- Herbal Care had an exclusive license to use the technology at best and did not acquire any property rights in the technology -- Thus, Body Blue held the transferred assets free and clear of any claim by Herbal Care.

Statutes, Regulations and Rules Cited:

Bankruptcy and Insolvency Act, s. 47(1)

Courts of Justice Act, s. 101

Rules of Court, Rule 57

Counsel:

Ms. D.M. Haak, for Body Blue 2006 Inc.

Mr. J.W. Tighe, for Herbal Care Systems Inc.

Mr. D. Ullmann, for ISCA Financial Services -- Interim Receiver (Present at the outset of hearing but excused before argument).

ENDORSEMENT

1 **G.B. MORAWETZ J.**:-- Body Blue 2006 Inc. ("Body Blue 2006") moves for an Order declaring that title to certain intellectual property, in particular, paraben glycol free technology ("PG Free"), once owned by Body Blue Inc. ("Old Body Blue"), was conveyed to Body Blue 2006 (formerly BBTA Industries Inc.) by Court Order dated May 17, 2006 (the "Approval and Vesting Order" or the "A&V Order") and that Herbal Care's contractual or licenced rights, if any, ended by reason of the A&V Order.

2 On April 28, 2006, ISCA Financial Services (the "Receiver") was appointed as Interim Receiver and Receiver and Manager of Old Body Blue.

3 It is not disputed that, at the time the Receiver was appointed, PG Free was owned by Old Body Blue.

4 By agreement dated May 19, 2006, in exchange for a payment to the Receiver of $7,159,947.66, Old Body Blue's right, title and interest in and to the purchased assets, expressly including PG Free, was transferred to Body Blue 2006. Pursuant to the terms of the A&V Order, upon the filing of the Receiver's Certificate with the Court, all right title and interest of Old Body Blue in the purchased assets (including PG Free), vested in Body Blue 2006.

5 On June 9, 2006, prior to the expiration of the appeal period in respect of the A&V Order, counsel to Herbal Care advised counsel for Body Blue 2006 that during the period that Old Body Blue had been the owner of PG Free, Old Body Blue had licenced to Herbal Care the exclusive rights to manufacture and sell PG Free, and that Herbal Care took the position that its right to manufacture and sell PG Free was not affected by the A&V Order.

6 Counsel to Herbal Care also advised that it would, if necessary, seek an amendment to the A&V Order.

7 Herbal Care did not, at any time, take any steps to set aside or vary the A&V Order. Herbal Care has not taken any steps to appeal the A&V Order.

8 Herbal Care has commenced an action in Arizona seeking damages for tortious interference and unjust enrichment and declaratory relief related to its purported licence rights. The U.S. District Court confirmed that Body Blue 2006 acquired PG Free in accordance with the A&V Order, but held that Body Blue 2006 acquired the rights subject to Herbal Care's contractual interest. The Arizona Court reasoned:

> This Court will defer to a Canadian judgment and respect principles of international comity, however, it is Defendants' burden to prove that under Canadian law, a Canadian Court can allow Body Blue 2006 to purchase the assets of Body Blue, Inc. without the accompanying contractual obligations that Body Blue, Inc. was subject to merely by stating the property is acquired "free and clear of and from any claims and liens".

9 Body Blue 2006 brought a motion in the U.S. District Court for reconsideration, which motion was denied. The Arizona Court was not convinced that the Receiver had the right to deal with a licence right which Herbal Care alleges, in the Arizona action, that it owns.

10 In this motion, Herbal Care has put forth no evidence to support any property interest in PG Free. Further, the contract dated January 1, 2005 ("the Royalty Agreement") which is contained at Exhibit "Q" to the affidavit of Mr. Babich does not constitute a property claim.

11 Herbal Care takes the position that it has the exclusive licencing rights to use the PG Free Technology and that given the existence of the licencing agreement, the representations made in the Stock Redemption Agreement and the Royalty Agreement, there are disputed facts concerning the proper ownership of the licence.

12 Herbal Care seeks a dismissal of this motion to facilitate a full trial on the issues in the Arizona action. Herbal Care also complains that it did not receive Notice that the Receiver was selling the assets of Old Body Blue, and specifically, that Herbal Care's rights to the PG Free Technology were purported to be sold.

13 For the following reasons I have concluded that the position of Herbal Care is not sustainable.

14 The process by which the property of Old Body Blue was transferred to Body Blue 2006 was conducted in accordance with the provisions of section 47(1) of the *Bankruptcy and Insolvency Act*, section 101 of the *Courts of Justice Act*, and in accordance with Court Orders made in this proceeding.

15 At best, Herbal Care had an exclusive licence to use the PG Free technology. However, even if established, a licence agreement only creates a contractual agreement as between the parties. Even if the grant to Herbal Care to market and sell were construed as a traditional licence, it is not the case that Herbal Care acquired a property interest in such a right. This issue was considered in *Re T. Eaton Co.*, [1999] O.J. No. 4216 (S.C.J.) at paragraph 12:

> The true nature of an (exclusive) licence is leave or permission to do such a thing, which would otherwise be unlawful (and a contract not to give leave or permission to anyone else to do the same thing). It confers no interest or property in the thing.

16 In making this reference, Farley J. in turn relied on *Heap v. Hartley* 1889, 42 Ch. D. 461 (C.A.).

17 The remedy, if any, that Herbal Care has is contractual in nature. The exercise of that remedy has been impacted by the A&V Order.

18 Body Blue 2006 submits that the Court can interpret the terms of a Vesting Order in resolving disputes that arise subsequent to the making of the Vesting Order. Counsel cites the decision of Stinson J. in *Extreme Retail* (*Canada*) *Inc. v. Bank of Montreal*, [2007] O.J. No. 3304 (S.C.J.) at paragraphs 17, 20 and 21 in support of this proposition. The relevant comments of Stinson J. are set out as follows:

> In my view, this dispute is governed by the plain language of the Approval and Vesting Order relating to the terms upon which Extreme acquired the assets that it purchased. I have earlier quoted the operative provision of that order. In my view, that language makes it plain that the assets that Extreme acquired were not subject to any higher rights.
>
> ...
>
> In my view, it is neither appropriate nor desirable to, in effect, open up and revisit the terms of a vesting order, especially one given two and a half years ago, and upon which parties have subsequently acted and conducted their affairs. It is impossible to say what would have occurred as the parties were negotiating the sale agreement, had the issue of BMO's claimed priority been

> raised at the time. I am not prepared to speculate that it would have been a matter of no moment: Extreme negotiated for and acquired the assets on the terms set out in the sale agreement and the Approval and Vesting Order. The assets were to be acquired free and clear. BMO was aware of this. BMO failed to protect its claimed position.
>
> ...
>
> In the present case, the Approval and Vesting Order was a final judicial determination of the rights of the parties represented in that proceeding in respect of the assets that were the subject of the sale. The CCAA objective of providing a mechanism for the efficient restructuring of corporations that encounter financial difficulty would be seriously undermined if parties who failed to assert or protect their rights at the time of the restructuring were permitted subsequently to return to court to undo past transactions. Such an approach should be discouraged.

19 I am in agreement with these statements of Stinson J.

20 In this case, the A&V Order determined the rights of the parties represented in that proceeding in respect of the assets that were the subject of the sale. Although Herbal Care had not been given notice and was not represented at the hearing giving rise to the A&V Order, this non-participation does not, in my view, impact on this motion. Herbal Care took no steps after becoming aware of the A&V Order to set aside or vary the A&V Order and did not appeal the A&V Order. Herbal Care is, in my view, bound by the terms of the A&V Order.

21 The claim of Herbal Care is one of contract. It is a claim against Old Body Blue. It does not affect the transfer of title to the property, assets and undertaking of Old Body Blue to Body Blue 2006.

22 Body Blue 2006 holds the transferred assets free and clear of any claim of Herbal Care. Paragraph 6 of the A&V Order clearly provides that after the filing of the Receiver's Certificate, which evidences that the transaction has been completed, any and all "claims" of any "claimant" in or to the "purchased assets" shall vest in the proceeds derived from the completion of the transaction.

23 I am satisfied, that it is appropriate for me to both interpret and clarify the A&V Order. In this regard I accept the statements contained in the factum of Body Blue 2006 and the authorities cited. See *Molson Canada v. O-I Canada Corp.* (2003), 43 C.B.R. (4th) 172 and *Canadian Imperial Bank of Commerce v. McIvor*, [1998] S.J. No. 610 (Q.B.).

24 In the result, I have concluded that Herbal Care has no property rights in the PG free technology. The A&V Order had the effect of conveying title in PG Free to Body Blue 2006, free and clear of the rights asserted by Herbal Care. The right, title and interest of Old Body Blue in and to PG Free Technology is vested in Body Blue 2006, and Body Blue 2006 and any successors in title are not bound by any of the claims asserted by Herbal Care. Further, this determination is not dependent on the outcome of the action commenced in Arizona.

25 The motion of Body Blue 2006 is granted with costs.

26 Counsel did not provide a Costs Outline at the conclusion of the hearing. Counsel to Body Blue 2006 submitted that $10,000 would be an appropriate award, win or lose. The figure was calculated based on a substantial indemnity basis. Counsel to Herbal Care suggested that a figure of $3,000, win or lose, would be more appropriate. In my view, having considered the record, the submissions of counsel, the impact of Rule 57 and the principles set forth in *Boucher v. Public Accountants Council for the Province of Ontario* (2004), 71 O.R. (3d) 291 (C.A.), costs are awarded to Body Blue 2006 on a partial indemnity basis in the amount of $6,500, payable within 30 days.

G.B. MORAWETZ J.

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5

Indexed as:

Canadian Red Cross Society (Re)

IN THE MATTER OF the Companies' Creditors Arrangement Act, R.S.C. 1985 c. C-36
AND IN THE MATTER OF a Plan of Compromise or Arrangement of the Canadian Red Cross Society/La Société Canadienne De La Croix-Rouge
AND IN THE MATTER OF the Canadian Red Cross Society/ La Société Canadienne De La Croix-Rouge

[1998] O.J. No. 3306

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Blair J.

August 19, 1998.

(28 pp.)

[Ed. note: Supplementary reasons released August 19, 1998. See [1998] O.J. No. 3307. Further supplementary reasons also released August 19, 1998. See [1998] O.J. No. 3513.]

Counsel:

B. Zarnett, B. Empey and J. Latham, for the Canadian Red Cross.
E.B. Leonard, S.J. Page and D.S. Ward, for the Provinces except Que. and for the Canadian Blood Services.
Jeffrey Carhart, for the Héma-Québec and for the Government of Québec.
Marlene Thomas and John Spencer, for the Attorney General of Canada.

Pierre R. Lavigne and Frank Bennett, for the Quebec '86-90 Hepatitis C Claimants.
Pamela Huff and Bonnie Tough, for the 1986-1990 Haemophiliac Hepatitis C Claimants.
Harvin Pitch and Kenneth Arenson, for the 1986-1990 Hepatitis C Class Action Claimants.
Aubrey Kaufman and David Harvey, for the Pre 86/Post 90 Hepatitis C Class Action Claimants.
Bruce Lemer, for the B.C. 1986-90 Class Action.
Donna Ring, for the HIV Claimants.
David A. Klein, for the B.C. Pre-86/Post-90 Hepatitis C Claimants.
David Thompson, agent for the Quebec Pre-86/Post 90 Hepatitis C Claimants.
Michael Kainer, for the Service Employees International Union.
I.V.B. Nordheimer, for the Bayer Corporation.
R.N. Robertson, Q.C. and S.E. Seigel, for the T.D. Bank.
James H. Smellie, for the Canadian Blood Agency.
W.V. Sasso, for the Province of British Columbia.
Justin R. Fogarty, for the Raytheon Engineers.
Nancy Spies, for the Central Hospital et al (Co-D).
M. Thomson, for the various physicians.
C.H. Freeman, for the Blood Trac Systems.

BLAIR J. (endorsement):--

Background and Genesis of the Proceedings

1 The Canadian Red Cross Society/La Société Canadienne de la Croix Rouge has sought and obtained the insolvency protection and supervision of the Court under the Companies' Creditors Arrangement Act ("CCAA'). It has done so with a view to putting forward a Plan to compromise its obligations to creditors and also as part of a national process in which responsibility for the Canadian blood supply is to be transferred from the Red Cross to two new agencies which are to form a new national blood authority to take control of the Canadian Blood Program.

2 The Red Cross finds itself in this predicament primarily as a result of some $8 billion of tort claims being asserted against it (and others, including governments and hospitals) by a large number of people who have suffered tragic harm from diseases contacted as a result of a blood contamination problem that has haunted the Canadian blood system since at least the early 1980's. Following upon the revelations forthcoming from the wide-ranging and seminal Krever Commission Inquiry on the Blood System in Canada, and the concern about the safety of that system - and indeed alarm - in the general population as a result of those revelations, the federal, provincial and territorial governments decided to transfer responsibility for the Canadian Blood Supply to a new national authority. This new national authority consists of two agencies, the Canadian Blood Service and Héma-Québec.

The Motions

3 The primary matters for consideration in these Reasons deal with a Motion by the Red Cross for approval of the sale and transfer of its blood supply assets and operations to the two agencies and a cross-Motion on behalf of one of the Groups of Transfusion Claimants for an order dismissing that Motion and directing the holding of a meeting of creditors to consider a counter-proposal which would see the Red Cross continue to operate the blood system for a period of time and attempt to generate sufficient revenues on a fee-for-blood-service basis to create a compensation fund for victims.

4 There are other Motions as well, dealing with such things as the appointment of additional Representative Counsel

and their funding, and with certain procedural matters pertaining generally to the CCAA proceedings. I will return to these less central motions at the end of these Reasons.

Operation of the Canadian Blood System and Evolution of the Acquisition Agreement

5 Transfer of responsibility for the operation of the Canadian blood supply system to a new authority will mark the first time that responsibility for a nationally co-ordinated blood system has not been in the hands of the Canadian Red Cross. Its first blood donor clinic was held in January, 1940 - when a national approach to the provision of a blood supply was first developed. Since 1977, the Red Cross has operated the Blood Program furnishing the Canadian health system with a variety of blood and blood products, with funding from the provincial and territorial governments. In 1981, the Canadian Blood Committee, composed of representatives of the governments, was created to oversee the Blood Program on behalf of the Governments. In 1991 this Committee was replaced by the Canadian Blood Agency - whose members are the Ministers of Health for the provinces and territories - as funder and co-ordinator of the Blood Program. The Canadian Blood Agency, together with the federal government's regulatory agency known as BBR (The Bureau of Biologics and Radiopharmaceuticals) and the Red Cross, are the principal components of the organizational structure of the current Blood Supply System.

6 In the contemplated new regime, The Canadian Blood Service has been designated as the vehicle by which the Governments in Canada will deliver to Canadians (in all provinces and territories except Quebec) a new fully integrated and accountable Blood Supply System. Quebec has established Héma-Québec as its own blood service within its own health care system, but subject to federal standards and regulations. The two agencies have agreed to work together, and are working in a co-ordinated fashion, to ensure all Canadians have access to safe, secure and adequate supplies of blood, blood products and their alternatives. The scheduled date for the transfer of the Canadian blood supply operations from the Red Cross to the new agencies was originally September 1, 1998. Following the adjournment of these proceedings on July 31st to today's date, the closing has been postponed. It is presently contemplated to take place shortly after September 18, 1998 if the transaction is approved by the Court.

7 The assets owned and controlled by the Red Cross are important to the continued viability of the blood supply operations, and to the seamless transfer of those operations in the interests of public health and safety. They also have value. In fact, they are the source of the principal value in the Red Cross's assets which might be available to satisfy the claims of creditors. Their sale was therefore seen by those involved in attempting to structure a resolution to all of these political, social and personal problems, as providing the main opportunity to develop a pool of funds to go towards satisfying the Red Cross's obligations regarding the claims of what are generally referred to in these proceedings as the "Transfusion Claimants". It appears, though, that the Transfusion Claimants did not have much, if any, involvement in the structuring of the proposed resolution.

8 Everyone recognizes, I think, that the projected pool of funds will not be sufficient to satisfy such claims in full, but it is thought - by the Red Cross and the Governments, in any event - that the proceeds of sale from the transfer of the Society's blood supply assets represent the best hope of maximizing the return on the Society's assets and thus of maximizing the funds available from it to meet its obligations to the Transfusion Claimants.

9 This umbrella approach - namely, that the blood supply operations must be transferred to a new authority, but that the proceeds generated from that transfer should provide the pool of funds from which the Transfusion Claimants can, and should, be satisfied, so that the Red Cross may avoid bankruptcy and continue its other humanitarian operations - is what led to the marriage of these CCAA proceedings and the transfer of responsibility for the Blood System. The Acquisition Agreement which has been carefully and hotly negotiated over the past 9 months, and the sale from the Red Cross to the new agencies is - at the insistence of the Governments - subject to the approval of the Court, and they are as well conditional upon the Red Cross making an application to restructure pursuant to the CCAA.

10 The Initial Order was made in these proceedings under the CCAA on July 20th.

The Sale and Transfer Transaction

11 The Acquisition Agreement provides for the transfer of the operation of the Blood Program from the Red Cross to the Canadian Blood Service and Héma-Québec, together with employees, donor and patient records and assets relating to the operation of the Program on September 1, 1998. Court approval of the Agreement, together with certain orders to ensure the transfer of clear title to the Purchasers, are conditions of closing.

12 The sale is expected to generate about $169 million in all, before various deductions. That sum is comprised of a purchase price for the blood supply assets of $132.9 million plus an estimated $36 million to be paid for inventory. Significant portions of these funds are to be held in escrow pending the resolution of different issues; but, in the end, after payment of the balance of the outstanding indebtedness to the T-D Bank (which has advanced a secured line of credit to fund the transfer and re-structuring) and the payment of certain creditors, it is anticipated that a pool of funds amounting to between $70 million and $100 million may be available to be applied against the Transfusion Claims.

13 In substance, the new agencies are to acquire all fixed assets, inventory, equipment, contracts and leases associated with the Red Cross Blood Program, including intellectual property, information systems, data, software, licences, operating procedures and the very important donor and patient records. There is no doubt that the sale represents the transfer of the bulk of the significant and valuable assets of the Red Cross.

14 A vesting order is sought as part of the relief to be granted. Such an order, if made, will have the effect of extinguishing realty encumbrances against and security interest in those assets. I am satisfied for these purposes that appropriate notification has been given to registered encumbrancers and other security interest holders to permit such an order to be made. I am also satisfied, for purposes of notification warranting a vesting order, that adequate notification of a direct and public nature has been given to all of those who may have a claim against the assets. The CCAA proceedings themselves, and the general nature of the Plan to be advanced by the Red Cross - including the prior sale of the blood supply assets - has received wide coverage in the media. Specific notification has been published in principal newspapers across the country. A document room containing relevant information regarding the proposed transaction, and relevant financial information, was set up in Toronto and most, if not all, claimants have taken advantage of access to that room. Richter & Partners were appointed by the Court to provide independent financial advice to the Transfusion Claimants, and they have done so. Accordingly, I am satisfied in terms of notification and service that the proper foundation for the granting of the Order sought has been laid.

15 What is proposed, to satisfy the need to protect encumbrancers and holders of personal security interests is,

a) that generally speaking, prior registered interests and encumbrances against the Red Cross's lands and buildings will not be affected - i.e., the transfer and sale will take place subject to those interests, or they will be paid off on closing; and,

b) that registered personal property interests will either be assumed by the Purchasers or paid off from the proceeds of closing in accordance with their legal entitlement.

Whether the Purchase Price is Fair and Reasonable

16 The central question for determination on this Motion is whether the proposed Purchase Price for the Red Cross's blood supply related assets is fair and reasonable in the circumstances, and a price that is as close to the maximum as is reasonably likely to be obtained for such assets. If the answer to this question is "Yes", then there can be little quarrel - it seems to me - with the conversion of those assets into cash and their replacement with that cash as the asset source available to satisfy the claims of creditors, including the Transfusion Claimants. It matters not to creditors and Claimants whether the source of their recovery is a pool of cash or a pool of real/personal/intangible assets. Indeed, it may well be advantageous to have the assets already crystallised into a cash fund, readily available and earning interest. What is important is that the value of that recovery pool is as high as possible.

17 On behalf of the 1986-1990 Québec Hepatitis C Claimants Mr. Lavigne and Mr. Bennett argue, however, that the

purchase price is not high enough. Mr. Lavigne has put forward a counter-proposal which he submits will enhance the value of the Red Cross's blood supply assets by giving greater play to the value of its exclusive licence to be the national supplier of blood, and which will accordingly result in a much greater return for Claimants. This proposal has been referred to as the "Lavigne Proposal" or the "No-Fault Plan of Arrangement". I shall return to it shortly; but first I propose to deal with the submissions of the Red Cross and of those who support its Motion for approval, that the proposed price is fair and reasonable. Those parties include the Governments, the proposed Purchasers - the Canadian Blood Service and Héma-Québec - and several (but not all) of the other Transfusion Claimant Groups.

18 As I have indicated, the gross purchase price under the Acquisition Agreement is $132.9 million, plus an additional amount to be paid for inventory on closing which will generate a total purchase price of approximately $169 million. Out of that amount, the Bank indebtedness is to be paid and the claims of certain other creditors defrayed. It is estimated that a fund of between $70 million and $100 million will be available to constitute the trust fund to be set aside to satisfy Transfusion Claims.

19 This price is based upon a Valuation prepared jointly by Deloitte & Touche (financial advisor to the Governments) and Ernst & Young (financial advisor to the Red Cross and the present Monitor appointed under the Initial CCAA Order). These two financial advisors retained and relied upon independent appraisal experts to appraise the realty (Royal LePage), the machinery and equipment and intangible assets (American Appraisal Canada Inc.) and the laboratories (Pellemon Inc.). The experience, expertise and qualifications of these various experts to conduct such appraisals cannot be questioned. At the same time, it must be acknowledged that neither Deloitte & Touche nor Ernst & Young are completely "independent" in this exercise, given the source of their retainers. It was at least partly for this reason that the Court was open to the suggestion that Richter & Partners be appointed to advise the 1986-1990 Ontario Class Action Claimants (and through them to provide independent advice and information to the other groups of Transfusion Claimants). The evidence and submissions indicate that Richter & Partners have met with the Monitor and with representatives of Deloitte & Touche, and that all enquiries have been responded to.

20 Richter & Partners were appointed at the instance of the 1986-1990 Ontario Hepatitis C Claimants Richter & Partners, with a mandate to share their information and recommendations with the other Groups of Transfusion Claimants. Mr. Pitch advises on behalf of that Group that as a result of their due diligence enquiries his clients are prepared to agree to the approval of the Acquisition Agreement, and, indeed urge that it be approved quickly. A significant number of the other Transfusion Claimant groups but by no means all - have taken similar positions, although subject in some cases to certain caveats, none of which pertain to the adequacy of the purchase price. On behalf of the 1986-1990 Hemophiliac Claimants, for instance, Ms. Huff does not oppose the transfer approval, although she raises certain concerns about certain terms of the Acquisition Agreement which may impinge upon the amount of monies that will be available to Claimants on closing, and she would like to see these issues addressed in any Order, if approval is granted. Mr. Lemer, on behalf of the British Columbia 1986-1990 Hepatitis C Class Action Claimants, takes the same position as Ms. Huff, but advises that his clients' further due diligence has satisfied them that the price is fair and reasonable. While Mr. Kaufman, on behalf of Pre 86/Post 90 Hepatitis C Claimants, advances a number of jurisdictional arguments against approval, his clients do not otherwise oppose the transfer (but they would like certain caveats applied) and they do not question the price which has been negotiated for the Red Cross's blood supply assets. Mr. Kainer for the Service Employees Union (which represents approximately 1,000 Red Cross employees) also supports the Red Cross Motion, as does, very eloquently, Ms. Donna Ring who is counsel for Ms. Janet Conners and other secondarily infected spouses and children with HIV.

21 Thus, there is broad support amongst a large segment of the Transfusion Claimants for approval of the sale and transfer of the blood supply assets as proposed.

22 Some of these supporting Claimants, at least, have relied upon the due diligence information received through Richter & Partners, in assessing their rights and determining what position to take. This independent source of due diligence therefore provides some comfort as to the adequacy of the purchase price. It does not necessarily carry the day, however, if the Lavigne Proposal offers a solution that may reasonably practically generate a higher value for the

blood supply assets in particular and the Red Cross assets in general. I turn to that Proposal now.

The Lavigne Proposal

23 Mr. Lavigne is Representative Counsel for the 1986-1990 Québec Hepatitis C Claimants. His cross-motion asks for various types of relief, including for the purposes of the main Motion,

a) an order dismissing the Red Cross motion for court approval of the sale of the blood supply assets;
b) an order directing the Monitor to review the feasibility of the Lavigne Proposal's plan of arrangement (the "No-Fault Plan of Arrangement") which has now been filed with the Court of behalf of his group of "creditors"; and,
c) an order scheduling a meeting of creditors within 6 weeks of the end of this month for the purpose of voting on the No-Fault Plan of Arrangement.

24 This cross-motion is supported by a group of British Columbia Pre 86/Post 90 Hepatitis C Claimants who are formally represented at the moment by Mr. Kaufman but for whom Mr. Klein now seeks to be appointed Representative Counsel. It is also supported by Mr. Lauzon who seeks to be appointed Representative Counsel for a group of Québec Pre 86/Post 90 Hepatitis C Claimants. I shall return to these "Representation" Motions at the end of these Reasons. Suffice it to say at this stage that counsel strongly endorsed the Lavigne Proposal.

25 The Lavigne Proposal can be summarized in essence in the following four principals, namely:

1. Court approval of a no-fault plan of compensation for all Transfusion Claimants, known or unknown;
2. Immediate termination by the Court of the Master Agreement presently governing the relationship between the Red Cross and the Canadian Blood Agency, and the funding of the former, which Agreement requires a one year notice period for termination;
3. Payment in full of the claims of all creditors of the Red Cross; and,
4. No disruption of the Canadian Blood Supply.

26 The key assumptions and premises underlying these notions are,

* that the Red Cross has a form of monopoly in the sense that it is the only blood supplier licensed by Government in Canada to supply blood to hospitals;
* that, accordingly, this license has "value", which has not been recognized in the Valuation prepared by Deloitte & Touche and by Ernst & Young, and which can be exploited and enhanced by the Red Cross continuing to operate the Blood Supply and charging hospitals directly on a fully funded cost recovery basis for its blood services;
* that Government will not remove this monopoly from the Red Cross for fear of disrupting the Blood Supply in Canada;
* that the Red Cross would be able to charge hospitals sufficient amounts not only to cover its costs of operation (without any public funding such as that now coming from the Canadian Blood Agency under the Master Agreement), but also to pay all of its creditors and to establish a fund which would allow for compensation over time to all of the Transfusion Claimants; and, finally,
* that the no-fault proposal is simply an introduction of the Krever Commission recommendations for a scheme of no-fault compensation for all transfusion claimants, for the funding of the blood supply program through direct cost recovery from hospitals, and for the inclusion of a component for a compensation fund in the fee for service delivery charge.

27 In his careful argument in support of his proposal Mr. Lavigne was more inclined to couch his rationale for the No-Fault Plan in political terms rather than in terms of the potential value created by the Red Cross monopoly licence and arising from the prospect of utilizing that monopoly licence to raise revenue on a fee-for-blood-service basis, thus leading - arguably - to an enhanced "value" of the blood supply operations and assets. He seemed to me to be suggesting, in essence, that because there are significant Transfusion Claims outstanding against the Red Cross, Government as the indirect purchaser of the assets should recognize this and incorporate into the purchase price an element reflecting the value of those claims. It was submitted that because the Red Cross has (or, at least, will have had) a monopoly licence regarding the supply of blood products in Canada, and because it could charge a fee-for-blood-service to hospitals for those services and products, and because other regimes M other countries employ such a fee for service system and build in an insurance or compensation element for claims, and because the Red Cross might be able to recover such an element in the regime he proposes for it, then the purchase price must reflect the value of those outstanding claims in some fashion. I am not able to understand, in market terms, however, why the value of a debtor's assets is necessarily reflective in any way of the value of the claims against those assets. In fact, it is the stuff of the everyday insolvency world that exactly the opposite is the case. In my view, the argument is more appropriately put - for the purposes of the commercial and restructuring considerations which are what govern the Court's decisions in these types of CCAA proceedings - on the basis of the potential increase in value from the revenue generating capacity of the monopoly licence itself. In fairness, that is the way in which Mr. Lavigne's Proposal is developed and justified in the written materials filed.

28 After careful consideration of it, however, I have concluded that the Lavigne Proposal cannot withstand scrutiny, in the context of these present proceedings.

29 Farley Cohen - a forensic a principal in the expert forensic investigative and accounting firm of Linquist Avery Macdonald Baskerville Company - has testified that in his opinion the Red Cross operating licence "provides the potential opportunity and ability for the Red Cross to satisfy its current and future liabilities as discussed below". Mr. Cohen then proceeds in his affidavit to set out the basis and underlying assumptions for that opinion in the following paragraphs, which I quote in their entirety:

1. In my opinion, if the Red Cross can continue as a sole and exclusive operator of the Blood Supply Program and can amend its funding arrangements to provide for full cost recovery, including the cost of proven claims of Transfusion Claimants, and whereby the Red Cross would charge hospitals directly for the Blood Safety Program, then there is a substantial value to the Red Cross to satisfy all the claims against it.
2. In my opinion, such value to the Red Cross is not reflected in the Joint Valuation Report.
3. My opinion is based on the following assumptions: (i) the Federal Government, while having the power to issue additional licences to other Blood System operators, would not do so in the interest of public safety; (ii) the Red Cross can terminate the current funding arrangement pursuant to the terms of the Master Agreement; and (iii) the cost of blood charged to the hospitals would not be cost-prohibitive compared to alternative blood suppliers. (highlighting in original)

30 On his cross-examination, Mr. Cohen acknowledged that he did not know whether his assumptions could come true or not. That difficulty, it seems to me, is an indicia of the central weakness in the Lavigne Proposal. The reality of the present situation is that all 13 Governments in Canada have determined unequivocally that the Red Cross will no longer be responsible for or involved in the operation of the national blood supply in this country. That is the evidentiary bedrock underlying these proceedings. If that is the case, there is simply no realistic likelihood that any of the assumptions made by Mr. Cohen will occur. His opinion is only as sound as the assumptions on which it is based.

31 Like all counsel - even those for the Transfusion Claimants who do not support his position - I commend Mr. Lavigne for his ingenuity and for his sincerity and perseverence in pursing his clients' general goals in relation to the blood supply program. However, after giving it careful consideration as I have said, I have come to the conclusion that

the Lavigne Proposal - whatever commendation it my deserve in other contexts - does not offer a workable or practical alternative solution in the context of these CCAA proceedings. I question whether it can even be said to constitute a "Plan of Compromise and Arrangement" within the meaning of the CCAA, because it is not something which either the debtor (the Red Cross) or the creditors (the Transfusion Claimants amongst them) have control over to make happen. It is, in reality, a political and social solution which must be effected by Governments. It is not something which can be imposed by the Court in the context of a restructuring. Without deciding that issue, however, I am satisfied that the Proposal is not one which in the circumstances warrants the Court in exercising its discretion under sections 4 and 5 of the CCAA to call a meeting of creditors to vote on it.

32 Mr. Justice Krever recommended that the Red Cross not continue in the operation of the Blood Supply System and, while he did recommend the introduction of a no-fault scheme to compensate all blood victims, it was not a scheme that would be centred around the continued involvement of the Red Cross. It was a government established statutory no-fault scheme. He said (Final Report, Vol. 3, p. 1045):

> The provinces and territories of Canada should devise statutory no-fault schemes that compensate all blood-injured persons promptly and adequately, so they do not suffer impoverishment or illness without treatment. I therefore recommend that, without delay, the provinces and territories devise statutory no-fault schemes for compensating persons who suffer serious adverse consequences as a result of the administration of blood components or blood products.

33 Governments - which are required to make difficult choices - have chosen, for their own particular reasons, not to go down this particular socio-political road. While this may continue to be a very live issue in the social and political arena, it is not one which, as I have said, is a solution that can be imposed by the Court in proceedings such as these.

34 I am satisfied, as well, that the Lavigne Proposal ought not to impede the present process on the basis that it is unworkable and impractical, in the present circumstances, and given the determined political decision to transfer the blood supply from the Red Cross to the new agencies, might possibly result in a disruption of the supply and raise concerns for the safety of the public if that were the case. The reasons why this is so, from an evidentiary perspective, are well articulated in the affidavit of the Secretary General of the Canadian Red Cross, Pierre Duplessis, in his affidavit sworn on August 17, 1998. I accept that evidence and the reasons articulated therein. In substance Dr. Duplessis states that the assumptions underlying the Lavigne Proposal are "unrealistic, impractical and unachievable for the Red Cross in the current environment" because,

a) the political and factual reality is that Governments have clearly decided - following the recommendation of Mr. Justice Krever - that the Red Cross will not continue to be involved in the National Blood Program, and at least with respect to Quebec have indicated that they are prepared to resort to their powers of expropriation if necessary to effect a transfer;

b) the delays and confusion which would result from a postponement to test the Lavigne Proposal could have detrimental effects on the blood system itself and on employees, hospitals, and other health care providers involved in it;

c) the Master Agreement between the Red Cross and the Canadian Blood Agency, under which the Society currently obtains its funding, cannot be cancelled except on one year's notice, and even if it could there would be great risks in denuding the Red Cross of all of its existing funding in exchange for the prospect of replacing that funding with fee for service revenues; and,

d) it is very unlikely that over 900 hospitals across Canada - which have hitherto not paid for their blood supply, which have no budgets contemplating that they will do so, and which are underfunded in event will be able to pay sufficient sums to enable the Red Cross not only to cover its operating costs and to pay current bills, but also to repay the present Bank indebtedness of approximately $35 million in full, and to repay existing unsecured

creditors in full, and to generate a compensation fund that will pay existing Transfusion Claimants (it is suggested) in full for their $8 billion in claims.

35 Dr. Duplessis summarizes the risks inherent in further delays in the following passages from paragraph 17 of his affidavit sworn on August 17, 1998:

> The Lavigne Proposal that the purchase price could be renegotiated to a higher price because of Red Cross' ability to operate on the terms the Lavigne Proposal envisions is not realistic, because Red Cross does not have the ability to operate on those terms. Accordingly, there is no reason to expect that CBS and H-Q would pay a higher amount than they have already agreed to pay under the Acquisition Agreement. Indeed, there is a serious risk that delays or attempts to renegotiate would result in lower amounts being paid. Delaying approval of the Acquisition Agreement to permit an experiment with the Lavigne Proposal exposes Red Cross and its stakeholders, including all Transfusion Claimants, to the following risks:
>
> (a) continued losses in operating the National Blood Program which will reduce the amounts ultimately available to all stakeholders;
> (b) Red Cross' ability to continue to operate its other activities being jeopardized;
> (c) the Bank refusing to continue to support even the current level of funding and demanding repayment, thereby jeopardizing Red Cross and all of Red Cross' activities including the National Blood Program;
> (d) CBS and H-Q becoming unprepared to complete an acquisition on the same financial terms given, among other things, the costs which they will incur in adjusting for later transfer dates, raising the risks of exproporiation or some other, less favourable taking of Red Cross' assets, or the Governments simply proceeding to set up the means to operate the National Blood Program without paying the Red Cross for its assets.

36 These conclusions, and the evidentiary base underlying them, are in my view irrefutable in the context of these proceedings.

37 Those supporting the Lavigne Proposal argued vigorously that approval of the proposed sale transaction in advance of a creditors' vote on the Red Cross Plan of Arrangement (which has not yet been filed) would strip the Lavigne Proposal of its underpinnings and, accordingly, would deprive those "creditor" Transfusion Claimants from their statutory right under the Act to put forward a Plan and to have a vote on their proposed Plan. In my opinion, however, Mr. Zarnett's response to that submission is the correct one in law. Sections 4 and 5 of the CCAA do not give the creditors a right to a meeting or a right to put forward a Plan and to insist on that Plan being put to a vote; they have a right to request the Court to order a meeting, and the Court will do so if it is in the best interests of the debtor company and the stakeholders to do so. In this case I accept the submission that the Court ought not to order a meeting for consideration of the Lavigne Proposal because the reality is that the Proposal is unworkable and unrealistic in the circumstances and I see nothing to be gained by the creditors being called to consider it. In addition, as I have pointed out earlier in these Reasons, a large number of the creditors and of the Transfusion Claimants oppose such a development. The existence of a statutory provision permitting creditors to apply for an order for the calling of a meeting does not detract from the Court's power to approve a sale of assets, assuming that the Court otherwise has that power in the circumstances.

38 The only alternative to the sale and transfer, on the one hand, and the Lavigne Proposal, on the other hand, is a liquidation scenario for the Red Cross, and a cessation of its operations altogether. This is not in the interests of anyone, if it can reasonably be avoided. The opinion of the valuation experts is that on a liquidation basis, rather than on a "going concern" basis, as is contemplated in the sale transaction, the value of the Red Cross blood supply operations and assets varies between the mid - $30 million and about $74 million. This is quite considerable less than the $169 million

(+/-) which will be generated by the sale transaction.

39 Having rejected the Lavigne Proposal in this context, it follows from what I have earlier said that I conclude the purchase price under the Acquisition Agreement is fair and reasonable, and a price that is as close to the maximum as is reasonably likely to be obtained for the assets.

Jurisdiction Issue

40 The issue of whether the Court has jurisdiction to make an order approving the sale of substantial assets of the debtor company before a Plan has been put forward and placed before the creditors for approval, has been raised by Mr. Bennett. I turn now to a consideration of that question.

41 Mr. Bennett argues that the Court does not have the jurisdiction under the CCAA to make an order approving the sale of substantial assets by the Applicant Company before a Plan has even been filed and the creditors have had an opportunity to consider and vote on it. He submits that section 11 of the Act permits the Court to extend to a debtor the protection of the Court pending a restructuring attempt but only in the form of a stay of proceedings against the debtor or in the form of an order restraining or prohibiting new proceedings. There is no jurisdiction to approve a sale of assets in advance he submits, or otherwise than in the context of the sanctioning of a Plan already approved by the creditors.

42 While Mr. Kaufman does not take the same approach to a jurisdictional argument, he submits nonetheless that although he does not oppose the transfer and approval of the sale, the Court cannot grant its approval at this stage if it involves "sanitizing" the transaction. By this, as I understand it, he means that the Court can "permit" the sale to go through - and presumably the purchase price to be paid - but that it cannot shield the assets conveyed from claims that may subsequently arise - such as fraudulent preference claims or oppression remedy claims in relation to the transaction. Apart from the fact that there is no evidence of the existence of any such claims, it seems to me that the argument is not one of "jurisdiction" but rather one of "appropriateness". The submission is that the assets should not be freed up from further claims until at least the Red Cross has filed its Plan and the creditors have had a chance to vote on it. In other words, the approval of the sale transaction and the transfer of the blood supply assets and operations should have been made a part and parcel of the Plan of Arrangement put forward by the debtor, and the question of whether or not it is appropriate and supportable in that context debated and fought out on the voting floor, and not separately before-the-fact. These sentiments were echoed by Mr. Klein and by Mr. Thompson as well. In my view, however, the assets either have to be sold free and clear of claims against them - for a fair and reasonable price - or not sold. A purchaser cannot be expected to pay the fair and reasonable purchase price but at the same time leave it open for the assets purchased to be later attacked and, perhaps, taken back. In the context of the transfer of the Canadian blood supply operations, the prospect of such a claw back of assets sold, at a later time, has very troubling implications for the integrity and safety of that system. I do not think, firstly, that the argument is a jurisdictional one, and secondly, that it can prevail in any event.

43 I cannot accept the submission that the Court has no jurisdiction to make the order sought. The source of the authority is twofold: it is to be found in the power of the Court to impose terms and conditions on the granting of a stay under section 11; and it may be grounded upon the inherent jurisdiction of the Court, not to make orders which contradict a statute, but to "fill in the gaps in legislation so as to give effect to the objects of the CCAA, including the survival program of a debtor until it can present a plan": Re Dylex Limited and Others, (1995), 31 C.B.R. (3d) 106, per Farley J., at p. 110.

44 As Mr. Zarnett pointed out, paragraph 20 of the Initial Order granted in these proceedings on July 20, 1998, makes it a condition of the protection and stay given to the Red Cross that it not be permitted to sale or dispose of assets valued at more than $1 million without the approval of the Court. Clearly this is a condition which the Court has the jurisdiction to impose under section 11 of the Act. It is a necessary conjunction to such a condition that the debtor be entitled to come back to the Court and seek approval of a sale of such assets, if it can show it is in the best interests of the Company and its creditors as a whole that such approval be given. That is what it has done.

45 It is very common in CCAA restructurings for the Court to approve the sale and disposition of assets during the process and before the Plan if formally tendered and voted upon. There are many examples where this has occurred, the recent Eaton's restructuring being only one of them. The CCAA is designed to be a flexible instrument, and it is that very flexibility which gives it its efficacy. As Farley J. said in Dylex, supra (p. 111), "the history of CCAA law has been an evolution of judicial interpretation". It is not infrequently that judges are told, by those opposing a particular initiative at a particular time, that if they make a particular order that is requested it will be the first time in Canadian jurisprudence (sometimes in global jurisprudence, depending upon the level of the rhetoric) that such an order has made! Nonetheless, the orders are made, if the circumstances are appropriate and the orders can be made within the framework and in the spirit of the CCAA legislation. Mr. Justice Farley has well summarized this approach in the following passage from his decision in Re Lehndorff General Partner (1993), 17 C.B.R. (3d) 24, at p. 31, which I adopt:

> The CCAA is intended to facilitate compromises and arrangements between companies and their creditors as an alternative to bankruptcy and, as such, is remedial legislation entitled to a liberal interpretation. It seems to me that the purpose of the statute is to enable insolvent companies to carry on business in the ordinary course or otherwise deal with their assets so as to enable plan of compromise or arrangement to be prepared, filed and considered by their creditors for the proposed compromise or arrangement which will be to the benefit of both the company and its creditors. See the preamble to and sections 4, 5, 7, 8 and 11 of the CCAA (a lengthy list of authorities cited here is omitted).
>
> The CCAA is intended to provide a structured environment for the negotiation of compromises between a debtor company and its creditors for the benefit of both. Where a debtor company realistically plans to continue operating or to otherwise deal with its assets but it requires the protection of the court in order to do so and it is otherwise too early for the court to determine whether the debtor company will succeed, relief should be granted under the CCAA (citations omitted)

(emphasis added)

46 In the spirit of that approach, and having regard to the circumstances of this case, I am satisfied not only that the Court has the jurisdiction to make the approval and related orders sought, but also that it should do so. There is no realistic alternative to the sale and transfer that is proposed, and the alternative is a liquidation/bankruptcy scenario which, on the evidence would yield an average of about 44% of the purchase price which the two agencies will pay. To forego that purchase price - supported as it is by reliable expert evidence - would in the circumstances be folly, not only for the ordinary creditors but also for the Transfusion Claimants, in my view.

47 While the authorities as to exactly what considerations a court should have in mind in approving a transaction such as this are scarce, I agree with Mr. Zarnett that an appropriate analogy may be found in cases dealing with the approval of a sale by a court-appointed receiver. In those circumstances, as the Ontario Court of Appeal has indicated in Royal Bank v. Soundair Corp. (1991), 7 C.B.R. (3d) 1, at p. 6 the Court's duties are,

> (i) to consider whether the receiver has made a sufficient effort to get the best price and has not acted improvidently;
> (ii) to consider the interests of the parties;
>
> (iii)to consider the efficacy and integrity of the process by which offers are obtained; and,

(iv) to consider whether there has been unfairness in the working out of the process.

48 I am satisfied on all such counts in the circumstances of this case.

49 Some argument was directed towards the matter of an order under the Bulk Sales Act. Because of the nature and extent of the Red Cross assets being disposed of, the provisions of that Act must either be complied with, or an exemption from compliance obtained under s. 3 thereof. The circumstances warrant the granting of such an exemption in my view. While there were submissions about whether or not the sale would impair the Society's ability to pay its creditors in full, I do not believe that the sale will impair that ability. In fact, it may well enhance it. Even if one accepts the argument that the emphasis should be placed upon the language regarding payment "in full" rather than on "impair", the case qualifies for an exemption. It is conceded that the Transfusion claimants do not qualify as "creditors" as that term is defined under the Bulk Sales Act; and if the claims of the Transfusion Claimants are removed from the equation, it seems evident that other creditors could be paid from the proceeds in full.

Conclusion and Treatment of Other Motions

50 I conclude that the Red Cross is entitled to the relief it seeks at this stage, and orders will go accordingly. In the end, I come to these conclusions having regard in particular to the public interest imperative which requires a Canadian Blood Supply with integrity and a seamless, effective and relatively early transfer of blood supply operations to the new agencies; having regard to the interests in the Red Cross in being able to put forward a Plan that may enable it to avoid bankruptcy and be able to continue on with its non-blood supply humanitarian efforts; and having regard to the interests of the Transfusion Claimants in seeing the value of the blood supply assets maximized.

51 Accordingly an order is granted - subject to the caveat following - approving the sale and authorizing and approving the transactions contemplated in the Acquisition Agreement, granting a vesting order, and declaring that the Bulk Sales Act does not apply to the sale, together with the other related relief claimed in paragraphs (a) through (g) of the Red Cross's Notice of Motion herein. The caveat is that the final terms and settlement of the Order are to be negotiated and approved by the Court before the Order is issued. If the parties cannot agree on the manner in which the "Agreement Content" issues raised by Ms. Huff and Mr. Kaufman in their joint memorandum of comments submitted in argument yesterday, I will hear submissions to resolve those issues.

Other Motions

52 The Motions by Mr. Klein and by W. Lauzon to be appointed Representative Counsel for the British Columbia and Quebec Pre86/Post 90 Hepatitis C Claimants, respectively, are granted. It is true that Mr. Klein had earlier authorized Mr. Kaufman to accept the appointment on behalf of his British Columbia group of clients, but nonetheless it may be - because of differing settlement proposals emanating to differing groups in differing Provinces - that there are differences in interests between these groups, as well as differences in perspectives in the Canadian way. As I commented earlier, in making the original order appointing Representative Counsel, the Court endeavours to conduct a process which is both fair and perceived to be fair. Having regard to the nature of the claims, the circumstances in which the injuries and diseases inflicting the Transfusion Claimants have been sustained, and the place in Canadian Society at the moment for those concerns, it seems to me that those particular claimants, in those particular Provinces, are entitled if they wish to have their views put forward by those counsel who are already and normally representing them in their respective class proceedings.

53 I accept the concerns expressed by Mr. Zarnett on behalf of the Red Cross, and by Mr. Robertson on behalf of the Bank, about the impact of funding on the Society's cash flow and position. In my earlier endorsement dealing with the appointment of Representative Counsel and funding, I alluded to the fact that if additional funding was required to defray these costs those in a position to provide such funding may have to do so. The reference, of course, was to the Governments and the Purchasers. It is the quite legitimate but nonetheless operative concerns of the Governments to ensure the effective and safe transfer of the blood supply operations to the new agencies which are driving much of

what is happening here. Since the previous judicial hint was not responded to, I propose to make it a specific term and condition of the approval Order that the Purchasers, or the Governments, establish a fund - not to exceed $2,000,000 at the present time without further order - to pay the professional costs incurred by Representative Counsel and by Richter & Partners.

54 The other Motions which were pending at the outset of yesterday's Hearing are adjourned to another date to be fixed by the Commercial List Registrar.

55 Orders are to go in accordance with the foregoing.

BLAIR J.

6

Case Name:

L & L Tool Inc. v. General Motors Corp.

Between
L & L Tool Inc., plaintiff, and
General Motors Corporation and General Motors of Canada Limited, Pricewaterhousecoopers Inc., Michael James Anderson, Smith Lyons, and Gowling Lafleur Henderson LLP, defendants

[2004] O.J. No. 2785

[2004] O.T.C. 576

132 A.C.W.S. (3d) 9

Court File No. 004723

Ontario Superior Court of Justice

Low J.

Heard: May 18, 2004.
Judgment: June 29, 2004.

(71 paras.)

Practice -- Pleadings -- Striking out pleadings -- Grounds, issues which could have been raised in prior action between same parties.

Motion by the defendants General Motors, General Motors Canada and Pricewaterhouse Coopers to strike the plaintiff L&L Tool's claim against them. L&L sought an order for leave, nunc pro tunc, to commence the action against Pricewaterhouse. L&L was an auto parts maker that ran into significant financial difficulty in 1997 when its bank called its loan. Its assets were then sold by Pricewaterhouse as court-appointed receiver. L&L stated that GM, GMC and others were responsible for its loss and that Pricewaterhouse was responsible for its inability to prove its loss because it failed to safeguard L&L's records. GMC allegedly breached its agreement with L&L by failing to supply steel in a timely manner and supplying steel that was unfit for its purpose. GM's requirement that L&L ship its product express caused unexpected expenses. GM's failure to pay in a timely manner allegedly resulted in the bank calling L&L's loan. There had been two court applications in 1997 following L&L's financial difficulties. The applications were based on the premise that a Restructuring Agreement was valid. L&L now sought to assert that the Restructuring Agreement was void.

HELD: Motion allowed in part. The validity of the Restructuring Agreement was res judicata. If the court had been apprised of L&L's claims at the time of the previous applications, they would have been considered on the merits. Portions of the claim were struck. The claim against Pricewaterhouse would not necessarily fail and could be brought to trial. Leave was granted nunc pro tunc.

Statutes, Regulations and Rules Cited:

Courts of Justice Act, s. 142.

Ontario Rules of Civil Procedure, Rules 21.01(1)(b), 21.01(3)(d).

Counsel:

John L Finnigan and Deborah Palter for the moving parties, the defendants General Motors Corporation, General Motors of Canada Limited, and Pricewaterhouse Coopers Inc.

Harold Maltz for the responding party, the plaintiff L & L Tool Inc.

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1 **LOW J.**:-- In 1997, the plaintiff, an auto parts maker, ran into significant financial difficulty. Its bank called its loan and, later in that year, the plaintiff's assets were sold by a court appointed receiver, the defendant Pricewaterhouse Coopers Inc. (PW).

2 The plaintiff has launched this action claiming that some of the defendants are responsible for its loss of its business and undertaking which it claims was worth $35 million and that PW is responsible for its inability to prove its loss.

THE MOTIONS BEFORE THE COURT

3 This motion is brought by the defendants General Motors Corporation (GM), General Motors of Canada Limited (GMC) and Pricewaterhouse Coopers Inc. (PW) under rules 21.01(1)(b) and 21.01(3)(d) and s. 142 of the CJA to strike out the Amended Amended Statement of Claim as against them. The plaintiff brings a cross-motion for leave, nunc pro tunc, if leave be required, to commence the action against PW.

THE PLAINTIFF'S CLAIMS

4 The plaintiff claims against the defendants GM and GMC damages of $35,000,000 for breach of agreements under which plaintiff was to supply auto parts to GM and plaintiff was to purchase steel from GMC to produce the parts. It also claims a declaration that a written financial accommodation agreement made among it, the Bank of Montreal, GM, and GMC on February 14, 1997 is void and unenforceable. Plaintiff's position is that it entered into the written financial accommodation agreement under duress. It has pleaded also that the agreement and other agreements made at about the same time were breached by GM and GMC. It also asserts misrepresentation and breach of a duty of good faith.

5 The plaintiff claims against the defendants Michael Anderson and the law firms Smith Lyons and Gowling Lafleur Henderson damages of $35,000,000 for professional negligence. Those defendants are not parties to this motion.

6 The plaintiff claims against the defendant PW a mandatory order requiring it to return to the plaintiff its business, financial and banking records and, in the alternative, damages of $35,000,000 for spoliation of evidence.

BACKGROUND

7 As alleged in the statement of claim, the plaintiff made and supplied auto parts to the defendant GM under a contract or contracts made in Michigan and governed by Michigan law. As a condition of its parts supply agreement with GM, plaintiff was obligated to purchase steel from GMC to make the parts.

8 The plaintiff alleges that GMC breached its agreement with plaintiff by supplying steel that was not fit to be used in the manufacture of the parts and by failing to supply the steel in timely fashion to meet GM's delivery schedule. This resulted, it is alleged, in production delays on the part of the plaintiff and in rejection by GM of some parts made by plaintiff under the supply agreement.

9 GM required delivery of the parts on a "just in time" basis. This required a flow of parts to GM as and when the parts were required for installation. The usual mode of shipment was to be at the lowest rate and the cost was to be borne by GM, but if the plaintiff caused an inability to meet GM's delivery requirements, GM was entitled to require the plaintiff to ship by express freight at its own expense with GM paying shipping only at the lowest rate. The plaintiff pleads that the practice in the industry is that the parts supplier is required to ship express only if the usual transportation method would result in the auto manufacturer not having a sufficient supply of parts to ensure continuous production.

10 The plaintiff alleges that from April 1996 to January 1997, GM was in breach of the parts supply agreement because it required the plaintiff to ship express although it actually had a sufficient quantity of parts on hand to meet its production requirements and because the inability to meet GM's delivery requirement using the usual lowest cost transport was not caused by the plaintiff. Plaintiff alleges that the requirement by GM that plaintiff ship express caused it to incur an extraordinary and unexpected expense of $1.3 million. It is also alleged that in January 1997, in breach of the supply agreement, GM refused to pay the plaintiff $1.3 million owing for parts sold in the previous month.

11 On February 7 1997, the plaintiff's bank, the Bank of Montreal, made demand on its secured loan to plaintiff, requiring $4 million to be paid by February 17, 1997. It issued a notice of intention to enforce security under its general security agreement. Plaintiff pleads that at that time, GM owed plaintiff, net of set offs, $740,000 and failed to pay it, thus contributing to the bank's calling the loan and, implicitly, all of the sequelae thereof.

12 On February 14, 1997, the plaintiff, GM, GMC and the bank entered into a written agreement titled "Financial Accommodation Agreement" referred to in the pleading and hereinafter as the "Restructuring Agreement". The parties recited in the agreement that the plaintiff was in default to the bank and that the plaintiff had requested certain financial accommodation from the bank and from GM.

13 The Restructuring Agreement provided, inter alia, that GMC would buy an $800,000 participation in the plaintiff's secured debt to the bank, that the bank would forbear from enforcing its rights against the plaintiff, that GMC would provide working capital to plaintiff to continue and complete certain work, the working capital to be secured by the plaintiff's assets, that the plaintiff agrees to the appointment of a court appointed interim receiver, and that a failure on the part of the plaintiff, by May 7, 1997, to consummate, on terms reasonably acceptable to GM and to the bank, a sale of substantially all of its stock or assets or to restructure or recapitalize its business was an event of default by plaintiff under the agreement.

14 Pursuant to the Restructuring Agreement, PW was appointed as court appointed interim receiver under an order of the court made by Cameron J. (the Order) dated February 18, 1997. On the hearing of the motion, submissions were made by counsel for the bank, for GM and for the plaintiff.

THE ORDER APPOINTING THE RECEIVER AND ITS SEQUELAE

15 The Order provided, inter alia:

- that the plaintiff shall make best efforts to sell substantially all of the assets as a going concern or otherwise or to make a substantial investment in the plaintiff to discharge its

debt to the bank on or before March 14, 1997;

- that the plaintiff shall not enter into any sale agreement without the prior written approval of the bank and GM;
- that in the event that the plaintiff does not enter into a sale agreement as contemplated by the order, the interim receiver is authorized to offer the plaintiff's assets for sale as a going concern by private sale or as otherwise directed by the court;
- that the plaintiff shall deliver or otherwise make available to the interim receiver access to the assets and all books, securities, documents, contracts, deed, paper, records and accounts relating to the assets;
- that no legal actions shall be taken against the interim receiver with respect to the assets without leave of the court being first obtained;
- that the interim receiver shall incur no liability or obligation as a result of its appointment or the fulfillment of its duties in carrying out the order save and except for negligence or willful misconduct.

16 The plaintiff was not able to consummate a sale of its assets and it did not refinance either by the deadline or thereafter.

17 On June 27, 1997, in an application before this court wherein the bank, GM and GMC were applicants and the plaintiff was respondent, the parties attended on a motion for court approval of the sale of the plaintiff's assets by PW, the court appointed receiver. PW's report as interim receiver was filed in evidence before the court. The report, dated June 25, 1997, disclosed, inter alia:

- That on February 17 1997, GMC, which was owed $3.9 million by the plaintiff, assigned a portion of that receivable to GM in an amount equal to the amount owed by GM to the plaintiff;
- that on the same date notice of the assignment was given to the plaintiff;
- that on the same date, plaintiff signed a written acknowledgment of notice of the assignment, of the set off, and of the fact that GM was no longer indebted to plaintiff in any amount;
- that plaintiff had had discussions with GM and the bank but that no restructuring plan was put forward by the plaintiff that was acceptable to the bank or to GM;
- that plaintiff was unable to locate a third party interested in either acquiring substantially all of its asset or in investing in it sufficiently to allow the plaintiff to pay its debt to the bank on or before the deadline of March 14, 1997 which was extended at plaintiff's request;
- that GMC was the plaintiff's largest unsecured creditor;
- that the plaintiff had suffered operating losses of $233,000, $150,000 and $1,045,000 in 1994, 1995 and 1996 respectively and that it was insolvent as at February 17, 1997 in that it was not able to pay its liabilities generally when due and in that the net realizable value of its assets was less than its liabilities;
- that the total deficiency was $5,476,000 as at February 18, 1997;
- that because the plaintiff had been unable to find a third party buyer, PW negotiated an agreement of purchase and sale of the bulk of the plaintiff's assets, located at its Bowmanville plant, with a purchaser, REA International Inc, a company with which GM was prepared to negotiate the requisite arrangements to enable completion of the sale. The sale price was $1.5 million. PW negotiated a sale of other assets of the plaintiff located at Peterborough to a second purchaser, Continental Plants Canada, for $276,500;
- that the appraisals of the assets obtained by the interim receiver were $1,379,775 and $1072,225 for the Bowmanville assets and $417,205 and $359,350 for the Peterborough

assets;

- that following disbursement of anticipated sale proceeds, GM would be left with a shortfall in excess of $2,000,000 on account of its secured claim and there would be nothing available for distribution to the unsecured creditors of the company with claims totalling $4,285,000 as of the date of the Order appointing the interim receiver.

18 In its motion materials, PW recommended that the agreements of purchase and sale with REA and Continental be approved once executed and sought court authorization to complete the transactions.

19 Plaintiff did not file any material on the motion. It did not challenge the PW report. The plaintiff was represented at the hearing and did not oppose the motion.

20 An order was granted by my brother Cameron J. on June 27, 1997 approving PW's agreement of purchase and sale with REA and authorizing it to carry out the transaction.

PROCEEDINGS AFTER THE SALE OF PLAINTIFF'S ASSETS

21 On March 32, 1998, the defendant GM caused a petition in bankruptcy to be issued against the plaintiff. The plaintiff filed a notice disputing the petition arguing that without its books and records it could not be determined whether or not it was insolvent and pointing out that nothing was to be gained by the petition as all of the plaintiff's assets had already been disposed of. Plaintiff contended that GM still owed moneys to it and that valuable assets, principally back up tooling worth allegedly $1,179,803 was disposed of for no consideration by PW, GM or GMC. The petition in bankruptcy was subsequently withdrawn.

22 On September 30, 2002, the plaintiff issued its original statement of claim. It subsequently amended the claim to add PW as a party defendant but it did not seek leave of the court to do so.

THE CLAIM AGAINST PW

23 The claim against PW appears to be grounded primarily in negligence. Plaintiff asserts that PW had a duty to safeguard and return the plaintiff's records and that it has failed to do so or, alternatively, has destroyed the records. The plaintiff also pleads that it relies on the tort of spoliation of evidence.

24 The moving parties argue that the claim against PW ought to be struck because it was commenced without first obtaining leave, because PW is held immune from liability by the terms of the Order appointing it, and because the plaintiff has not properly pleaded the tort of spoliation of evidence such that all of the elements of the cause of action are present.

25 While the Order appointing PW as interim receiver grants it immunity against liability for acts done in the fulfillment of its duties, the Order also specifically exempts from immunity acts of negligence or willful misconduct. The plaintiff's pleading alleges both in the alternative. To the extent that the claim is that PW deliberately destroyed or withheld documents, willful misconduct is asserted. To the extent that the pleading alleges breach of duty, the claim sounds in negligence.

26 It is argued on behalf of the moving parties that the order of June 27, 1997 approving the sale of the assets by PW specifically authorizes it to deliver such documents and deeds as may be necessary or desirable in the opinion of PW to complete the sale. While the plaintiff acknowledges in argument that some of the documents of which it seeks return may arguably have been deliverable to the purchaser of the assets, there were also documents or classes of documents put into PW's possession that relate only to the plaintiff's own financial circumstances, for example, its bank reconciliations, bank statements, and general ledgers. It is said that such documents cannot legitimately have been delivered to the purchaser of the assets as part of the sale transaction.

27 I agree with the plaintiff to the extent that that I am not able to conclude that it is plain and obvious that plaintiff's claim on the point must fail. If PW took possession of and failed by negligence or willful misconduct to return documents that are the property of the plaintiff which were not properly deliverable to the purchaser of the assets, then the statutory immunity and the immunity under the Order arguably does not apply.

28 In relation to the claim of spoliation of evidence by PW, the moving parties argue that the pleading is bad in any case and should be struck as disclosing no reasonable cause of action. I have been referred to the decisions in Coriale (Litigation Guardian of) v. Sisters of St. Joseph of Sault Ste. Marie (1998), 27 C.P.C. (4th) 328 at 338 to 341, 41 O.R. (3d) 347 and Spasic Estate v. Imperial Tobacco (2000), 188 D.L.R. (4th) 577 at 586, 49 O.R. (3d) 699 (C.A.).

29 It is said that the plaintiff pleading the tort of spoliation of evidence must set out whether the documents were destroyed, altered or mutilated, the identity of the person said to have destroyed, altered or mutilated the documents, particulars of any special duty owed by the defendant in respect of the preservation of the documents, and that the acts of the defendant have made it impossible for the plaintiff to prove his claim.

30 Moving parties point out that at para. 71 of the plaintiff's pleading, the allegation is that the destruction of evidence by PW will "impair" the plaintiff's ability to prove the value of its business. The pleader has not used the word "impossible" and moving parties argue that the plea of any condition short of impossibility is fatal. Moving parties rely on the following passage in Spasic per Borins J.A.: "If it is established that the conduct of the respondents resulted in harm to the plaintiff by making it impossible for her to prove her claim, then it will be for the trail judge, in the context of a complete record, to determine whether the plaintiff should have a remedy."

31 Borins J.A. also stated, however, "I view the plaintiff's claim based on the tort of spoliation as an additional, or alternative, claim to be considered only if it is established that the destruction or suppression of evidence by the respondents results in the inability of the plaintiff to establish the other nominate torts pleaded in the statement of claim." Thus the tort of spoliation, even if it has grown beyond the character of an evidentiary principle and has acquired the status of an independent tort, is nevertheless not a "stand alone" tort. Rather, its adjudication must follow a finding that there has been failure on the part of the plaintiff to prove the primary cause of action, the documents relative to which have allegedly been destroyed, altered or mutilated. The "impossibility" referred to in Spasic thus refers simply to a failure to prove the primary cause of action and on the adjudication of the claim of spoliation, the question is whether the spoliation was the cause of the failure. If the plaintiff is able to make out his case on the primary cause of action, the spoliation will not have caused damage, and the matter will be at an end. It is an all or nothing proposition. It is therefore in my view sufficient, to communicate to the defendant the case he has to meet, to say that the spoliation of evidence has or will have impaired the plaintiff's ability to prove his primary cause of action. To impair a thing is, inter alia, to damage it or to make it ineffectual. On motions of this kind, a degree of latitude is to be afforded to the draftsman, and I am not persuaded that the word used clearly takes allegation out of the ambit of the tort of spoliation, itself a creature in the early stages of evolution in this jurisdiction.

32 The plaintiff argues that no leave is required for the bringing of the action against PW because the books and records of the plaintiff do not fall within the definition of Assets in the Order appointing PW as interim receiver. It is said that paragraph 8 of the Order refers to "all of the assets and all books, securities, documents..." suggesting that books and documents are something separate and apart from "assets". It is only where an action is contemplated against PW in respect of the "Assets" that leave is required. Whether in paragraph 8 of the Order the term "assets" includes the classes of property specifically named therein is not without difficulty, but I would read the general provision, paragraph 2 of the Order, as controlling. The plain meaning of the term "assets" is comprehensive. In my view, leave is required.

33 In Gallo v. Beber, [1998] O.J. No. 5357, Feldman J.A. held, quoting RoyNat Inc. v Allan (1988), 69 C.B.R. (N.S.) 245 (Alta. Q.B.), that "An application for leave to commence an action nunc pro tunc should be granted if to do so does not cause prejudice or any substantial injustice, and if leave would have been granted if it had been sought at the appropriate time. In the absence of prejudice, leave will generally be granted unless it is clear that there is no foundation

for the claim or the action is frivolous or vexatious." The moving parties have not shown that any prejudice would arise from the granting of leave nunc pro tunc, and in my view, the claim on its face is neither clearly without foundation nor clearly frivolous or vexatious. I would therefore grant leave nunc pro tunc.

THE CLAIMS AGAINST GM AND GMC

34 The plaintiff alleges that starting in the fall of 1996, GMC supplied steel to the plaintiff that was not fit for the manufacture of auto parts and that it failed to supply the steel in time to meet GM's delivery schedule. Reading the pleading liberally, I infer that the plaintiff is claiming damages for this breach and that its theory is that but for these breaches by GMC, the plaintiff would not have ultimately suffered the loss of its business which it contends was worth $35,000,000. The action was not clearly statute barred at the time the claim was issued on September 30, 2002. I therefore would not strike out the plaintiff's claim based on this alleged breach of contract on the part of GMC.

35 The plaintiff alleges that GM breached the parts supply contract. According to the pleading, the breaches took place from April 1996 to January 1997. The plaintiff pleads that the law of the state of Michigan applies to the parts supply contract. The court has received expert evidence as to the limitation period under the law of Michigan for contracts for the sale of goods. The limitation period is 4 years. It is apparent from the allegations in the pleading that the parts supply contract was one for the sale of goods. The limitation period would therefore have expired by February, 2001. The claim for damages for breach of the parts supply contract or contracts with GM is thus prima facie statute barred.

36 The plaintiff has raised, however, a question as to the tolling of the limitation period under Michigan law. The evidence of Mark Miller, expert for the plaintiff, indicates that the limitation period is tolled during the pendency of a prior lawsuit between the parties involving the same cause of action. Mr. Miller opines that because plaintiff responded to the petition in bankruptcy with a notice asserting, among other things, that GM breached the parts supply contract by failing to pay contracted amounts for parts and tooling, the limitation period for the cause of action asserted in this lawsuit was tolled during the time the bankruptcy petition was pending.

37 The evidence of William T. Burgess, expert for the moving parties indicates that under Michigan law, an extension or a tolling of a limitation period is available under very limited circumstances under the Michigan Tolling Statute. The statute requires that a complaint involving the same cause of action be filed to toll the statute of limitations. The limitation period will be tolled at the time the complaint is filed and a copy of the summons and complaint are served on the defendant. Mere notice to defendant of the plaintiff's intent to sue is insufficient unless the plaintiff has diligently tried to file and serve within the limitation period or there was a minor procedural defect in the filing and service within the limitation period and the defendant has actual notice that the plaintiff has attempted to commence action and tried to serve the process within the limitation period. Notice that the plaintiff plans to sue is insufficient as is the conduct of settlement negotiations. The limitation period is also tolled by disability, fraudulent concealment of the existence of a claim from the plaintiff, and, in insurance situations, where the insured is not notified of denial of claim until shortly before or after the limitation has run. These situations are of no relevance here.

38 What is required to toll the limitation period under Michigan law is that there be a claim asserted by the plaintiff against the defendant for the same cause of action in a prior proceeding which never reached adjudication. The court must have acquired jurisdiction over the defendant in respect of the cause of action for the limitation period to be tolled, and jurisdiction over the defendant is acquired by service of process. (Barczak v. Rockwell International Corporation, 68 Mich. App. 759 (1976)).

39 Mr. Burgess opines that the plaintiff's Notice Disputing Petition did not constitute a sufficient request for affirmative relief against GM and GMC to toll the statute of limitations. The plaintiff's document was not a lawsuit claiming relief against the defendants GM. The Michigan law requires a suit to have been commenced. Secondly, the notice disputing petition did not involve the same causes of action as those raised in the statement of claim. The issue at hand in the petition and notice disputing petition was the plaintiff's solvency. The issue in this action is whether GM is

liable in damages to plaintiff for the loss of its business and undertaking as a result of alleged breaches of a contract or contracts for the purchase of auto parts.

40 In my view, Mr. Miller fails to give effect to the significant distinction between commencing an action and making an allegation. The mere making of an allegation, even if contained in a document filed in court, does not constitute the bringing of an action. There is no positive assertion of a cause of action in the plaintiff's notice disputing the petition in bankruptcy and indeed, the forum and the vehicle do not contemplate that a positive claim for damages can be made.

41 Mr. Burgess has significant experience and qualifications in the area in which he offers an opinion to the court. He was a graduate of Yale Law School in 1984, clerked with the Michigan Supreme Court, has practised in the areas of commercial law, litigation, banking and real estate since 1985, has been a adjunct professor at the University of Detroit Mercy Law School teaching Uniform Commercial Code, and at the University of Michigan School of Business Administration teaching business law. Mr. Miller is an attorney licensed to practise law in the state of Michigan since 1984. Nothing more is disclosed as to his credentials.

42 I have considered the relative qualifications of the expert witnesses, their affidavits and the case authorities referred to in their affidavits. I prefer the evidence of Mr. Burgess on the issue before me and find that the 4 year limitation period was not tolled. The claim for damages for breach of the parts supply agreement will therefore be struck.

CLAIM OF INVALIDITY AND BREACH OF THE RESTRUCTURING AGREEMENT AND OTHER AGREEMENTS

43 The plaintiff seeks a declaration that the February 14, 1997, Restructuring Agreement is void and unenforceable. The plaintiff pleads that it entered into the agreement under duress.

44 Plaintiff also asserts that the Restructuring Agreement and other agreements made at the same time were breached by GM and GMC.

45 Paragraphs 49 - 58 and paragraphs 59 - 66 of the pleading deal with these issues.

46 These allegations go to impugn the legitimacy, first, of the appointment of the interim receiver and second, to challenge the legitimacy of the sale of plaintiff's assets by the interim receiver.

47 Paragraphs 49 to 54 are not pellucidly clear as to their import but paragraph 53 appears to allege that there were a multiplicity of agreements. Paragraph 50 appears to allege that the GM and GMC made representations to plaintiff to induce it to enter into agreements. Paragraph 52 alleges that on February 10 (four days prior to the signing of the Restructuring Agreement), the plaintiff's then lawyers, Smith Lyons, disclosed that it might have a conflict.

48 Paragraphs 59, 60 and 61 appear to allege breach of an agreement to pay market prices for parts that, at paragraph 60 is referred to as a request, and at paragraph 61 is referred to as an agreement. Paragraph 61 is particularly opaque: it reads:

> In breach of its agreement with GM and GM Canada and their obligation to act in good faith GM refused to pay market prices for parts supplied by L& L to GM.

49 Paragraphs 63 to 65 contain the complaint that GM and GMC refused to negotiate with three parties that plaintiff had located to submit offers to buy the plaintiff's business but instead would negotiate only with one supplier, REA International, the company that ultimately purchased assets from the interim receiver under approval obtained in the June 27, 1997 court order.

50 Paragraph 70 of the pleading claims damages of $35,000,000 against GM and GMC for "breach of contract, breach of its obligations to act in good faith, and misrepresentations". The essence of the plaintiff's claim is that it should be compensated for the loss of its business. The theory disclosed in the allegations in paragraphs 49 - 58 and 59 - 66 is that plaintiff would still be in possession of its business but for the existence and performance of the Restructuring Agreement that ultimately resulted in the court approved sale of plaintiff's assets by PW. Similarly, the paragraphs reveal plaintiff's theory that but for the failure of the defendants GM and GMC to abide by the side agreements made at the same time that the Restructuring Agreement was made, the plaintiff would either still be in possession of its business or the money realized on the sale of the business would have been substantially greater had the defendants GM and GMC agreed to a sale to one of the other prospective purchasers located by plaintiff.

51 The moving parties argue that all of these matters are res judicata.

52 I agree. Any issue as to the validity of the Restructuring Agreement and allegations of non- compliance by GM and GMC with that agreement and with contemporaneous agreements, if any, allegedly made to induce plaintiff to sign the Restructuring Agreement, are matters that could and should have been raised in the two applications to the court in 1997.

53 The Restructuring Agreement was made on February 14, 1997.

54 The Restructuring Agreement has been executed. The parties (including the bank, a non-party to this action) have changed their positions as a result of the Restructuring Agreement. Clearly the time to have challenged the enforceability of the agreement was before, and not after the provisions of the agreement had been executed by the various parties to it.

55 The subsequent actions of the parties and the Bank of Montreal (which is not a party to this action) and the steps taken in respect of the plaintiff's assets all flow from the Restructuring Agreement. The interim receiver was appointed pursuant to the Restructuring Agreement. The bank forbore pursuant to the Restructuring Agreement. GM and GMC advanced working capital pursuant to the Restructuring Agreement. The court approved sale of the assets flowed from the Restructuring Agreement. An attack on the Restructuring Agreement is a collateral attack on the February 17, 1997 Order appointing the interim receiver and the June 27, 1997 order approving the sale of assets.

56 Plaintiff was before the court on February 17. 1997 on the moving parties' motion to appoint a receiver and to obtain other relief. One of the main issues before the court was whether or not it should appoint a receiver.

57 That the Restructuring Agreement was made under duress was a matter that was clearly germane to the issue and could and should have been raised by the plaintiff in response to the motion if it had been of the view that the Restructuring Agreement was voidable for duress. The fact that the material filed by GM on the motion showed that plaintiff was agreeing to or was not opposing the appointment of a receiver was no impediment to plaintiff putting its own material before the court to show that its agreement was made under duress.

58 It was open to the plaintiff on February 17, 1997 to disclose to the court that it had a problem with its representation by the firm of Smith Lyons. It was open to the plaintiff to seek an adjournment to retain new solicitors and to file material if so advised. It was open to the plaintiff to oppose the motion. The plaintiff did none of these things. Instead, it permitted the court to proceed on the basis that it did not contest the material filed and did not oppose the relief sought.

59 The February 17, 1997 motion was not, however, the only occasion upon which the plaintiff could and should have raised its protests as to the enforceability of the Restructuring Agreement. The matter came on before the court on June 27, 1997, when PW, as court appointed interim receiver sought court approval to sell the plaintiff's assets under the February 17 Order which, in turn, was founded on the February 14 Restructuring Agreement. The issue before the court on that occasion was whether or not the court should approve the receiver's sale of the assets.

60 It was open to the plaintiff to make the claim at that time that it was not appropriate for the court to approve the asset sale by the receiver (at any price) because the order appointing it as receiver was made on the basis of an unsound foundation -- the Restructuring Agreement made under duress. It was open to the plaintiff to claim at that time that the other agreements made between it and GM and GMC as inducements to it to sign the Restructuring Agreement had been breached by GM or GMC and that it was therefore incorrect or unfair to permit the consequences of the Restructuring Agreement to unfold. It was open to the plaintiff to put evidence before the court that GM and GMC had refused to negotiate with three prospective purchasers that plaintiff had found if that was the case. It is not apparent from the statement of claim what amount those purchasers were prepared to pay - whether it was $35,000,000 or some figure less than that but higher than the amount obtained by the receiver from REA. One would assume that the latter was the case or the plaintiff would not appear to have a legitimate cause of complaint. Information that there were other willing purchasers, and in particular, prospective purchasers with richer offers, would have been very relevant to the court's determination as to the propriety of the receiver's sale to REA as there were unsecured creditors whose interests would be impacted by the quantum of recovery on the sale. Such information would also have been directly contrary to that in the PW report which plaintiff did not challenge.

61 I have no doubt that had the court been apprised of the plaintiff's allegations at that time, the issues would have been aired and determined on the merits. The enforceability of the Restructuring Agreement would have impacted on the soundness of the Order appointing the receiver and, in turn, on the propriety of the receiver selling the plaintiff's assets. It may be that the ultimate result to the plaintiff would have been no different in light of the fact that its bank was in a position to enforce its security, but that is a question going to the merits of the action.

62 Plaintiff did not raise with the court the propriety of the receiver selling plaintiff's assets and instead, permitted the court to proceed on the basis that the Order appointing the receiver was regular and that the Restructuring Agreement and consent of the plaintiff underlying the Order appointing the receiver was also regular.

63 As put by Vice-Chancellor Wigram in Henderson v. Henderson (1843), 3 Hare 100 at 115, 67 E.R. 313 at 319,

> ... where a given matter becomes the subject of litigation in, and of adjudication by, a Court of competent jurisdiction the Court requires the parties to the litigation to bring forward their whole case, and will not (except under special circumstances) permit the same parties to open the same subject of litigation in respect of matter which might have been brought forward as part of the subject in contest, but which was not brought forward, only because they have, from negligence, inadvertence, or even accident, omitted part of their case. The plea of res judicata applies, except in special cases, not only to points upon which the Court was actually required by the parties to form an opinion and pronounce a judgment, but to every point which properly belonged to the subject of litigation, and which the parties, exercising reasonable diligence, might have brought forward at the time.

64 The decision of Sharpe J., as he then was, in Las Vegas Strip Ltd. v. Toronto (City) (1996), 30 O.R. (3d) 286 at 293 et seq., aff'd [1996] O.J. No. 1513, is particularly helpful. The plaintiff launched an action seeking a declaration that a by-law prohibiting operation of a strip club was invalid. In prior proceedings, the plaintiff had been a defendant in an action in which a competitor, Zanzibar Tavern Inc., sought to restrain Las Vegas from operating a strip bar on the grounds that it was an illegal business under the City's adult entertainment by-law. While the focus of the facts pleaded in the action concerned the prior use of the premises, Zanzibar put squarely in issue the legal right of Las Vegas to carry on its operation. Sharpe J. held that there could be no doubt but that Las Vegas could have raised as a defence to the Zanzibar action the argument it sought to assert in its new action, that the By-law was invalid. Although a defence based on the invalidity of the By-Law would have been inconsistent with the defence of legal non-conforming use that Las Vegas did assert, the two defences could have been pleaded in the alternative.

65 Sharpe J. held that the failure of Las Vegas to come forward in the prior action with the invalidity defence was fatal to its attempt in its new action to advance that claim with a view to reversing the result in the Zanzibar action. He

referred to Glatt v. Glatt, [1937] S.C.R. 347 at p. 350, [1937] 1 D.L.R. 794, where the Supreme Court of Canada affirmed a judgment of the Ontario Court of Appeal in which Middleton J.A. had stated as follows, [1936] O.R. 75:

> It is I think clear beyond possibility of a doubt that a defendant who is sued must in the action in which he is sued put forward all defences which he has to the plaintiff's claim. He cannot allow the action to go to trial upon a certain defence which he sets up and when that defence fails set up another and inconsistent defence by bringing an action to set aside the judgment. If in the original action he applies for some relief, his application will be scrutinized with the greatest of care, but there would be no end to litigation if proceedings such as these received the sanction of the court.

66 Sharpe J. stated:

> Does the fact that Las Vegas now relies upon a different legal theory remove the present claim from the reach of the old? In my view it does not. The authorities establish that a litigant cannot establish a new and fresh cause of action by advancing a new legal theory in support of a claim based upon essentially the same facts. As was stated by the Privy Council in Hoystead v. Taxation Commissioner, [1926] A.C. 155 at pp. 165-66, [1925] All E.R. Rep. 56 (a passage quoted with approval by the Supreme Court of Canada in Maynard v. Maynard, [1951] S.C.R. 346 at p. 354, [1951] 1 D.L.R. 241 at p. 254, per Cartwright J.):
>
>> Parties are not permitted to begin fresh litigations because of new views they may entertain of the law of the case, or new versions which they present as to what should be proper apprehension by the Court of the legal result either of the construction of the documents or the weight of certain circumstances.
>>
>> If this were permitted, litigation would have no end, except when legal ingenuity is exhausted. It is a principle of law that this cannot be permitted, and there is abundant authority reiterating that principle."

67 As Binnie J. graphically put it in the more recent decision in Danyluk v. Ainsworth Technologies Inc. et al., [2001] 2 S.C.R. 460:

> The law rightly seeks finality to litigation. To advance that objective, it requires litigants to put their best foot forward to establish the truth of their allegations when first called upon to do so. A litigant to use the vernacular, is only entitled to one bite at the cherry ... A person should only be vexed once in the same cause. Duplicative litigation, potential inconsistent results, undue costs, and inconclusive proceedings are to be avoided.

68 To permit the plaintiff now to assert that the Restructuring Agreement was void and unenforceable will have far-reaching and mischievous consequences. The court has acted on two separate occasions, with the apparent approbation of the plaintiff, on the basis that the agreement was valid. Those were occasions when the validity of the agreement could and should have been put in issue if the plaintiff was of the view that the agreement was not valid. To attack the validity of the agreement now can only be a collateral attack on the court orders based upon it.

69 Insofar as the plaintiff alleges breaches of other alleged agreements in the paragraphs in question, those breaches go directly to the legitimacy of the sale of assets by the court appointed receiver and could and should have been raised at the time that the court was being asked to give its approval of the sale.

70 In my view, the allegations at paragraphs 29 - 58 and 59 - 66 and the claim for a declaration that the Restructuring Agreement is void and unenforceable ought to be struck out as abuse of process because the issues are res judicata.

71 If counsel are unable to agree as to costs, I may be spoken to upon arrangement with my assistant.

LOW J.

cp/e/nc/qw/qljml/qlkjg/qlbdp

7

Case Name:

Air Canada Pilots Assn. v. Air Canada Ace Aviation Holdings Inc.

Between
Air Canada Pilots Association, Plaintiff, and
Air Canada Ace Aviation Holdings Inc., Robert A. Milton, Montie R. Brewer, Marvin Yontef, David I. Richardson, Carlton D. Donaway and The Director appointed under the Canada Business Corporations Act, Defendants

[2007] O.J. No. 89

26 B.L.R. (4th) 124

28 C.B.R. (5th) 163

57 C.C.P.B. 204

154 A.C.W.S. (3d) 592

2007 CarswellOnt 123

Court File No. 06-CL-6672

Ontario Superior Court of Justice

P.A. Cumming J.

Heard: December 21-22, 2006.
Judgment: January 12, 2007.

(94 paras.)

Civil procedure -- Injunctions -- Interlocutory or interim injunctions -- The plaintiff pilots' association's motion for an interim interlocutory injunction enjoining the Ace Holdings Inc. from making further distributions of Air Canada's interests was dismissed -- The plaintiff was not a proper person to make an application under the Canada Business Corporations Act, nor had it established a serious issue to be tried -- Canada Business Corporations Act.

Corporations and associations law -- Corporations -- Actions -- Against corporation and directors -- Oppressive

conduct -- The plaintiff pilots' association's motion for an interim interlocutory injunction enjoining the Ace Holdings Inc. from making further distributions of Air Canada's interests was dismissed -- The plaintiff was not a proper person to make an application under the Canada Business Corporations Act, nor had it established a serious issue to be tried -- Canada Business Corporations Act.

The plaintiff pilots' association brought an oppression action seeking injunctive relief and a mandatory order requiring Ace Holdings Inc. (incorporated as part of the restructuring of Air Canada under the Companies' Creditors Arrangement Act) to return to the ownership of Air Canada all of its continuing interest in the Jazz Air LP, units of the Jazz Air Income fund (collectively, "Jazz"), Aeroplan Limited Partnership and units of the Aeroplan Income fund (collectively, "Aeroplan") to the extent that such were derived from the transfer to ACE from Air Canada of certain limited partnership units -- The plaintiff claimed to be a creditor of Air Canada with claims in excess of $1 billion, and claimed that as a result of the transaction the capital of ACE and Air Canada would be depleted, with the otherwise available capital base being reduced at a time when Air Canada faced significant cash obligations and requirements -- The plaintiff presently brought a motion seeking an interim interlocutory injunction enjoining ACE from making further or other distributions in excess of the accumulated consolidated net after-tax earnings of Air Canada since Sept. 30, 2004 -- HELD: The motion was dismissed, and the cross-motion granted -- The court declined to exercise its discretion to find that the plaintiff was a "proper person" to make an application under Part XX of the Canada Business Corporations Act -- To give effect to the plaintiff's motion at hand would introduce fundamental changes to the restructured enterprise as accepted and relied upon by investors who provided over $2 billion in new financing and equity -- The ACE directors were the ones properly charged with the responsibility of using their business judgment to assess the appropriateness of making distributions at any given point in time -- The plaintiff in effect sought to pre-empt that future business judgment by a present injunction -- Any issues raised in this action which touched upon issues adjudicated upon in the CCAA proceeding were barred by res judicata -- The plaintiff failed to meet the threshold test for injunctive relief, by failing to establish that there was a serious issue to be tried -- In seeking an injunction out of fear that Air Canada will again become insolvent or would be unable to finance its capital expenditure commitments, it was seeking remedial relief before there was even a real and credible possibility on an objective test that the event might occur -- The plaintiff had not established any basis upon which this Court could re-open through this collateral proceeding the agreements, constating documents and court orders under which the CCAA restructuring plan was completed -- The plaintiff was neither an employee of Air Canada nor a party to Air Canada's registered pension plan to which its members belonged -- The plaintiff's present and future members were, of course, employees entitled to wages, related benefit payments and pension benefits (from the pension plan trustee) as they became due in the future; but this did not constitute the plaintiff as a "creditor" of Air Canada in any legal sense, and in particular, within the meaning of s. 241(2) of the CBCA.

Statutes, Regulations and Rules Cited:

Canada Business Corporations Act, R.S.C. 1985, c. C-44, s. 192, s. 238(d), s. 241(2)

Companies Creditors' Arrangement Act, R.S.C. 1985, c. C-36,

Ontario Rules of Civil Procedure, R.R.O. 1990, Reg. 194, Rule 40.03

Counsel:

Richard B. Jones and Lynsey Connors, for the Plaintiff

Sean Dunphy and Kathy Mah, for the Defendants other than the Director appointed under the Canada Business Corporations Act

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REASONS FOR DECISION

P.A. CUMMING J.:--

Background

1 The plaintiff Air Canada Pilots Association ("ACPA") brings this action under Part XX of the *Canada Business Corporations Act*, R.S.C. 1985,c. C-44, as am. ("*CBCA*") seeking, *inter alia*, a declaration that the defendants threaten to effect results that are oppressive or unfairly prejudicial to the interests of the plaintiff as a putative creditor of the defendant Air Canada. ACPA seeks, *inter alia*, injunctive relief and a mandatory order requiring Ace Aviation Holdings Inc. ("ACE") to return to the ownership of Air Canada all of its continuing interest in the Jazz Air LP, units of the Jazz Air Income fund (collectively, "Jazz"), Aeroplan Limited Partnership and units of the Aeroplan Income fund (collectively, "Aeroplan") to the extent that such are derived from the transfer to ACE from Air Canada of certain limited partnership units. The 24 page Statement of Claim was issued October 4, 2006.

2 ACPA is the duly certified bargaining agent for some 3100 pilots flying for Air Canada and its affiliates, other than Jazz Air LP. Air Canada is a corporation continued under the *CBCA*, operating the largest airline in Canada. Jazz Air is a short haul regional airline. The ACPA collective agreement with Air Canada expires July 1, 2009.

3 Being insolvent, Air Canada filed for protection pursuant to the *Companies Creditors' Arrangement Act*, R.S.C. 1985, c. C-36 as am. ("*CCAA*") on April 1, 2003. Air Canada underwent an extensive and complex restructuring and rebirth under the direction of Mr. Justice James Farley of this Court. The completed restructuring resulted in a Sanction Order of this Court on August 23, 2004. The Sanction Order sanctioned the Consolidated Plan of Reorganization, Compromise and Arrangement of Air Canada and specific subsidiaries (the "Plan"). The Plan was implemented with effect from September 30, 2004.

4 ACE is a corporation incorporated June 29, 2004 under the *CBCA* as part of the *CCAA* restructuring. ACE, a public corporation, now holds all the issued and outstanding share capital of Air Canada. The four individual defendants are directors of Air Canada and except for Mr. Brewer (the President of Air Canada) are also directors of ACE.

5 Pursuant to the restructuring, several parts of Air Canada's former business were constituted as separate limited partnerships. The restructuring included the creation of ACE as a holding company having the ownership of Air Canada and five or six former Air Canada subsidiaries and unincorporated divisions converted into sister enterprises to Air Canada. These were constituted as separate "Holdco" Limited Partnerships, including Aeroplan Limited Partnership and Jazz Air LP, with Air Canada retaining preferred limited partnership units ("LP units") while ACE held the general partnership units ("GP units").

6 Under this arrangement, Air Canada ultimately retained preferred limited partnership units in exchange for the transfer of the business units to the limited partnerships. ACE became the general partner of the business partnerships.

7 In 2006, ACE caused Air Canada to transfer all its limited partnership units in the Jazz Air LP to ACE for $400 million and a promissory note of $83 million. Some 19.1% of Jazz Air LP was then sold to Jazz Air Income Fund.

8 The Aeroplan Income Fund was created in 2005 and acquired some 14.4% of the Aeroplan Limited Partnership from ACE.

9 On August 31, 2006, ACE issued a notice of special meeting of shareholders and a management proxy circular for a meeting to be held October 5, 2006 to consider a proposed corporate plan of arrangement of ACE (the "CBCA Arrangement") pursuant to s. 192 of the *CBCA*. More than 95% of the shareholders approved the *CBCA* Arrangement, which was then given approval by the Quebec Superior Court October 6, 2006, granting authority to the board of directors of ACE to proceed with special distributions of securities (such as income fund units) of its subsidiary entities by way of reduction of the stated capital of the shares of ACE.

10 The CBCA Arrangement authorizes the ACE board of directors to proceed with an initial special distribution of an indeterminate number of units in the Aeroplan Income fund. This initial distribution of Aeroplan units is to be within 90 days of completion of the CBCA Arrangement ie. by early January, 2007.This intention triggered the present motion on an urgent basis for an interim and interlocutory injunction. However, it is noted that ACPA did not oppose the proposed CBCA Arrangement at the approval hearing before the Quebec Superior Court but rather, at that hearing simply outlined the steps intended to be taken through this action in Ontario.

11 ACPA claims to be a creditor of Air Canada for amounts that vary and accrue from time to time. In particular, ACPA asserts present claims in excess of $1 billion arising from deficits in pension plans and funding obligations on the part of Air Canada. ACPA claims that the capital of ACE and its subsidiary Air Canada will be depleted by each of the contemplated distributions. ACPA says that as a result the otherwise available capital base would be reduced at a time when Air Canada faces significant cash obligations and requirements (in particular, for new aircraft and payments to reduce and eliminate the pension deficits).

The Motion for an Interim and Interlocutory Injunction

12 The hearing at hand deals with a motion brought by ACPA seeking an interim and interlocutory injunction enjoining ACE from, *inter alia*, making further or other distributions in excess of the accumulated consolidated net after-tax earnings of Air Canada since September 30, 2004. On December 28, 2006 I advised counsel for the parties that I was dismissing the motion for interim and interlocutory injunctive relief with Reasons for Decision to follow. These are my reasons.

13 The defendants have brought a cross-motion, seeking a declaration that ACPA is not a proper person to make an application under Part XX of the *CBCA* and further, that ACPA is without legal capacity to continue this action and hence, the action is to be dismissed in its entirety.

The Evidence

14 Captain Andrew J. Wilson, President of ACPA, is the affiant for the plaintiff in support of its motion. Mr. S.J. Isaacs, a Senior Vice President with ACE is an affiant for the defendants in respect of the motion at hand.

15 ACPA says it is not seeking to alter the Plan. Rather, it says that the issue that will go to trial through its action is whether or not Air Canada and ACE actually implemented the Plan as approved and authorized by the Sanction Order.

16 Mr. Isaacs was involved with the debt restructuring proceedings of Air Canada under the *CCAA* pursuant to the filing for protection April 1, 2003, which culminated in the Sanction Order dated August 23, 2004 by Justice Farley. The corporate restructuring of the old Air Canada contemplated a new structure whereby each business component would be competitive and self-sustaining as a means of attracting equity and debt financing necessary to exit *CCAA*.

17 Mr. Isaacs sets forth in his affidavit the history of related events as seen from his perspective. Mr. Isaacs states that some $8.3 billion in creditor claims were compromised pursuant to the Plan of which ACPA's claim on behalf of the pilots was some $300 million or about 3.6% of the total.

18 As stated above, the *CCAA* restructuring included the creation of ACE as a holding company having the ownership of Air Canada and five or six former Air Canada subsidiaries and unincorporated divisions converted into sister enterprises to Air Canada. These were constituted as separate "Holdco" Limited Partnerships with Air Canada retaining preferred limited partnership units ("LP units") while ACE held the general partnership units ("GP units").

19 The LP units represented the value of the assets of the relevant transferred business units of the old Air Canada as at September 30, 2004. The LP units were entitled to a fixed rate of return plus their fair market value as determined at September 30, 2004 (totaling $2.3 billion in the aggregate). Any future increases in value after September 30, 2004 would accrue to the benefit of the GP units. The preferred limited partnership units also received the right to receive a

cumulative income distribution of 5% of the freeze value.

20 For regulatory reasons, two subsidiaries of Air Canada, Touram Inc. (also known as "Air Canada Vacations") and Destina.ca Inc. were reorganized by retaining their corporate structure. Air Canada retained a preferred share interest in such former subsidiaries while ACE held all of the common shares. Thus, the restructuring in respect of these two entities paralleled substantively the restructuring in respect of the other business units through the formation of limited partnerships.

21 (As an aside, I mention that by reason of post-emergence reorganizations, and in particular the completion of Air Canada's November, 2006 Initial Public Offering, apart from Aeroplan, Jazz and Air Canada Technical Services ("ACTS"), the remaining sister businesses have largely been again placed underneath Air Canada).

22 In my view, it was apparent from the beginning of the restructuring process in April, 2003 that it was intended and necessary that there would not be any direct equity link between Air Canada and any of the other entities projected to be spun off. (See the Air Canada April 1, 2003 press release; the confidential April 30, 2003 Air Canada initial presentation and May 21, 2003 further detailed presentation to its affected labour groupings; and the August, 2003 presentation to potential equity investors).

23 In the Press Release of April 1, 2003, announcing the intended restructuring under the *CCAA* under the title "Corporate Restructuring" it is stated:

> Air Canada will also undertake a corporate reorganization that will create a new holding parent corporation, [ACE]. With separate business units for each of the activities in which the corporation is involved. ... As part of the reorganization all of Air Canada's equity interests in its existing subsidiaries including Aeroplan, Air Canada Technical Services, Jazz ZIP, Air Canada Vacations, Air Canada Capital and Destina will be directly owned, as sister companies by [ACE].

24 In my view, it would have been clear from the outset of negotiations that under the proposed structure a basic concept was that the equity interest in the former business units of Air Canada would be transferred to and held by ACE. ACE was the general partner in the limited partnerships and, by reason of the inherent nature of the so-called "freeze units" (ie. the LP units) so created, would benefit from all future growth in the value of the business units directly and not indirectly through its investment in Air Canada.

25 Although the tax plan was modified from the initial approach contemplated such that limited partnerships were employed rather than corporations to house the businesses of the spun off entities, the constant feature of the Plan was that Air Canada's interest in these entities was at all times fixed and this was the basis upon which substantial equity and exit financing was solicited and ultimately obtained.

26 To give effect to ACPA's motion at hand would introduce fundamental changes to the restructured enterprise as accepted and relied upon by investors who provided over $2 billion in new financing and equity.

27 Deutsceh Bank Securities Inc. ("DB") was a party to a Standby Purchase Agreement dated October 20, 2003, amended as of April 29, 2004 and approved by this Court May 4, 2004 whereby DB agreed to subscribe to a total of $850 million for any shares not acquired by Air Canada's creditors in the rights offering made available to them by the Plan.

28 A Global Restructuring Agreement ("GRA") between Air Canada and General Electric Capital Corporation ("GECC"), Air Canada's largest aircraft lessor (involving some 106 aircraft), was given Court approval January 16, 2004. This complex agreement included an exit facility of US $681 million to be made available upon emergence form *CCAA* proceedings as well as a financing agreement governing the acquisition of regional aircraft. Pursuant to the GRA, GECC was required to be satisfied regarding the business plan, ownership capital and governing structures affecting Air Canada upon emergence.

29 The RJ Financing Agreement included a commitment for a further US $950 million to finance the purchase of new regional aircraft. Court approval was given July 2, 2004 to an Investment Agreement dated June 23, 2004 with Cerebus ACE Investment LLC ("Cerebus") whereby Cerebus agreed to invest $250 million in ACE equity. This investment Agreement was conditional upon completion of the Standby Purchase Agreement with DB and the GRA.

30 The equity infusions and new credit commitments of over $2 billion were made by each of GECC, DB, Cerebus and the investors in ACE in reliance upon, among other things, the tax structure and corporate reorganization which placed the future growth value of the Air Canada sister companies with ACE while leaving the restructuring "freeze value" with Air Canada.

31 Air Canada and each of its trade unions entered into negotiations in May, 2003, resulting in significant labour cost saving arrangements. A major component of these agreements included Air Canada withdrawing a proposal to restructure its pension arrangements and thereby reduce the solvency deficiency associated with such pension arrangements, then totaling some $1.4 billion.

32 Air Canada and labour would jointly request from the Federal Government a program permitting Air Canada to reduce such solvency deficiency over a ten-year period instead of the usual five-year period provided by law.

33 On June 17, 2003, Air Canada and ACPA signed a memorandum of agreement governing concessions made by ACPA in the course of the collective bargaining undertaken under the supervision of Winkler J. of this Court. Although Air Canada's intentions to raise new equity based upon a corporate reorganization had been the subject of discussion, the memorandum of agreement signed did not contain any provisions relating to the form of the Air Canada restructuring plan nor any conditions regarding the proposed corporate re-organization or any condition requiring ACPA's consent thereto.

34 A main accomplishment of ACPA and the other union representatives was to obtain the agreement of Air Canada not to compromise pension and retirement benefits. In return, the unions supported Air Canada in its request for regulatory relief permitting the solvency deficit of some $1.4 billion to be amortized over 10 years.

35 The "Pension Beneficiaries Group" on October 31, 2003, provided Air Canada with a proposal as to how such 10 year funding arrangements might operate, expressly requesting protection in respect of "downside risk" if the parts of Air Canada were sold off with the proceeds of such sales distributed to shareholders and Air Canada as a remaining employer was not able to fund the residual initial solvency deficiency. Air Canada responded February 15, 2004 that the requested "downside protection" was not a subject Air Canada was prepared to negotiate.

36 A "term sheet" was ultimately negotiated and signed February 18, 2004 regarding the funding of the solvency deficiency over 10 years. The Pension Beneficiaries group specifically agreed in a memo delivered February 16, 2004 that "downside protection [was] off the table" and, accordingly, the term sheet contains no restrictions upon shareholder distributions.

37 On May 14, 2004, Air Canada entered into a protocol with the federal Office of the Superintendent of Financial Institutions ("OSFI") whereby OSFI agreed to recommend to the Government of Canada the adoption of a new regulation permitting Air Canada to amortize the solvency deficiency substantially on the basis set forth in the protocol of February 18, 2004 with the Pension Beneficiaries Group. The OSFI protocol further provided that there would be no deemed trust over any of Air Canada's assets pursuant to prior directions issued by OSFI and that Air Canada would issue a series of subordinated secured promissory notes totaling $346.6 million in favour of the trustees of Air Canada's pension plans. The protocol, given Court approval by an Order dated June 23, 2004, does not contain any restrictions upon Air Canada's or ACE's ability to make distributions. Nor do the Air Canada Pension Plan Solvency Deficiency Funding Regulations enacted August 9, 2004.

38 ACPA did not negotiate approval rights in respect of the Plan at closing nor would this seem to realistically have been possible in all the circumstances.

39 Court approval was given to Air Canada June 17, 2004 to enter into a new Commercial Agreement with Aeroplan, ACPA being a party to the proceedings. The ACPA collective agreement with Air Canada obliges Air Canada to ensure it retains its status as a primary outlet (Air Canada being only one of over 60 Aeroplan partners) for Aeroplan reward redemption flying; however, the collective agreement does not impose any restrictions in respect of the ownership of Aeroplan or the distribution of Aeroplan units.

40 The corporate structure of ACE approved in the *CCAA* proceeding was designed to allow for equity growth in Air Canada and the *separate* sister businesses to accrue to the benefit of the common holding company, ACE. The corporate structure of ACE was designed to allow for future distributions to ACE shareholders. New money was invested and loaned based upon such structure. The structure of ACE and its subsidiary businesses was known (or on an objective test should certainly have been reasonably known) by ACPA well before the *CCAA* Plan was finalized and sanctioned by Court Order. ACPA had an opportunity to negotiate and vote upon the *CCAA* Plan as sanctioned. Indeed, ACPA has benefited from the Plan inasmuch as Air Canada has arisen from its insolvent state to again prosper as a result of the *CCAA* Plan. The reasonable expectations of ACPA from the Plan are being met. ACPA cannot now fairly attempt to unwind the *CCAA* Plan and enhance its benefits in its own self-interest. The $2.1 billion received by Air Canada in exchange for its preferred limited partnership units was greater than the entire value of the overall ACE enterprise upon emergence from the *CCAA* proceeding.

41 Moreover, the so-called "business judgment rule" provides that

> ... the court should be reluctant to substitute its own opinion for that of the directors where the business decision was made in reasonable and informed reliance on the advice of financial and legal advisors appropriately retained and consulted in the circumstances. *CW Shareholdings Inc. v. WIC Western International Communications Ltd.* (1998), 160 D.L.R. (4th) 131 (Ont. Ct. Gen. Div.) at 150 and 152.

42 The ACE directors are the ones properly charged with the responsibility of using their business judgment to assess the appropriateness of making distributions at any given point in time. ACAP seeks to enjoin future unknown acts of directors in respect of possible distributions based upon circumstances at such future points of time. ACPA has no idea what the future financial condition of ACE or Air Canada will be at the time of any such consideration as to a distribution. ACPA in effect seeks to pre-empt that future business judgment by a present injunction.

43 ACPA is bound by the Sanction Order and cannot seek to vary or amend it in collateral proceedings. The Sanction Order provides in para. 29

> 29. **THIS COURT ORDERS** THAT, AS AT THE completion Time, each and every one of the Affected Unsecured Creditors will be deemed to forever release, waive and discharge all claims, obligations, suits, judgments, damages, demands, debts, rights, causes of action and liabilities (including any remedies to challenge transfers which may fall within the scope of any bulk sales, fraudulent conveyance or similar statute), whether liquidated or unliquidated, fixed or contingent, matured or unmatured, known or unknown, foreseen or unforeseen, then existing or thereafter arising, in law, equity or otherwise that are based in whole or in part on any act, omission, transaction, event or other occurrence taking place on or prior to the Completion Time in any way relating to the Applicants, the Newco's, the CCAA Proceedings or the Plan (for greater certainty including the Business Restructuring) against: (i) the Applicants and the Newco's (other than Excluded Clams, Post-Filing Clams and the rights to enforce the Applicants' and Newcos' obligations under the Plan and the securities, contracts, instruments, releases and other agreements and documents delivered thereunder or entered into in connection therewith or pursuant thereto); (ii) the directors, officers and employees of the Applicants in each case as of the Date of Filing (and in addition, those who become officers and/or directors and employees thereafter but on or prior to the Completion Time), (iii) the former directors, officers and

> employees of the Applicants and the Newco's, (iv) Persons who may claim contribution or indemnification against or from the Applicants, or (v) the respective current and former legal counsel and other advisors or professionals of the entities referred to in subclauses (i)-(iii) of section 5.2(2) Plan (including the Monitor, its counsel and its current officers and directors, and the current and former officers, directors, employees, shareholders and professionals of the released parties), acting in such capacity, provided that nothing herein will release or discharge a released party if the released party is judged by the express terms of a judgment rendered on a final determination on the merits to have committed fraud or willful misconduct or to have been grossly negligent, or, in the case of directors or officers, in respect of any claim referred to in section 5.1(2) of the CCAA.

44 The matters resolved by the *CCAA* Plan and Sanction Order are *res judicata* through issue and/or cause of action estoppel. The doctrine of *res judicata* prevents relitigation of matters which have already been determined by a court of competent jurisdiction. See *Danyluk v. Ainsworth Technologies Inc.,* [2001] 2 S.C.R. 460 at para. 20.

45 ACPA's claim in the action at hand, in effect, seeks to directly attack the *CCAA* Plan and Sanction Order of 2004. Any issues raised in this action which touch upon issues adjudicated upon in the *CCAA* proceeding are barred by *res judicata.* The *CCAA* Plan was a final judicial determination of the rights between Air Canada and ACPA and others in respect of the issues that arose in the restructuring. Paragraph 29 of the Sanction Order is clear in respect of foreclosing any claims regarding the completion of the corporate reorganization through the restructuring.

46 As well, the Quebec Superior Court issued a final order October 6, 2006, approving the ACE CBCA Arrangement which authorizes the board of directors of ACE to make future special distributions by way of reduction of capital. This was a final decision pronounced by a Court of competent jurisdiction over the parties and subject matter which involved the same issues or course of action being advanced in the litigation at hand. The parties to the Quebec proceeding included ACPA who were notified, attended, and thereby attorned to the jurisdiction of the Quebec Court, without taking issue with that Court's jurisdiction.

47 ACPA does not assert fraudulent misrepresentation. Rather, ACPA says that it did not realize that Air Canada did not retain equity in the businesses (Aeroplan, Jazz, etc.) spun off as sister businesses under ACE as the common holding company in the restructuring. ACPA says it did not understand that Air Canada would not participate as an equity participant in any future growth in the value of those sister businesses.

48 This position seems disingenuous. First, in my view, the materials culminating in the restructuring provide the natural and logical inference that ACE is the holding corporation for all the businesses in issue, with Air Canada simply in a horizontal relationship to the spun off sister businesses (Aeroplan, Jazz, ACTS, etc.) with no continuing equity position for Air Canada in respect of future growth of those businesses. Given the sophisticated expert advice available to ACPA throughout the restructuring negotiations, it seems improbable that ACPA would not be advised correctly and precisely as to the true nature of the economic and legal relationships in respect of the subject businesses.

49 On July 12, 2004 Air Canada mailed its Circular in respect of the creditors' meeting called to vote upon the *CCAA* Plan as authorized by an Order of the Court dated July 9, 2004. The Circular was also a prospectus in respect of the ACE shares that Air Canada creditors were being offered under the Plan and under the $850 million rights offering. The Circular described the corporate restructuring by which Air Canada's ownership interest in Aeroplan, Jazz and ACTS were to be transferred to ACE and the order in which the very complex series of transactions were to occur. The Circular noted (at page 57) that prior to the compromise of the $8.3 billion in unsecured claims through creditors being offered securities of ACE, and prior to new equity being invested through the rights offering, Air Canada would transfer its limited partnership units in Aeroplan and the other business units to separate "Holdco" partnerships in exchange for the issuance to Air Canada of "preferred limited partnership units" of each of the Holdco partnerships. (This was done pursuant to s. 5.1(1)(m) of the Plan.) The value being offered to Air Canada creditors consisted of simply the possibility of future value accruing in ACE. With some $8.3 billion in creditors' claims compromised through the restructuring, the

unsecured creditors of Air Canada received shares in ACE which represented about 10 cents to the dollar in recovery of their claims as creditors of the old Air Canada.

50 The July, 2004 Circular was first sent in draft form to the Service List on June 29, 2004. ACPA concessions as part of the restructuring were agreed to well in advance of the release of the Circular. ACPA signed a Memorandum of Agreement June 17, 2003 and a further Memorandum of Agreement on June 4, 2004 relating to its concessions. ACPA was a party to a term sheet signed February 18, 2004, between Air Canada and its pension beneficiary group relating to the funding of the solvency deficiencies in Air Canada's pension plans.

51 Thus, the *preferred* limited partnership units retained by Air Canada in the Aeroplan, Jazz and ACTS limited partnerships all had the same characteristics, namely, a right to receive on redemption a fixed or "freeze" value (being the values of the underlying assets transferred into the limited partnership, to a total of about $2.3 billion, established by independent valuators). In part, the complexity of the step transactions was necessitated from a tax planning standpoint to preserve Air Canada's tax accounts and the tax value of its loss carryforwards. The freeze values compare favourably with the trading value of ACE shares immediately following upon completion of the restructuring and, indeed, the values realized by ACPA through ACPA's sale in the market of all of the ACE shares received by ACPA through the rights offering.

52 With the filing by Aeroplan of a prospectus June 22, 2005, offering to the public units in an Aeroplan Income Fund, Air Canada transferred its preferred limited partnership units to ACE and received the full "freeze value" plus accrued but unpaid distributions, totaling some $1.012 billion.

53 Similarly, on January 25, 2006, ACE paid to Air Canada $452 million for its preferred limited partnership units in Jazz.

54 As well, ACE has recently purchased the preferred limited partnership units held by Air Canada in respects of ACTS for $672 million, representing the freeze value plus accrued distributions.

55 ACPA does not allege fraud. Even if could be found there was a misrepresentation (and I do not make any such finding) on the part of one or more of the defendants in the course of the restructuring, ACPA's assertion amounts to nothing more than such constitutes an innocent misrepresentation. ACPA does not seek rescission (which would not be available in any event given implementation of the Plan) and an innocent misrepresentation would not constitute actionable oppression.

56 Second, even if ACPA was somehow under a misunderstanding as to Air Canada's and ACE's relationship to the sister businesses, there is nothing in the evidentiary record to support an allegation of innocent misrepresentation. At most, ACPA can say it misunderstood matters; not that matters were misrepresented to it.

57 Third, even if it could be somehow said there was an arguable innocent misrepresentation, such does not survive the completion of the restructuring. The August 23, 2004 Sanction Order, *inter alia*, specifically released (in paragraph 29) all claims (including those of the plaintiff) arising from implementation of the corporate reorganization.

58 A Sanction Order is intended to bring certainty and finality to the restructuring process. This is critical to the proper functioning of the marketplace and the commercial expectations and reliance placed upon new contracts and property rights following upon the completion of the restructuring. ACPA did not appeal or seek to vary the Sanction Order.

59 In reality, ACPA attacks the finality of the Sanction Order. ACPA seeks to alter the terms upon which some $8.3 billion in Air Canada creditor claims were converted into 45.7 million ACE shares, some $1.1 billion in fresh funds were solicited from creditors and others to acquire equity in ACE ($250 million from Cerebus and $850 million through a rights offering) and upon which almost $800 million in post-restructuring convertible debt and equity has been raised by ACE. ACPA advances through this proceeding a collateral attack upon both the August 23, 2004, Sanction Order

and the October 6, 2006, approval Order of the Quebec Superior Court in respect of the CBCA Arrangement. In my view, the matters ACPA seeks to enjoin are *res judicata*.

60 ACPA seeks to re-assemble the pre-restructuring corporate structure and trap the value of Aeroplan, Jazz and other divisions historically underneath Air Canada for the benefit of the ACPA members. Paradoxically, this would leave the other creditors who gave up some $8 billion in creditor claims and those creditors and others who purchased shares in ACE, or extended credit to ACE, in reliance upon the finality and sanctity of the restructuring, at a severe disadvantage. Although ACPA members are in a stronger, more economically protected position because of the restructuring of the previously insolvent Air Canada, ACPA would now seek to appropriate to itself other values realized through the restructuring.

61 To obtain the requested injunctive relief ACPA must establish a strong *prima facie* case, that it will suffer irreparable harm if the injunction is not granted and that the balance of convenience favours ACPA.

62 In my view, and I so find, ACPA has failed to meet the threshold test for injunctive relief in an oppression claim. First, ACPA has failed to demonstrate through the evidentiary record a strong *prima facie* case. At the least, in seeking an interim and interlocutory injunction through the oppression remedy in anticipation of perceived harm in the future, a plaintiff should have to meet the higher threshold test of a "strong *prima facie* case". *Stern v. Imasco Ltd.* (1999), 1 B.L.R. (3d) 198 (Ont. Sup. Ct.) at para. 32; *Gazit (1997) Inc. v. Centrefund Realty Corp*, [2000] O.J. No. 3070 (Ont. Sup.Ct.) at para. 77.

63 Indeed, in my view, ACPA has not even established that there is a serious issue to be tried. ACPA's motion is premised upon speculative threatened or future harm. ACPA seeks an injunction out of fear that Air Canada will again become insolvent or will be unable to finance its capital expenditure commitments. ACPA seeks remedial relief before there is even a real and credible possibility on an objective test that the event may occur. ACPA speculates through its counsel that in 2009 there will be a "train wreck" with a second restructuring necessitated. This is not a sufficient ground to support an oppression application within the ambit of s. 241(2) of the *CBCA*. The general principle with *qua timet* injunctions is that there must be a high degree of probability that harm will in fact occur. *Operation Dismantle Inc. v. Canada*, [1985] 1 S.C.R. 441 at 458.

64 The test for a *qua timet* injunction is: there is a substantial issue to be tried that the impugned conduct constitutes an actionable violation of rights; there is a high degree of probability that harm is imminent; the apprehended harm will be irreparable; and the balance of convenience favours the granting of the order. *Mondavio Productions Ltd. v. Neverland Studios Ltd.,* [1994] O.J. No. 1814 (Ont. Ct. Gen. Div.) at para. 22; *Vanswan Properties Inc. v. Peckham* (1999), 2 C.P.R. (4th) 537 (Ont. Sup. Ct.) at p. 542. ACPA has not met any of these requirements.

65 Moreover, the *CBCA* does not expressly protect against merely threatened' anticipatory oppression. *Bank of Montreal v. Dome Petroleum Ltd.* (1987), 67 C.B.R. (N.S.) 296 (Alta. Q.B.) at 307; Markus Koehnen, *Oppression and Related Remedies* (Toronto: Canada Limited, 2004) at 50.

66 In my view, and I so find, ACPA has not established any basis upon which this Court can re-open through this collateral proceeding the agreements, constating documents and Court Orders under which the *CCAA* restructuring Plan was completed.

67 Second, irreparable harm refers to the nature of the harm suffered rather than its magnitude. It means harm which cannot be quantified in monetary terms. *RJR-Macdonald Inc. v. Canada (Attorney General),* [1994] 1 S.C.R. 311 at 341. ACPA has failed to establish that it will face irreparable harm if the injunction is not granted. The claimed potential future harm put forward is purely speculative. There is not any cogent evidence to support the existence of irreparable harm. There must be proof of the actual existence of irreparable harm. *Centre Ice Ltd. v. National Hockey League* (1994), 53 C.P.R. (3d) 34 (F.C.A.) at 52. Indeed, ACPA's affiant Captain Wilson admits in effect (at paragraph 63 of his affidavit) that the contemplated harm to ACPA members is speculative.

68 As a result of the above restructuring transactions, Air Canada's liquidity as a newly public company is some $1 billion higher than ACE's consolidated liquidity was in 2004. There is no real evidence purporting to establish irreparable harm to ACPA or its members if the injunction were not granted. In contrast, the uncontradicted evidence of the defendants is that to grant the injunction could well result in a loss of investor confidence and impair Air Canada's access to capital markets.

69 Finally, the balance of convenience favours the defendants. The balance of convenience is a determination of which of two parties will suffer the greater harm from the granting or refusal to grant interim and interlocutory injunctive relief pending a decision as to the merits. Air Canada is meeting its liabilities as they fall due, has raised $200 million in equity through a recent Initial Public Offering, and has increased its committed bank financing by some $150 million. There is no prospect of ACPA being able to compensate ACE shareholders for their opportunity cost in being unable to monetize their equity through distributions during the duration of an interim and interlocutory injunction.

70 As well, ACPA declines to offer the normative undertaking as to damages if an interlocutory injunction were to be granted. Rule 40.03 of the Rules of Civil Procedure RRO 1990, Reg. 194 requires such an undertaking unless the Court orders otherwise. It is exceptional to authorize an interlocutory injunction without the required undertaking. *Jagtoo v. 407 ETR Concession Co.* [1999] O.J. No. 4944 (Ont. Sup. Ct.) at para. 49; *Airport Limousine Drivers Association v. Greater Toronto Airports Authority*, [2005] O.J. No. 3509 (Ont.Sup. Ct.) at para. 156. ACPA does not advance any real argument as to why exceptional treatment should be extended in the instant case.

71 ACPA makes a vague allegation of misrepresentation on the part of Air Canada and the defendants in the course of the restructuring negotiations. In reality, ACPA is not able to point to any express misrepresentation on the part of the defendants. ACPA does not point to reliance on any statement made by any defendant. Mr. Wilson allowed in his cross-examination that he had not read the Circular/Plan.

72 Rather, in effect, ACPA says it did not understand that preferred limited partnership units meant that such units were in the nature of "freeze units" such that Air Canada would not participate in any equity growth in respect of the business operations being moved into the limited partnerships under the control of ACE. In my view, on an objective test basis, the preface of "preferred" to the limited partnership units would lead to the inference by a reasonable person that such partnership units were not participating in equity growth.

73 ACPA asserts that given the interrelationship between ACPA and Air Canada that there was a positive duty on the part of ACE to expressly disclose that any future appreciation of equity value in the sister businesses would accrue to ACE. ACPA asserts that this aspect of the structure was not visible in the consolidated financial statements following the restructuring.

74 The defendant corporations were not obliged to make further disclosure to ACPA and they were never asked for any explanation by ACPA as to the rights attaching to the "preferred limited partnership units".

Does ACPA have standing under Part XX of the *CBCA?*

75 ACPA claims that it is a proper person to make an application under Part XX of the *CBCA*. A "complainant" is defined in s. 238(d) of the *CBCA* as including "any other person who, in the discretion of the court, is a proper person to make an application. ..." ACPA asks this Court to exercise the discretion conferred upon it by statute to recognize ACPA as a proper person to bring forward its claim of oppression.

76 ACPA says that it was an affected unsecured creditor in the *CCAA* proceeding and therefore that it properly has standing to bring its application for oppression. ACPA submits that it is a creditor of Air Canada with a special relationship of dependence and vulnerability analogous to a complainant who is a minority shareholder in the position of having reasonable expectations of management. ACPA does not complain of any breaches of the employment relationship in respect of its member pilots. ACPA is not a creditor of ACE nor does ACPA have any direct relationship with ACE.

77 ACPA does not plead any breach of contract, does not make any allegation as to actual or imminent insolvency, does not offer any expert evidence and offers only the affidavit evidence of the head of ACPA whose personal knowledge of the material facts seems limited.

78 The defendants say that ACPA is an unincorporated association, being a trade union certified to represent Air Canada's currently employed pilots for collective bargaining purposes under the *Canada Labour Code*, R.S.C. 1985, c. L-2. As such, ACPA exercises its statutory agency on behalf of the pilots within the limits of its enabling statute. ACPA does not itself supply any services to Air Canada and is not a creditor of Air Canada in its own right. The pilots are not creditors of Air Canada other than in the ephemeral sense of being employees receiving wages from time to time and there is no issue of outstanding unpaid wages.

79 ACPA is not itself a party to, or beneficiary of, Air Canada's registered pension plans to which the ACPA pilots belong. While Air Canada has obligations to its retired pilots in respect of a trusted supplementary retirement plan as well as other post retirement benefits these obligations are currently being met. Moreover, virtually all of the claims ACPA purports to represent (that is, in reality those of Air Canada's pilots) in this proceeding were unaffected claims in the 2004 restructuring (being either pension or post-retirement benefits or future wage claims). The "Affected Unsecured Claims" held by ACPA were sold by ACPA within days of the Sanction Order and prior to emergence.

80 ACPA, as with other creditors, was entitled to receive a combination of equity in ACE, and the right to subscribe for further equity in ACE, in full satisfaction of its $300 million restructuring claim. ACPA used the total proceeds of the sale of its affected unsecured claim to subscribe for the maximum amount of equity in ACE that it was entitled to acquire under the Plan pursuant to the rights offering price of $20.00 per share. ACPA then sold such shares for proceeds of $23.75 per share prior to the closing of the restructuring. As such, ACPA had no direct interest in the Plan as an affected unsecured creditor claimant at the time of its completion.

81 Section 241(2) of the *CBCA* refers to actionable grounds as:

> (2) **Grounds** - If, on an application under subsection (1), the court is satisfied that in respect of a corporation or any of its affiliates
>
> (a) any act or omission of the corporation or any of its affiliates effects a result,
> (b) the business or affairs of the corporation or any of its affiliates are or have been carried on or conducted in a manner, or
> (c) the powers of the directors of the corporation or any of its affiliates are or have been exercised in a manner
>
> that is oppressive or unfairly prejudicial to or that unfairly disregards the interests of any security holder, creditor, director or officer, the court may make an order to rectify the matters complained of.

82 An applicant must have some nexus to the alleged harm, such that the applicant has a real interest in bringing the litigation based upon the applicant's relationship with the alleged oppressive party. *Re Sammi Atlas Inc.* (1997), 49 C.B.R. (3rd) 165 (Ont. Ct. Gen. Div.) at para. 6.

83 ACPA alleges that if ACE is allowed to carry out its CBCA Arrangement and make distributions to its own shareholders, Air Canada may be unable to pay the wage and pension obligations owed by Air Canada to the members of ACPA under the Collective Agreement.

84 In my view, the essential nature of ACPA's claim at hand relates to future wages and future pension benefits which are governed by the Collective Agreement. ACPA, in effect, is seeking to obtain through the action at hand

protections it was unable to obtain in the *CCAA* proceeding and the collective bargaining conducted within the context of that proceeding. Moreover, if ACPA were to have an arguable grievance, ACPA's exclusive remedy is one of arbitration through the collective agreement. *Weber v. Ontario Hydro*, [1995] 2 S.C.R. 929 at 953. See also *St. Anne Nackawic Pulp & Paper Co. Ltd. v. Canadian Paper Workers Union, Local 219*, [1986] 1 S.C.R. 704 at 718-719.

85 ACPA itself is neither an employee of Air Canada nor a party to Air Canada's registered pension plan to which ACPA members belong. ACPA's present and future members are, of course, employees entitled to wages, related benefit payments and pension benefits (from the pension plan trustee) as they become due in the future. In my view, this does not constitute ACPA a "creditor" of Air Canada in any legal sense, and in particular, within the meaning of s. 241(2).

86 Corporations and their directors do not generally owe creditors any special duty of care or fiduciary duty. *Peoples Department Stores Inc. (Trustee of) v. Wise*, [2004] 3 S.C.R. 461 at para. 67. There are exceptional, limited circumstances where creditors have established that a reasonable expectation has been created that a corporation's affairs would be conducted so as to protect the creditor's interests, in which courts have held that a creditor is a "proper person" to bring an oppression application. See for example *First Edmonton Place Ltd. v. 315888 Alberta Ltd.*, [1988] A.J. No. 511 (Alta. Q.B.) at 20; *Waiser v. Deahy Medical Assessments Inc.*, [2006] O.J. No. 224 (Ont. Sup. Ct.) at para. 34; *Leon Van Neck & Son Ltd. v. McGorman,* [1998] O.J. No. 4813, affirmed (2000), 135 O.A.C. 293 (Ont. C.A.).

87 In the situation at hand, it is the assets of ACE, not of Air Canada, which may be distributed to its shareholders pursuant to the CBCA Arrangement. The evidentiary record does not establish any reasonable expectation on ACPA's part that ACE's affairs would be conducted in respect of making distributions so as to protect the interests of ACPA.

88 In my view, and I so find, neither ACPA nor its members constitute a "proper person" to be a "complainant' within the meaning of s. 238 of the *CBCA*.

89 The defendants also assert that ACPA, as an unincorporated association, is not a legal entity. The defendants argue that, as such, ACPA does not have legal capacity to bring the action at hand. Given my finding that ACPA is not a "proper person" to bring this action as an application for relief from oppression under Part XX of the *CBCA* it is not necessary to deal with this assertion by the defendants.

90 I mention, as an aside, and as stated to counsel in the course of their submissions, that Rule 12.08 allows the Court to authorize a trade union to bring a proceeding on behalf of its members for the benefit of all. Had I found ACPA to be a proper person to pursue its claim under Part XX of the *CBCA*, in my view, ACPA could properly be authorized to continue the proceeding under Rule 12.08.

Disposition

91 For the reasons given, the motion by ACPA for an interim and interlocutory injunction is dismissed.

92 The entirety of the statement of claim of ACPA is based upon a claim of oppression and seeking consequential remedies under Part XX of the *CBCA*. The underlying premise is that ACPA is a "proper person" to make an application under Part XX and that this Court should exercise its discretion to so find. Given the evidentiary record, this Court declines to exercise its discretion to find that the ACPA is a "proper person" to make an application under Part XX of the *CBCA*.

93 For the reasons given, the defendants' cross-motion seeking a declaration that ACPA is not a proper person to make an application under Part XX of the *CBCA*, is granted.

94 I may be spoken to as to costs.

P.A. CUMMING J.

8

Case Name:

Target Canada Co. (Re)

RE: IN THE MATTER OF the Companies' Creditors Arrangement Act, R.S.C., 1985, c. C-36, as amended AND IN THE MATTER OF a Plan of Compromise or Arrangement of Target Canada Co., Target Canada Health Co., Target Canada Mobile GP Co., Target Canada Pharmacy (BC) Corp., Target Canada Pharmacy (Ontario) Corp., Target Canada Pharmacy Corp., Target Canada Pharmacy (SK) Corp., and Target Canada Property LLC.

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32 C.B.R. (6th) 48

Court File No.: CV-15-10832-00CL

Ontario Superior Court of Justice

G.B. Morawetz R.S.J.

December 21 and 22, 2015; supplementary written submissions: December 30, 2015; January 6 and 8, 2016.
Judgment: January 15, 2016.

(89 paras.)

Counsel:

Jeremy Dacks, Shawn Irving and *Tracy Sandler* for Target Canada Co., Target Canada Health Co., Target Canada Mobile GP Co., Target Canada Pharmacy (BC) Corp., Target Canada Pharmacy (Ontario) Corp., Target Canada

Pharmacy Corp., Target Canada Pharmacy (SK) Corp., and Target Canada Property LLC (the "Applicants").

Linda Galessiere and *Gus Camelino* for 20 VIC Management Inc. (on behalf of various landlords), Morguard Investments Limited (on behalf of various landlords), Calloway Real Estate Investment Trust (on behalf of Calloway REIT (Hopedale) Inc.), Calloway REIT (Laurentian Inc.), Crombie REIT, Triovest Realty Advisors Inc. (on behalf of various landlords), Brad-Lea Meadows Limited and Blackwood Partners Management Corporation (on behalf of Surrey CC Properties Inc.).

Laura M. Wagner and Mathew P. Gottlieb for KingSett Capital Inc.

Yannick Katirai and *Daniel Hamson* for Eleven Points Logistics Inc.

Daniel Walker for M.E.T.R.O. (Manufacture, Export, Trade, Research Office) Incorporated / Kerson Invested Limited.

Jay A. Schwartz, Robin Schwill for Target Corporation.

Miranda Spence for CREIT.

Jay Carfagnini, Jesse Mighton, Alan Mark and Melaney Wagner for Alvarez & Marsal Canada Inc. in its capacity as Monitor.

James Harnum for Employee Representative Counsel.

Harvey Chaiton for the Directors and Officers of the Applicants.

Stephen M. Raicek and *Mathew Maloley* for Faubourg Boisbriand Shopping Centre Limited and Sun Life Assurance Company of Canada.

Vern W. DaRe for Doral Holdings Limited and 430635 Ontario Inc.

Stuart Brotman for Sobeys Capital Incorporated.

Catherine Francis for Primaris Reit.

Kyla Mahar for Centerbridge Partners and Davidson Kempner.

William V. Sasso, Pharmacist Representative Counsel.

Varoujan C. Arman for Nintendo of Canada Ltd., Universal Studios Canada Inc., Thyssenkrupp Elevator (Canada) Limited, RPI Consulting Group Inc.

Brian Parker for Montez (Cornerbrook) Inc., Admns Meadowlands Investment Corp, and Valiant Rental Inc.

Roger Jaipargas for Glentel Inc., Bell Canada and BCE Nexxia.

Nancy Tourgis for Issi Inc.

ENDORSEMENT

1 G.B. MORAWETZ R.S.J.:-- The Applicants Target Canada Co., Target Canada Health Co., Target Canada Mobile

GP Co., Target Canada Pharmacy (BC) Corp, Target Canada Pharmacy (Ontario) Corp, Target Canada Pharmacy Corp, Target Canada Pharmacy (Sk) Corp, and Target Canada Property LLC ("Target Canada") bring this motion for an order, *inter alia*:

(a) accepting the filing of a Joint Plan Compromise and Arrangement in respect of Target Canada Entities (defined below) dated November 27, 2015 (the "Plan");

(b) authorizing the Target Canada Entities to establish one class of Affected Creditors (as defined in the Plan) for the purpose of considering and voting on the Plan (the "Unsecured Creditors' Class");

(c) authorizing the Target Canada Entities to call, hold and conduct a meeting of the Affected Creditors (the "Creditors' Meeting") to consider and vote on a resolution to approve the Plan, and approving the procedures to be followed with respect to the Creditors' Meeting;

(d) setting the date for the hearing of the Target Canada Entities' motion seeking sanction of the Plan should the Plan be approved by the required majority of Affected Creditors of the Creditors Meeting.

2 On January 13, 2016, the Record was endorsed as follows: "The Plan is not accepted for filing. The Motion is dismissed. Reasons to follow."

3 These are the reasons.

4 The Applicants and Partnerships listed on Schedule "A" to the Initial Order (the "Target Canada Entities") were granted protection from their creditors under the *Companies' Creditors Arrangement Act* ("CCAA") pursuant to the Initial Order dated January 15, 2015 (as Amended and Restated, the "Initial Order"). Alvarez & Marsal Canada Inc. was appointed in the Initial Order to act as the Monitor.[1]

5 The Target Canada Entities, with the support of Target Corporation as Plan Sponsor, have now developed a Plan to present to Affected Creditors.

6 The Target Canada Entities propose that the Creditors' Meeting will be held on February 2, 2016.

7 The requested relief sought by Target Canada is supported by Target Corporation, Employee Representative Counsel, Centerbridge Partners, L.P. and Davidson Kempner, CREIT, Glentel Inc., Bell Canada and BCE Nexxia, M.E.T.R.O. Incorporated, Eleven Points Logistics Inc., Issi Inc. and Sobeys Capital Incorporated.

8 The Monitor also supports the motion.

9 The motion was opposed by KingSett Capital, Morguard Investments Limited, Morguard Investment REIT, Smart REIT, Crombie REIT, Triovest, Faubourg Boisbriand and Sun Life Assurance, Primaris REIT, and Doral Holdings Limited (the "Objecting Landlords").

<u>Background</u>

10 In February 2015, the court approved the Inventory Liquidation Process and the Real Property Portfolio Sale Process ("RPPSP") to enable the Target Canada Entities to maximize the value of their assets for distribution to creditors.

11 By the summer of 2015, the processes were substantially concluded and a claims process was undertaken. The Target Canada Entities began to develop a plan that would distribute the proceeds and complete the orderly wind-down of their business.

12 The Target Canada Entities discussed the development of the Plan with representatives of Target Corporation.

13 The Target Canada Entities negotiated a structure with Target Corporation whereby Target Corporation would subordinate significant intercompany claims for the benefit of remaining creditors and would make other contributions under the Plan.

14 Target Corporation maintained that it would only consider subordinating these intercompany claims and making other contributions as part of a global settlement of all issues relating to the Target Canada Entities including a settlement and release of all Landlord Guarantee Claims where Target Corporation was the Guarantor.

15 The Plan as structured, if approved, sanctioned and implemented will

(i) complete the wind-down of the Target Canada Entities;

(ii) effect a compromise, settlement and payment of all Proven Claims; and

(iii) grant releases of the Target Canada Entities and Target Corporation, among others.

16 The Plan provides that, for the purposes of considering and voting on the plan, the Affected Creditors will constitute a single class (the "Unsecured Creditors' Class").

17 In the majority of CCAA proceedings, motions of this type are procedural in nature and more often than not they proceed without any significant controversy. This proceeding is, however, not the usual proceeding and this motion has attracted significant controversy. The Objecting Landlords have raised concerns about the terms of the Plan.

18 The Objecting Landlords take the position that this motion deals with not only procedural issues but substantive rights. The Objecting Landlords have two major concerns.

Objection # 1 -- Breach of paragraph 19A of the Amended and Restated Order

19 First, in February 2015, an Amended and Restated Order was sought by Target Canada. Paragraph 19A was incorporated into the Amended and Restated Order, which provides that the claims of any landlord against Target Corporation relating to any lease of real property (the "Landlord Guarantee Claims") shall not be determined in this CCAA proceeding and shall not be released or affected in any way in any plan filed by the Applicants.

20 Paragraph 19A provides as follows:

> 19A. THIS COURT ORDERS that, without in any way altering, increasing, creating or eliminating any obligation or duty to mitigate losses or damages, the rights, remedies and claims (collectively, the "Landlord Guarantee Claims") of any landlord against Target US pursuant to any indemnity, guarantee, or surety relating to a lease of real property, including, without limitation, the validity, enforceability or quantum of such Landlord Guarantee Claims: (a) shall be determined by a judge of the Ontario Superior Court of Justice (Commercial List), whether or not the within proceeding under the CCAA continue (without altering the applicable and operative governing law of such indemnity, guarantee or surety) and notwithstanding the provisions of any federal or provincial statutes with respect to procedural matters relating to the Landlord Guarantee Claims; provided that any landlord holding such guarantees, indemnities or

> sureties that has not consented to the foregoing may, within fifteen (15) days of the making of this Order, bring a motion to have the matter of the venue for the determination of its Landlord Guarantee Claim adjudicated by the Court; (b) shall not be determined, directly or indirectly, in the within CCAA proceedings; (c) shall be unaffected by any determination (including any findings of fact, mixed fact and law or conclusions of law) of any rights, remedies and claims of such landlords as against Target Canada Entities, whether made in the within proceedings under the CCAA or in any subsequent proposal or bankruptcy proceedings under the BIA, other than that any recoveries under such proceedings received by such landlords shall constitute a reduction and offset to any Landlord Guarantee Claims; and (d) shall be treated as unaffected and shall not be released or affected in any way in any Plan filed by the Target Canada Entities, or any of them, under the CCAA, or any proposal filed by the Target Canada Entities, or any of them, under the BIA.

21 The evidence of Target Canada in support of the requested change consisted of the Affidavit of Mark Wong, who stated at the time:

> "A component of obtaining the consent of the Landlord Group for approval of the Real Property Portfolio Sales Process ("RPPSP") was the agreement of The Target Canada Entities to seek approval of certain changes to the initial order in the form of an amended and restated initial order...[T]hese proposed changes were the subject of significant negotiation between the Landlord Group and The Target Canada Entities, with the assistance and input of the Monitor and Target Corporation."

22 The Monitor, in its second report dated February 9, 2015, stated:

> (3.4) Counsel to the Landlord Group advised that the Real Property Portfolio Sales Process proceeding on a consensual basis as described below is conditional on the proposed changes to the initial order.
>
> (3.5) The Monitor recommends approval of the amended and restated initial order as it reflects;
>
> (a) revisions negotiated as among The Target Canada Entities, the Landlord Group and Target U.S. (in conjunction with revisions to the Real Property Portfolio Sales Process), with the assistance of the Monitor; and
>
> (b) a fair and reasonable balancing of interests.

23 Thus, Objecting Landlords contend that the agreement resulting in Paragraph 19A of the Amended and Restated Initial Order was not just a condition of the Landlord Group's agreement to the RPPSP -- it was also a condition of the Landlord Group withdrawing both its opposition to the CCAA process and its intention to commence a bankruptcy application to put the Applicants into bankruptcy at the come back hearing.

24 The Objecting Landlords contend that the Applicants now seek to file a plan that releases the Landlord Guarantee Claims. This, in their view, is a clear breach of paragraph 19A, which Target Canada sought and the Monitor supported.

Objection # 2 -- Breach of paragraph 55 of the Claim Procedure Order

25 Second, the Objecting Landlords contend that the Plan violates the Claims Procedure Order and the CCAA. They argue that the Claims Procedure Order was also settled after prolonged negotiations between the Target Canada Entities

and their creditors, including the landlords and that this order sets out a comprehensive claims process for determining all claims, including landlords' claims.

26 The Objecting Landlords contend that Paragraph 55 of the Claims Procedure Order expressly excludes Landlord Guarantee Claims and provides that nothing in the Claims Procedure Order shall prejudice, limit, or otherwise affect any claims, including under any guarantee, against Target Corporation or any predecessor tenant. Paragraph 55 also ends with the *proviso* that "[f]or greater certainty, this Order is subject to and shall not derogate from paragraph 19A of the Initial Order."

27 The Objecting Landlords take the position that, in clear breach of Paragraph 55 and of the Claims Procedure Order generally, the Plan provides for a set formula to determine landlord claims, including claims against Target Corporation under its guarantees. KingSett further contends that the formula not only purports to determine landlords' claims for distribution purposes, it also purports to determine their claims for voting purposes, with no ability to challenge either. KingSett contends that this violates the terms of the Claims Procedure Order that was sought by the Applicants and supported by the Monitor.

28 In summary, the Objecting Landlords take the position that the foregoing issues are crucial threshold issues and are not merely "procedural" questions and as such the court has to determine whether it can accept a plan for filing if that plan in effect permits Target Canada to renege on their agreements with creditors, violate court orders and the CCAA.

29 In my view the issues raised by the Objecting Landlords are significant and they should be determined at this time.

<u>Position of Target Canada</u>

30 Target Canada takes the position that the threshold for the court to authorize Target Canada to hold the creditors meeting is low and that Target Canada meets this threshold.

31 Target Canada submits that the Plan has been the subject of numerous discussions and/or negotiations with Target Corporation (leading to a structure based on Target Corporation serving as Plan Sponsor), the Monitor and a wide variety of stakeholders. Target Canada states that if approved, the Plan will effect a compromise, settlement and payment of all proven claims in the near term in a manner that maximizes and accelerates stakeholder recovery.

32 Target Corporation, as Plan Sponsor and a creditor of Target Canada, has agreed to subordinate approximately $5 billion in intercompany claims to the claims of other Affected Creditors. Based on the Monitor's preliminary analysis, the Plan provides for recoveries for Affected Creditors generally in the range of 75% to 85% of their proven claims.

33 Target Canada contends that recent case law supports the jurisdiction of the CCAA court to provide that third party claims be addressed within the CCAA and leaves it open to a debtor company to address such claims in a plan.

34 The Plan provides that Affected Creditors will vote on the Plan as a single unsecured class. Target Canada submits that this is appropriate on the basis that all Affected Creditors have the required commonality of interest (i.e. an unsecured claim) in relation to the claims against Target Canada and the Plan will compromise and release all of their claims.

35 Target Canada is of the view that fragmentation of these creditors into separate classes would jeopardize the ability to achieve a successful plan.

36 The Plan values the Landlord Restructuring Period Claims of landlords whose leases have been disclaimed by applying a formula ("Landlord Formula Amount") derived from the formula provided under s. 65.2 (3) of the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3 ("BIA" and "BIA Formula"). The Landlord Formula Amount enhances the BIA Formula by permitting recovery of an additional year of rent. Target Corporation intends to contribute

funds necessary to pay this enhancement (the "Landlord Guarantee Top-Up Amounts") Target Canada contends that the use of the BIA Formula to value landlord claims for voting and distribution purposes has been approved in other CCAA proceedings.

37 With respect to the Landlord Formula Amount to calculate the Landlord Restructuring Period Claims, the formula provides for, in effect, Landlord Restructuring Period Claims to be valued at the lesser of either:

(i) rent payable under the lease for the two years following the disclaimer plus 15% of the rent for the remainder of the lease term; or

(ii) four years rent.

38 Target Canada further contends that the court has the jurisdiction to modify the Initial Order on Plan Implementation to permit the Target Canada Entities to address Landlord Guarantee Claims in the Plan and that it is appropriate to do so in these circumstances. This justification is based on the premise that the landscape of the proceedings has been significantly altered since the filing date, particularly in light of the material contributions that Target Corporation prepared to make as Plan Sponsor in order to effect a global resolution of issues. Further, they argue that Landlord Guarantee Creditors are appropriately compensated under the Plan for their Landlord Guarantee Claims by means of the Landlord Guarantee Creditor Top-Up amounts, which will be funded by Target Corporation. As such, Landlord Guarantee Creditors will be paid 100% of their Landlord Restructuring Period Claims, valued in accordance with the Landlord Formula Amount.

39 The Applicants contend that they seek to achieve a fair and equitable balance in the Plan. The Applicants submit that questions as to whether the Plan is in fact balanced, and fair and reasonable towards particular stakeholders, are matters best assessed by Affected Creditors who will exercise their business judgment in voting for or against the Plan. Until Affected Creditors have expressed their views, considerations of fairness are premature and are not matters that are required to be considered by the court in granting the requested Creditors' Meeting. If the Plan is approved by the requisite majority of the Affected Creditors, the court will then be in a position to fully evaluate the fairness and reasonableness of the Plan as a whole, with the benefit of the business judgment of Affected Creditors as reflected in the vote of the Creditors' Meeting.

40 The significant features of the Plan include:

(i) the Plan contemplates that a single class of Affected Creditors will consider and vote on the plan.

(ii) the Plan entitles Affected Creditors holding proven claims that are less than or equal to $25,000 ("Convenience Class Creditors") to be paid in full;

(iii) the Plan provides that all Landlord Restructuring Period Claims will be calculated using the Landlord Formula Amount derived from the BIA Formula;

(iv) As a result of direct funding from Target Corporation of the Landlord Guarantee Creditor Top-Up amounts, Landlord Guarantee Creditors will be paid the full value of their Landlord Restructuring Period Claims;

(v) Intercompany Claims will be valued at the amount set out in the Monitor's Intercompany Claims Report;

(vi) If approved and sanctioned, the Plan will require an amendment to Paragraph 19A of the Initial Order which currently provides that the Landlord Guarantee Claims are to be dealt with outside these CCAA proceedings. The Plan provides that this amendment will be addressed at the sanction hearing once it has been determined whether the Affected Creditors support the Plan.

(vii) In exchange for Target Corporations' economic contributions, Target Corporation and certain other third parties (including Hudson's Bay Company and Zellers, which have indemnities from Target Corporation) will be released, including in relation to all Landlord Guarantee Claims.

41 If the Plan is approved and implemented, Target Corporation will be making economic contributions to the Plan. In particular:

(a) In addition to the subordination of the $3.1 billion intercompany claim that Target Corporation agreed to subordinate at the outset of these CCAA proceedings, on Plan Implementation Date, Target Corporation will cause Property LLP to subordinate almost all of the Property LLP ("Propco") Intercompany Claim which was filed against Propco in an additional amount of approximately $1.4 billion;

(b) In turn, Propco will concurrently subordinate the Propco Intercompany Claim filed against TCC in an amount of approximately $1.9 billion (adjusted by the Monitor to $1.3 billion);

(c) Target Corporation will contribute funds necessary to pay the Landlord Guarantee Creditor Top-Up Amounts.

42 Target Canada points out that in discussions with Target Corporation to establish the structure for the Plan, Target Corporation maintained that it would only consider subordinating these remaining intercompany claims as part of a global settlement of all issues relating to the Target Canada Entities, including all Landlord Guarantee Claims.

43 The issue on this motion is whether the requested Creditors' Meeting should be granted. Section 4 of the CCAA provides:

4. Where a compromise or arrangement is proposed between a debtor company and its unsecured creditors or any class of them, the court may, on the application in a summary way of the company, or any such creditor or of the trustee in bankruptcy or liquidator of the company, order a meeting of the creditors or class of creditors, and, if the court so determines, of shareholders of the company, to be summoned in such manner as the court directs.

44 Counsel cites *Nova Metal Products* for the proposition that the feasibility of a plan is a relevant significant factor to be considered in determining whether to order a meeting of creditors. However, the court should not impose a heavy burden on a debtor company to establish the likelihood of ultimate success at the outset (*Nova Metal Products v. Comiskey (Trustee of)* (1990), 41 O.A.C. 282 (C.A.).

45 Counsel submit that the court should order a meeting of creditors unless there is no hope that the plan will be approved by the creditors or, if approved, the plan would not for some other reason be approved by the court (*ScoZinc Ltd.*, Re, 2009 NSSC 163, 55 C.B.R. (5th) 205).

46 Counsel also submits that the court has described the granting of the Creditors' Meeting as essentially a "procedural step" that does not engage considerations of whether the debtors' plan is fair and reasonable. Thus, counsel contends, unless it is abundantly clear the plan will not be approved by its creditors, the debtor company is entitled to put its plan before those creditors and to allow the creditors to exercise their business judgment in determining whether to support or reject it.

47 Target Canada takes the position that there is no basis for concluding that the Plan has, no hope of success and the court should therefore exercise its discretion to order the Creditors Meeting.

48 Counsel to Target Canada submits that the flexibility of the CCAA allows the Target Canada Entities to apply a uniform formula for valuing Landlord Restructuring Period Claims for voting and distribution purposes, including Landlord Guarantee Claims, in the interests of ensuring expeditious distributions to all Affected Creditors

49 Counsel contends that if each Landlord Restructuring Period Claim had to be individually calculated based on the unique facts applicable to each lease, including future prospects for mitigation and uncertain collateral damage, the resulting disputes would embroil disputes between landlords and the Target Canada Entities in lengthy proceedings. Counsel contends that the issue relating to the Landlord Guarantee Claims is more properly a matter of the overall fairness and reasonableness of the Plan and should be addressed at the sanction hearing.

50 The Plan also contemplates releases for the benefit of Target Corporation and other third parties to recognize the material economic contribution that have resulted in favourable recoveries for Affected Creditors. These releases, Target Canada contends, satisfy the well established test for the CCAA court to approve third party releases. (*ATB Financial v. Metcalfe & Mansfield Alternative Investments II Corp.*, (2008) 42 C.B.R. (5th) 90 (Ont. S.C.J. [Commercial List], affirmed 2008 ONCA 587, (sub nom. Re *Metcalfe & Mansfield Alternative Investments II Corp.*)

51 Likewise, the issue of Third Party Claims and Third Party Releases is a matter that can be addressed at sanction.

52 With respect to the amendment to Paragraph 19A of the Initial Order, counsel submits that since the date of the Initial Order, and since this paragraph was included in the Initial Order, the landscape of the restructuring has shifted considerably, most notably in the form of the economic contributions that are being offered by Target Corporation, as Plan Sponsor.

53 The Target Entities propose that on Plan Implementation, Paragraph 19A of the Initial Order will be deleted. Counsel submits that the court has the jurisdiction to amend the Initial Order through its broad jurisdiction under s. 11 of the CCAA to make any order that it considers appropriate in the circumstances and further, the court would be exercising its discretion to amend its own order, on the basis that it is just and appropriate to do so in these particular circumstances. Counsel submits that the requested amendment is essential to the success of the Plan and to maximize and expedite recoveries for all stakeholders. Further, the notion that a post-filing contract cannot be amended despite subsequent events fails to do justice to the flexible and "real time" nature of a CCAA proceeding.

54 As such, counsel contends that no further information is necessary in order for the landlords to determine whether the Plan is fair and reasonable and they are in a position to vote for or against the Plan.

Position of the Objecting Landlords

55 At the outset of this proceeding, Target Canada, Target Corporation and Target Canada's landlords agreed that Landlord Guarantee Claims would not be affected by any Plan. In exchange, several landlords with Landlord Guarantee Claims agreed to withdraw their opposition to Target Canada proceeding with the liquidation under the CCAA and the RPPSP.

56 Counsel to the landlords submit that 10 months after having received the benefit of the landlords not opposing the RPPSP and the continuation of the CCAA, Target Canada seeks the court's approval to unequivocally renege on the

agreement that violates the Amended Order by filing a Plan that compromises Landlord Guarantee Claims.

57 The Objecting Landlords also contend that the proposed plan violates the Amended Order and the Claims Procedure Order by purporting to the value the landlords' claims, including all Landlord Guarantee Claims, using a formula.

58 Objecting Landlords take the position that they have claims against Target Canada as a result of its disclaimer of long term leases, guaranteed by Target Corporation, in excess of the amount that the Plan values these claim. One example is the claim of KingSett. KingSett insists they have a claim of at least $26 million which has been valued for Plan purposes at $4 million plus taxes.

59 The Objecting Landlords submit that the court cannot and should not allow a plan to be filed that violates the court's orders and agreements made by the Applicant. Further, if the motion is granted, the CCAA will no longer allow for a reliable process pursuant to which creditors can expect to negotiate with an Applicant in good faith. Counsel contends that the amendment of the Initial Order to buttress the agreement between the parties not to compromise the Landlord Guarantee Claims was intended to strengthen, not weaken, the landlords' ability to enforce Target Canada and Target Corporation's contractual obligation not to file a plan that compromises Landlord Guarantee Claims and it would be a perverse outcome for the court to hold otherwise.

60 With respect to claims procedure, the Claims Procedure Order provides in Paragraph 32 that a claim that is subject to a dispute "shall" be referred to a claims officer of the court for adjudication. The Objecting Landlords submit that the Claims Procedure Order reaffirms the agreement between Target Canada, Target Corporation and the Landlord Group with respect to Landlord Guarantee Claims; they refer to Paragraph 55 which specifically provides that nothing in the order shall prejudice, limit, bar, extinguish or otherwise affect any rights or claims, including under any guarantee or indemnity, against Target Corporation or any predecessor tenant.

61 Counsel for the Objecting Landlords submit that the Plan provides the basis for Target Corporation to avoid its obligation to honour guarantees to landlords, which Target Corporation agreed would not be compromised as part of the CCAA proceedings. Counsel contends that the Plan seeks to use the leverage of the "Plan Sponsor" against the creditors to obtain approval to renege on its obligations. This, according to counsel, amounts to an economic decision by Target Corporation in its own financial interest.

62 In support of its proposition that the court cannot accept a plan's call for a meeting where the plan cannot be sanctioned, counsel references *Crystallex International Corp.*, Re, 2013 ONSC 823, 2013 CarswellOnt 3043 [Commercial List]. Counsel submits that the court should not allow the Applicants to file a plan that from the outset cannot be sanctioned because it violates court orders or is otherwise improper.

63 In this case, counsel submits that the Plan cannot be accepted for filing because it violates Paragraph 19A of the Amended Order and Paragraph 55 of the Claims Procedure Order. The Objecting Landlords stated as follows:

> Paragraph 19A of the Amended Order is unequivocal. Landlord Guarantee Claims:
>
> (a) shall not be determined, directly or indirectly, in the CCAA proceeding;
>
> (b) shall be unaffected by any determination of claims of landlords against Target Canada; and,
>
> (c) shall be treated as unaffected and shall not be released or affected in any way in any Plan filed by Target Canada under the CCAA.

Likewise, the Claims Procedure Order, as amended, clearly provides that:

(a) disputed creditors' claims shall be adjudicated by a Claims Officer or the Court;

(b) creditors have until February 12, 2016 to object to intercreditor claims; and,

(c) the claims process shall not affect Landlord Guarantee Claims and shall not derogate from paragraph 19A of the Amended Order.

There is no dispute that the Plan that Target Canada now seeks to file violates these terms of the Amended Order and the Claims Procedure Order...

64 With respect to the issue of Paragraph 19A, counsel submits that this provision benefits Target Canada's creditors who have guarantees from Target Corporation. Further, under the plan, these creditors gain nothing from subordination of Target Corporation's intercompany claim, which only benefits creditors who did not obtain guarantees from Target Corporation. Counsel referred to *Alternative Fuel Systems Inc.*, Re, 2003 ABQB 745, 20 Alta. L.R. (4th) 265, aff'd 2004 ABCA 31, 346 A.R. 28, where both courts emphasized the importance of following a claims procedure and complying with ss. 20(1)(a)(iii) to determine landlord claims.

65 Accordingly, counsel submits that barring landlord consent at the claims process stage of the CCAA proceeding, the court cannot unilaterally impose a cookie cutter formula to determine landlord claims at the plan stage.

Analysis

66 Target Canada submits that the threshold for the court to authorize Target Canada to hold the creditors meeting is low and that Target Canada meets this threshold.

67 In my view, it is not necessary to comment on this submission insofar as this Plan is flawed to the extent that even the low threshold test has not been met.

68 Simply put, I am of the view that this Plan does not have even a reasonable chance of success, as it could not, in this form, be sanctioned.

69 As such, I see no point in directing Target Canada to call and conduct a meeting of creditors to consider this Plan, as proceeding with a meeting in these circumstances would only result in a waste of time and money.

70 Even if the Affected Creditors voted in favour of the Plan in the requisite amounts, the court examines three criteria at the sanction hearing:

(i) Whether there has been strict compliance with all statutory requirements;

(ii) Whether all materials filed and procedures carried out were authorized by the CCAA;

(iii) Whether the Plan is fair and reasonable.

(See *Re Quintette Coal Ltd*. (1992), 13 C.B.R. (3d) 146 (B.C.S.C.); *Re Dairy Corp. of Canada Ltd*., [1934] O.R. 436 (Ont. S.C.); *Olympia & York Developments Ltd. v. Royal Trust Co*. (1993), 17 C.B.R. (3d) 1 (Ont. Gen. Div.); *Re Northland Properties Ltd*. (1988), 73 C.B.R. (N.S.) 175 (B.C.S.C.) at p. 182, aff'd (1989), 73 C.B.R. (N.S.) 195 (B.C.C.A.); *Re BlueStar Battery Systems International Corp*. (2000), 25 C.B.R. (4th) 216 (Ont. S.C.J. [Commercial List]).

71 As explained below, the Plan cannot meet the required criteria.

72 It is incumbent upon the court, in its supervisory role, to ensure that the CCAA process unfolds in a fair and transparent manner. It is in this area that this Plan falls short. In considering whether to order a meeting of creditors to consider this Plan, the relevant question to consider is the following: Should certain landlords, who hold guarantees from Target Corporation, a non-debtor, be required, through the CCAA proceedings of Target Canada, to release Target Corporation from its guarantee in exchange for consideration in the Plan in the form of the Landlord Formula Amount?

73 The CCAA proceedings of Target Canada were commenced a year ago. A broad stay of proceedings was put into effect. Target Canada put forward a proposal to liquidate its assets. The record establishes that from the outset, it was clear that the Objecting Landlords were concerned about whether the CCAA proceedings would be used in a manner that would affect the guarantees they held from Target Corporation.

74 The record also establishes that the Objecting Landlords, together with Target Canada and Target Corporation, reached an understanding which was formalized through the addition of paragraph 19A to the Initial and Restated Order. Paragraph 19A provides that these CCAA proceedings would not be used to compromise the guarantee claims that those landlords have as against Target Corporation.

75 The Objecting Landlords take the position that in the absence of paragraph 19A, they would have considered issuing bankruptcy proceedings as against Target Canada. In a bankruptcy, landlord claims against Target Canada would be fixed by the BIA Formula and presumably, the Objecting Landlords would consider their remedies as against Target Corporation as guarantor. Regardless of whether or not these landlords would have issued bankruptcy proceedings, the fact remains that paragraph 19A was incorporated into the Initial and Restated Order in response to the concerns raised by the Objecting Landlords at the motion of the Target Corporation, and with the support of Target Corporation and the Monitor.

76 Target Canada developed a liquidation plan, in consultation with its creditors and the Monitor, that allowed for the orderly liquidation of its inventory and established the sale process for its real property leases. Target Canada liquidated its assets and developed a plan to distribute the proceeds to its creditors. The proceeds are being made available to all creditors having Proven Claims. The creditors include trade creditors and landlords. In addition, Target Corporation agreed to subordinate its claim. The Plan also establishes a Landlord Formula Amount. If this was all that the Plan set out to do, in all likelihood a meeting of creditors would be ordered.

77 However, this is not all that the plan accomplishes. Target Canada proposes that paragraph 19A be varied so that the Plan can address the guarantee claims that landlords have as against Target Corporation. In other words, Target Canada has proposed a Plan which requires the court to completely ignore the background that led to paragraph 19A and the reliance that parties placed in paragraph 19A.

78 Target Canada contends that it is necessary to formulate the plan in this matter to address a change in the landscape. There may very well have been changes in the economic landscape, but I fail to see how that justifies the departure from the agreed upon course of action as set out in paragraph 19A. Even if the current landscape is not favourable for Target Corporation, this development does not justify this court endorsing a change in direction over the objections the Objecting Landlords.

79 This is not a situation where a debtor is using the CCAA to compromise claims of creditor. Rather, this is an attempt to use the CCAA as a means to secure a release of Target Corporation from its liabilities under the guarantees in

exchange for allowing claims of Objecting Landlords in amounts calculated under the Landlord Formula Amount. The proposal of Target Canada and Target Corporation clearly contravenes the agreement memorialized and enforced in paragraph 19A.

80 Paragraph 19A arose in a post-CCAA filing environment, with each interested party carefully negotiating its position. The fact that the agreement to include paragraph 19A in the Amended and Restated Order was reached in a post-filing environment is significant (see *The Trustees of the Labourers' Pension Fund of Central and Eastern Canada v. Sino-Forest Corporation,* 2015 ONSC 4004, 27 C.B.R. (6th) 134 at paras. 33-35). In my view, there was never any doubt that Target Canada and Target Corporation were aware of the implications of paragraph 19A and by proposing this Plan, Target Canada and Target Corporation seek to override the provisions of paragraph 19A. They ask the court to let them back out of their binding agreement after having received the benefit of performance by the landlords. They ask the court to let them try to compromise the Landlord Guarantee Claims against Target Corporation after promising not to do that very thing in these proceedings. They ask the court to let them eliminate a court order to which they consented without proving that they having any grounds to rescind the order. In my view, it is simply not appropriate to proceed with the Plan that requires such an alteration.

81 The CCAA process is one of building blocks. In this proceedings, a stay has been granted and a plan developed. During these proceedings, this court has made number of orders. It is essential that court orders made during CCAA proceedings be respected. In this case, the Amended Restated Order was an order that was heavily negotiated by sophisticated parties. They knew that they were entering into binding agreements supported by binding orders. Certain parties now wish to restate the terms of the negotiated orders. Such a development would run counter to the building block approach underlying these proceedings since the outset.

82 The parties raised the issue of whether the court has the jurisdiction to vary paragraph 19A. In view of my decision that it is not appropriate to vary the Order, it is not necessary to address the issue of jurisdiction.

83 A similar analysis can also be undertaken with respect to the Claims Procedure Order. The Claims Procedure Order establishes the framework to be followed to quantify claims. The Plan changes the basis by which landlord claims are to be quantified. Instead of following the process set forth in the Claims Procedure Order, which provides for appeal rights to the court or claims officer, the Plan provides for quantification of landlord claims by use of Landlord Formula Amount, proposed by Target Canada.

84 In my view, it is clear that this Plan, in its current form, cannot withstand the scrutiny of the test to sanction a Plan. It is, in my view, not appropriate to change the rules to suit the applicant and the Plan Sponsor, in midstream.

85 It cannot be fair and reasonable to ignore post-filing agreements concerning the CCAA process after they have been relied upon by counter-parties or to rescind consent orders of the court without grounds to do so.

86 Target Canada submits that the foregoing issues can be the subject of debate at the sanction hearing. In my view, this is not an attractive alternative. It merely postpones the inevitable result, namely the conclusion that this Plan contravenes court orders and cannot be considered to be fair and reasonable in its treatment of the Objecting Landlords. In my view, this Plan is improper (see *Crystallex*).

Disposition

87 Accordingly, the Plan is not accepted for filing and this motion is dismissed.

88 The Monitor is directed to review the implications of this Endorsement with the stakeholders within 14 days and is to schedule a case conference where various alternatives can be reviewed.

89 At this time, it is not necessary to address the issue of classification of creditors' claim, nor is it necessary to address the issue of non-disclosure of the RioCan Settlement.

G.B. MORAWETZ R.S.J.

1 Capitalized terms not defined herein have the same meaning as set out in the Plan.

9

Case Name:

Romspen Investment Corp. v. Edgeworth Properties

RE: Romspen Investment Corporation, Applicant, and Edgeworth Properties et al, Respondents

[2014] O.J. No. 3445

2014 ONSC 4340

243 A.C.W.S. (3d) 21

16 C.B.R. (6th) 81

2014 CarswellOnt 9980

Court File No. CV-11-9452-00CL

Ontario Superior Court of Justice

J.A. Thorburn J.

Heard: June 17, 2014.
Judgment: July 18, 2014.

(60 paras.)

Creditors and debtors law -- Receivers -- Court appointed receivers -- Order -- Terms -- Effect on other proceedings -- Motion by Edgeworth Properties Inc ("EPI") to vary receivership order allowed -- EPI was primary holding and operating company of Edgeworth Property Group, which had filed for CCAA protection -- Under receivership order, Romspen, a first priority third party mortgagee and lender to receiver, applied proceeds from sale of receivership property to receiver's charges, first mortgage on property sold and blanker mortgage on all receivership property -- Court did not intend that Romspen's blanket mortgage would be repaid before receiver's other borrowings and such an interpretation of receivership order was not commercially reasonable.

Motion by Edgeworth Properties Inc to vary the receivership order. Edgeworth Properties was the primary holding and operating company of the Edgeworth Group. The Edgeworth Group had applied for CCAA protection. Romspen acquired the first priority position of certain third party mortgages and was the lender in respect of the receiver's borrowings. An offer for the sale of one of the significant receivership properties had been approved by the court. Pursuant to the receivership order proceeds from the sale of receivership properties were to be applied first to the receiver's charges and borrowing charges in respect of the receivership property sold, then to any first mortgage related to the property and finally to its mortgage in respect of all of the receivership properties. Edgeworth Properties sought to

vary the receivership order so that proceeds from the sale of the receivership properties were applied first to the amounts secured by the receiver's charges and borrowing charges on the property sold, second to the amounts secured by any first mortgage on property sold, third to the amounts secured by the receiver's borrowing charges on other receivership properties, fourth to the amounts secured by the mortgage held by Romspen and last to the monitor in the concurrent CCAA proceeding. Edgeworth Properties claimed that this would maximize recovery for all creditors. It claimed that by applying funds to Romspen's mortgage (which bore interest at 13 per cent) before applying them to the receiver's other borrowings (which bore interest at 24 per cent) resulted in fewer funds flowing from the receivership proceeding to the CCAA proceeding.

HELD: Motion allowed. The Court did not intend that Romspen's blanket mortgage would be repaid before the receiver's other borrowings and such an interpretation of the receivership order was not commercially reasonable. The other third party mortgagees did not agree with such an allocation. Romspen's interpretation of the order would put Edgeworth Properties in a worse position. Applying the proceeds to the receiver's other borrowings before the blanket mortgage would result in more funds being available to in the CCAA proceedings to creditors. At the time that the receivership order was granted, no one knew there would be a lengthy delay in selling receivership property. Finally, the objective in approving the CCAA proceedings and appoint a Receiver was to maximize the value of Edgeworth Group's assets and sell the properties. Edgeworth Group did not delay in bringing the matter forward. Romspen would not be prejudiced as it would still recover interest on what was owed to it.

Statutes, Regulations and Rules Cited:

Bankruptcy and Insolvency Act, RSC 1985, c B-3, s. 247, s. 247(a), s. 248, s. 250

Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36,

Rules of Civil Procedure, Rule 59, Rule 59.06

Counsel:

Lisa Corne and M. Brzezinski for the Applicant Romspen, Responding Party on this Motion.

Seema Aggarwal and J. Dietrich, for the Respondent Edgeworth Group, Moving Party on this Motion.

Steven Weisz for the Monitor Grant Thornton Limited.

Craig Mills for the Receiver MNP Ltd.

ENDORSEMENT

J.A. THORBURN J.:--

1. Relief Sought

1 Edgeworth Properties Inc. is the primary holding and operating company of the Edgeworth Group.

2 The Edgeworth Group applied to the court to commence proceedings under the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36. Campbell J. approved the CCAA proceedings and appointed a Receiver.

3 The Edgeworth Group holds the residual interest from the sale of the Receivership properties after satisfaction of

any charges granted under the Receivership Order and the discharge of the security interest of the third party mortgagees.

4 Romspen acquired the first priority position of certain of the third party mortgagees and is the lender in respect of the Receiver's borrowings.

5 To date, Romspen has applied the proceeds from the sale of the Receivership properties as follows,

a) first, to the total amounts secured by the Receiver's charges and borrowing charges in respect of the Receivership property sold;
b) second, to any first mortgage related to such Receivership property (which was acquired by Romspen from the third party mortgagee in question); and
c) third, to Romspen's cross-collateralized mortgage in respect of all of the Receivership properties (the blanket mortgage).

6 Edgeworth Group seeks to vary the Receivership Order so that the proceeds from the sale of the Receivership properties are applied as follows,

a) first to the total amounts secured by the Receiver's charges and the Receiver's borrowing charges in respect of the Receivership property sold;
b) second to the total amounts secured by any first mortgage related to the Receivership property sold;
c) third to the total amounts secured by the Receiver's borrowing charges in respect of the other Receivership properties;
d) fourth to the total amounts secured by the mortgage held by Romspen that is cross-collateralized across all of the Receivership properties (the blanket mortgage); and
e) last to the Monitor in the concurrent CCAA proceeding for application in the concurrent proceeding.

7 In the alternative, Edgeworth seeks an order pursuant to section 248 of the *Bankruptcy and Insolvency Act*, RSC 1985, c B-3, as amended, directing Romspen and the Receiver to apply proceeds and deeming the proceeds to have been applied in the manner set out in paragraph 4 above.

8 Edgeworth claims this would be consistent with the overarching reason for having both a CCAA proceeding and a Receivership, which is to maximize the recovery for all creditors.

9 Edgeworth claims that applying the surplus proceeds available after payment in full to the third party mortgagees, to Romspen's blanket mortgage (which bears interest at 12%) before applying them to the Receiver's other borrowings (which bear interest at 24%) will result in fewer funds flowing from the Receivership proceeding to the CCAA proceeding.

2. <u>The Issue</u>

10 Edgeworth and Romspen do not agree on the order of the payment of proceeds. Romspen's blanket mortgage bears interest at 12% while the Receiver's other borrowings bear interest at 24%.

11 Romspen claims the Receivership Order requires that the blanket mortgage be repaid first. Romspen relies on sections 22 and 25 of the Receivership Order.

12 Edgeworth claims the only commercially reasonable result is for the Receiver's other borrowings to be repaid before the blanket mortgage. Edgeworth claims Romspen's proposed allocation of proceeds creates a result that was not intended by the parties.

13 The key issues to be determined are whether,

a) the Receivership Order finally determined the order of the allocation of proceeds,
b) whether the Receivership Order creates a result that was not intended by the parties, and
c) whether the Receivership Order should be varied to take into account new evidence and /or the fact that it would result in an allocation of proceeds that is not commercially reasonable as required by section 248 of the *Bankruptcy and Insolvency Act*.

3. Background Facts

14 Romspen opposed the initial application for CCAA proceedings and brought a cross motion for foreclosure proceedings based on the Model Receivership Order. The third party mortgagees objected to Romspen's proposal because they did not want the Receiver's borrowings in respect of one property to enhance the third party mortgagee's position with respect to another Receivership property.

15 Prior to the Receivership Order, Romspen was critical of Edgeworth management for being "slow and ineffective in achieving sales of units in the Spruce Ridge condominium project."

16 On November 10, 2011, the Court issued an Order, which was subsequently amended, granting the Companies the protection of a stay of proceedings until December 12, 2011, appointing Grant Thornton Limited as the Companies' Monitor under the CCAA, appointing Eagle Ridge Capital Corporation as the Companies' Chief Restructuring Organization, and appointing MNP Ltd as Receiver of the Companies' 16 properties.

17 Paragraph 22 of the Receivership Order grants to the Receiver certain charges on the Receivership properties to secure the Receiver's fees and disbursements. It provides that, "the Receiver shall be entitled to and are hereby granted a charge on each Debtor's Receivership Property in respect of the Debtor Specific Expenses for such Debtor's Receivership Property and a proportional share of the General Expenses, which share shall be allocable to the Receivership Property according to the proportion which the first-ranking Third Party Mortgagee's individual principal outstanding loan in relation to such Debtor's Receivership Property represents of the principal amount outstanding to the Third Party Mortgagees in the aggregate, as of the date of this Order. Each Debtor Specific Charge shall form a first charge on the Receivership Property to which it relates, in priority to all security interest, trust, liens, charges and encumbrances, statutory or otherwise, in favour of any Person..."

18 Paragraph 25 grants to the Receiver certain charges on the Receivership properties to secure the Receiver's borrowings to fund the Receivership provided the amount does not exceed $1 million for all of the properties except Spruce Drive and $1 million for Spruce Drive. "... each Receivership Property shall be and is hereby charged by way of a fixed and specific charge as security for the payment of the monies borrowed in relation to such Receivership Property together with interest and charges thereon, in priority to all security interests, trust, liens, charges and encumbrances, statutory or otherwise, in favour of any Person but subordinate in priority to the Receiver's Charge and the charges as set out in subsections 14.06(7), 81.4(4) and 81.6(2) of the BIA."

19 In accordance with paragraph 6 of the Receivership Order, the Edgeworth Group holds the residual interest from the sale of the Receivership properties after satisfaction of any charges granted under the Receivership Order and the discharge of the security interests of the third party mortgagees.

20 On April 13 and August 3, 2012, the Court issued orders permitting Romspen and Firm Capital Mortgage Inc. to commence judicial sale or foreclosure proceedings in respect of certain of Edgeworth's properties subject to their respective security.

21 Romspen acquired the first priority position of certain of the third party mortgagees and is the lender in respect of the Receiver's borrowings.

22 The Receiver received two offers for one of the significant properties, the Spruce Ridge property: the first offer was received in late 2011 and rejected by the Receiver, and the second offer was approved by the Court and the closing is pending. In the 12th Report, the Receiver states that, "the Receiver's remediation efforts increased recoveries by approximately $2.3 million over the CPIV [first] Offer." This report was prepared before taking into account the cost of borrowing.

23 The Spruce Ridge Drive condominiums were not sold for approximately two years due to the need for extensive remedial work and further delays occasioned through dealings with the Canadian Mortgage and Housing Corporation.

4. <u>The Effect of the Order</u>

24 Applying the surplus proceeds to the blanket mortgage (with an interest rate of 12% per annum) before applying them to the Receiver's borrowings in the respect of the other Receivership properties (with an interest rate of approximately 24% per annum) results in fewer residual funds flowing from the Receivership proceeding to the CCAA Proceeding and the subordinate creditors.

25 If by contrast, the surplus proceeds are applied to the Receiver's other borrowings before the blanket mortgage, (as Edgeworth suggests) the Monitor estimates that this would result in as much as $875,000 becoming available in the CCAA proceeding to the benefit of the subordinate creditors. Romspen would still recover interest owing in respect of the Receiver's borrowings and the blanket mortgage.

26 The Monitor notes that with the benefit of hindsight, the Edgeworth Group's estate "would have been in a marginally better financial position had the Receiver pursued the [first] CPIV Offer in late 2011...This is the case as the [second] Platinum offer, while resulting in a $2.3 million higher gross realization, required the Receiver to borrow funds from Romspen for a longer period of time, such that the net realization from the [second] Platinum offer is slightly less than the estimated net realization that might have been achieved from the CPIV Offer." The Monitor goes on to say that, "[a]ssuming the 'interest dispute' is decided in favour of the Applicants, the [second] Platinum offer would have likely yielded a marginally better net realization than the [first] CPIV Offer."

5. <u>The Positions of the Parties</u>

27 Edgeworth claims that,

a) at the time the Receivership Order was granted, it was not envisaged or intended that the surplus proceeds would be applied first to the blanket mortgage and then to the Receiver's other borrowings;

b) it took much longer to dispose of the Spruce Ridge properties than the parties envisaged and the Receiver was therefore required to borrow funds from Romspen for a longer period that originally contemplated;

c) Edgeworth did not delay in bringing this motion. The Monitor's counsel corresponded several times with the Receiver's counsel to request an accounting of Romspen's debt and the application of funds. A motion was brought to require Romspen to provide such information. In the Monitor's November 7, 2013 report, the Monitor notes that the information is required to "assess and analyze the appropriateness of the application of funds from the Receivership and Foreclosure Proceedings and assess and analyze the fees and interest charged";

d) if Edgeworth's request is granted, Romspen will still recover interest at the agreed rate; and

e) Section 247 of the *Bankruptcy and Insolvency Act* requires the Receiver to deal with the property of an insolvent person in a commercially reasonable manner and Romspen's proposal is not commercially reasonable.

28 Edgeworth therefore seeks an Order that the surplus proceeds of the Receivership be applied first to the Receiver's other borrowings (for which the interest is 24%) and then to the blanket mortgage (which bears interest at 12%). Edgeworth suggests that this should be done by varying the Receivership Order, by making an Order pursuant to section 248 of the *Bankruptcy and Insolvency Act*, or by invoking the equitable doctrine of unjust enrichment to grant restitution.

29 Romspen takes the position that the Receivership Order is clear. There is no error or omission and there are no new facts that would require reconsideration of the Receivership Order. Romspen claims there are important policy reasons for holding that absent an error or omission, orders should be enforced. Romspen further claims it would be unfair, after the parties came to an agreement, for the court to impose changes to the agreement merely because the risk taken by Romspen turned out to benefit it.

30 Romspen claims that Edgeworth is effectively seeking consolidation of its estates and it claims that consolidation affects the substantive rights of debtors and creditors. This should not be done where it unfairly prejudices one particular creditor. (*Ashley v. Marlow Group Private Portfolio Management Inc.* 2006 CarswellOnt 3449, [2006] O.J. No. 1195 at para 78.)

31 Finally, Romspen claims that Edgeworth's motion should be denied because it has known for 14 months that Romspen has been accruing interest and took no action until it became apparent that there was surplus income and potential for Romspen to benefit at the expense of Edgeworth.

32 The Monitor supports the position taken by Edgeworth.

33 The Receiver takes no position on this motion.

6. The Law

The Importance of Finality

34 Absent exceptional circumstances, orders are final as it is in the interests of the parties and the community that there be definite and discernible ends to legal disputes. (*Tsaoussis (Litigation guardian of) v. Baetz*, [1998] O.J. No. 3516, 41 O.R. (3d) 257 (C.A.), leave to appeal to S.C.C. refused, [1998] S.C.C.A. No. 518.)

35 The court in *Indalex Ltd., Re*, 2013 SCC 6, [2013] 1 S.C.R. 271, at para. 240, held that, "[a] judicially ordered constructive trust, imposed long after the fact, is a remedy that tends to destabilize the certainty which is essential for commercial affairs and which is particularly important in financing a workout for an insolvent corporation."

36 In *Shire International Real Estate Investments Ltd., Re*, 2011 ABQB 654, [2012] A.W.L.D. 163, at paras. 1-3, Kent J. held that, "once some properties had been sold and their portion of DIP financing crystallized, trying to readjust the DIP allocation to make it more fair, would make it even less fair for the remaining unsold properties." As such, he refused to make any reallocation.

The Process by which an Order Can be Amended or Set Aside

37 The *Rules of Civil Procedure*, R.R.O. 1990, Reg. 194, provide a limited set of circumstances where an order can be varied or set aside. Rule 59.06(1) provides that,

> An order that contains an error arising from an accidental slip or omission or requires amendment in any particular on which the court did not adjudicate may be amended on a motion in the proceeding.

Rule 59.06(2) provides that a party who seeks to have an order set aside on the basis of facts arising or discovered after it was made may bring a motion.

Setting Aside an Order on the Basis of New Facts

38 New facts will only justify setting aside an order where the evidence might well have altered the judgment and could not with reasonable diligence have been discovered sooner. (*Hall v. Powers* (2005), 80 O.R. (3d) 462 (S.C.), at para 12.) If that hurdle is cleared, the court will then consider whether there is prejudice to other parties who may have relied on the order.

39 The onus is on the party who seeks to vary the order to establish that another creditor will not be adversely affected. (*Ashley v. Marlow Group Private Portfolio Management Inc*., 2006 CarswellOnt 3449, 270 D.L.R. (4th) 744 (S.C.), at para 78.).

The Receiver's Obligations as Provided for in the *Bankruptcy and Insolvency Act*

40 Section 247 of the *Bankruptcy and Insolvency Act* provides that the Receiver "shall deal with the property of the insolvent person or the bankrupt in a commercially reasonable manner."

41 Section 248 provides that,

> Where the court, on the application of the Superintendent, the insolvent person, the trustee (in the case of a bankrupt), a Receiver or a creditor, is satisfied that the secured creditor, the Receiver or the insolvent person is failing or has failed to carry out any duty imposed by sections 244 to 247, the court may make an order, on such terms as it considers proper,
>
> (a) directing the secured creditor, Receiver or insolvent person, as the case may be, to carry out that duty, or
> (b) restraining the secured creditor or Receiver, as the case may be, from realizing or otherwise dealing with the property of the insolvent person or bankrupt until that duty has been carried out, or both.

42 Section 250 provides that an application may be made under section 248 notwithstanding any order of a court. Where there is any inconsistency between an order made under the Act or a court order, the order made under the Act prevails to the extent of the inconsistency.

7. Analysis and Conclusion

43 The Court appoints Receivers to manage the affairs of a company in a commercially reasonable manner.

44 The Receivership Order provides that charges be granted on a Receivership property by Receivership property basis such that the position of first mortgagees of one Receivership property is not enhanced by the Receiver's borrowing in respect of another Receivership property. This would seem to indicate that the court did not intend that Romspen's blanket mortgage would be repaid before the Receiver's other borrowings.

45 Rule 59 of the *Rules of Civil Procedure* enables a party to vary an order where there is a matter upon which the court did not clearly adjudicate or where there is an error or omission.

46 The following points, taken together, satisfy me that Romspen's interpretation of the allocation of proceeds is not what the parties intended when the Receivership Order was granted and that new facts have arisen since the Receivership Order was issued which make it apparent that Romspen's proposed allocation is not commercially reasonable.

47 Firstly, Romspen's affiant states that,

> [T]he allocation method expressed in the Receivership Order made eminent good sense as each landowning Debtor was a separate, single purpose company with distinct assets, liabilities and stakeholders ... and <u>the notion of levering assets of one estate to benefit stakeholders of a separate estate was understandably unworkable</u> and it is for that reason that the Receivership Order did not provide for a blanket, consolidated borrowing charge against all of the Edgeworth Group's assets. (emphasis added)

48 Secondly, prior to the issuance of the Receivership Order, the third party mortgagees made it clear that they did not agree with the proposed Romspen order because they did not want the Receiver's borrowings in respect of one property to prime another.

49 Thirdly, as noted by the Monitor, if Romspen is entitled to have the monies borrowed at 12% interest paid back before the monies borrowed at a 24% interest rate, the Edgeworth Group's estate, "would have been in a marginally better financial position had the Receiver pursued the [first] CPIV Offer in late 2011 ... This is the case as the [second] Platinum offer, while resulting in a $2.3 million higher gross realization, required the Receiver to borrow funds from Romspen for a longer period of time, such that the net realization from the Platinum offer is slightly less than the estimated net realization that might have been achieved from the [first] CPIV Offer." The Receiver's decision to reject the first offer and accept the second is commercially reasonable only if the proceeds are allocated as proposed by Edgeworth.

50 Fourthly, if the surplus proceeds are applied to the Receiver's other borrowings before the blanket mortgage, (as Edgeworth suggests) the Monitor estimates that this will result in as much as $875,000 becoming available in the CCAA proceeding to the benefit of the subordinate creditors.

51 Fifthly, at the time the Receivership Order was rendered, no one knew there would be a lengthy delay in selling the Spruce Ridge Condominium units. On the contrary, Romspen was critical of Edgeworth management for being, "slow and ineffective in achieving sales of units in the Spruce Ridge condominium project." The fact that it took the Spruce Ridge property two years to sell was not and could not have been anticipated at the time of the Receivership Order.

52 Sixthly, the objective in approving CCAA proceedings and appointing a Receiver is to maximize the value of the company's assets and sell the properties. The allocation of proceeds proposed by Romspen is inconsistent with this objective.

53 These factors are consistent with Edgeworth's interpretation that the Receivership Order was not intended to operate so that the blanket mortgage would be repaid before the Receiver's other borrowings.

54 Moreover, Edgeworth did not delay in bringing this matter forward. Romspen failed to comply with the Monitor's repeated written requests for information, which required a motion to compel Romspen to provide the information. Once the information was obtained, the Monitor and Edgeworth brought the issue to the court's attention without delay.

55 Finally, Romspen will not be prejudiced as it will still recover interest owing in respect of the Receiver's borrowings and the blanket mortgage at the proposed lending rate.

56 I appreciate the general need for certainty and finality in the issuance of court orders. However, in this case, the allocation of proceeds was not finally decided, Romspen's proposed allocation is inconsistent with the evidence available as to the intention of the parties at the time the Receivership Order was issued, and new facts are available regarding the timing of the sale of significant proceeds which was not available at the time the Receivership Order was issued.

57 Therefore, in accordance with Rule 59.06 of the *Rules of Civil Procedure,* the Receivership Order of November 10, 2011 is amended to provide as follows:

The proceeds from the sale of the Receivership properties shall be applied,

(a) first to the total amounts secured by the Receiver's charges and the Receiver's borrowing charges in respect of the property sold;
(b) second to the total amounts secured by any first mortgage related to the Receivership property sold;
(c) third to the total amounts secured by the Receiver's borrowing charges in respect of the other Receivership properties;
(d) fourth to the total amounts secured by the mortgage held by Romspen that is cross-collateralized across all of the Receivership properties; and
(e) last to the Monitor in the concurrent CCAA proceeding for application in the concurrent proceeding.

58 I note that section 247(a) of the *Bankruptcy and Insolvency Act* requires the Receiver to deal with the property of an insolvent person, "in a commercially reasonable manner". Repaying the blanket mortgage at the rate of 12% interest before repaying the other borrowing costs at 24% interest is not commercially reasonable.

59 Section 250 of the *Bankruptcy and Insolvency Act* enables the court to make an order under section 248 notwithstanding that the Receivership Order has been made. In the event I am incorrect that the Receivership Order can and should be amended, an Order shall be granted to apply to proceeds in a commercially reasonable manner as set out in paragraph 57.

60 If the parties are unable to agree on costs, they may provide written submissions of no more than three pages, within fifteen days.

J.A. THORBURN J.

10

Case Name:

Ashley v. Marlow Group Private Portfolio Management Inc.

Between
David Ashley, Alex Chapman, Michael DePencier,
Estate of Clive Bennett Mortimer, Bruce Heyland,
David Williams and Xenolith, plaintiffs, and
Marlow Group Private Portfolio Management Inc.,
Marlow Group Securities Inc., Marlow Group Inc.,
Marlow Private Estate Builders Inc. and
Terrence W. Marlow, defendants

[2006] O.J. No. 1195

270 D.L.R. (4th) 744

22 C.B.R. (5th) 126

151 A.C.W.S. (3d) 763

2006 CarswellOnt 3449

2006 CanLII 31307

Court File No. 05-CL-005797

Ontario Superior Court of Justice
Commercial List

R.E. Mesbur J.

Heard: January 6, 2006.
Judgment: January 17, 2006.

(84 paras.)

Insolvency law -- Legislation -- Bankruptcy and Insolvency Act -- Interpretation -- Motion by the receiver to assign the corporate defendants into bankruptcy and for ancillary relief allowed -- Corporate defendant held to be a securities firm -- Unregistered but allocated securities did not constitute customer name securities exempt from asset pool -- Bankruptcy and Insolvency Act, ss. 253, 258.

Insolvency law -- Claims -- Motion by the receiver to assign the corporate defendants into bankruptcy and for ancillary relief allowed -- Unregistered but allocated securities did not constitute customer name securities exempt from asset pool -- Securities were not the basis of a trust claim under a Part XII bankruptcy, because the securities vested in the trustee and formed part of the customer pool -- Bankruptcy and Insolvency Act, ss. 253, 255, 261.

Motion by the receiver to assign the corporate defendants into bankruptcy and for ancillary relief -- The corporate defendants were comprised of four companies owned and operated by Marlow -- The Marlow Group provided a number of investor services -- The Group went into receivership after Marlow became addicted to crack cocaine and an auditor found a significant shortfall in client trust accounts -- The company owned large blocks of securities that were ostensibly allocated to investors, but were not registered in clients' names -- The Receiver sought a declaration that only the Group's registered securities were considered customer name securities for the purpose of the Bankruptcy and Insolvency Act in order that the unregistered securities could be placed in the customer pool fund and shared proportionally among all customers -- The Receiver also sought consolidation of the corporate defendants as a single securities firm in order to be administered as one estate under Part XII of the Act -- The Receiver submitted that trust claims were not permitted in security firm bankruptcies -- Certain stakeholders and parties filed cross-motions in opposition -- HELD: Motion allowed and cross-motions dismissed -- The Group's investment company was a securities firm for the purpose of Part XII of the Act because it clearly carried on the business of buying and selling securities on behalf of customers -- The mere allocation of securities to customers did not amount to registration and was insufficient to block the inclusion of such securities in the customer pool -- There was no ground to exclude the securities from the customer pool on the basis of a trust claim because under a Part XII bankruptcy, the securities vested in the trustee and formed part of the customer pool -- It was inappropriate to consolidate the companies within the Group substantively because it was unclear whether it would adversely affect the rights of any creditor of any particular company within the Group.

Statutes, Regulations and Rules Cited:

Bankruptcy and Insolvency Act, s. 5(4)(a), s. 14.06, s. 67, s. 183, s. 253, s. 255, s. 258, s. 261, s. 261(1), s. 262(1), s. 262(2.1)

Canadian Charter of Rights and Freedoms, 1982, s. 18

Limited Partnership Act, R.S.O. 1990 c. L.16, s. 4(1)

Limited Partnership Act, Regulations, Reg. 713

Securities Act, R.S.O. 1990 c. S.5, s. 1(1)

Counsel:

Tanya Pagliaroli, for the Plaintiffs (The "Ashley Group").

Derek J. Bell and Raj Sahni, for the Receiver, A. Farber & Partners Inc.

Terrence J. O'Sullivan and M. Paul Michell for John Goudey, Thomas Abel, Shobana Ananth, Shane Anderson, Donald Bayer, Michael Caicco, Charles Cutts, John Coudey, Arnold H. Hochman, Mark Irwin, Gary Levy, Karen Malatest, Hamish McEwan, Pierre Meunier, Paul Oakley, Barry Reiter, Mike Stroud, Michelle Szames, Stephen Szames, James Turner, John Unger, and 2044102 Ontario Inc. (The "Goudey Group").

Arnie Herschom for Paul Benson, Brenda Benson and 145403 Ontario Inc. (the "Benson Group").

O. Pasparakis for Goodman & Company, Investment Counsel Ltd.

M. MacNaughton and B. Wong for Canadian Investor Protection Fund.

Roy Lee for The Superintendent In Bankruptcy.

Jeff Carhart and Arthi Sambasivan for Ron Eden.

R.E. MESBUR J.:--

Nature of the motion:

1 There is very little jurisprudence concerning Part XII of the *Bankruptcy and Insolvency Act.* At Issue on this motion is the correct Interpretation of the term "securities firm" within the meaning of Part XII of Act, whether trust claims can be made to cash or securities under Part XII, and whether the court should consider compelling the re-registration of certain securities on the eve of a bankruptcy.

2 If the defendants or some of them, are found to be securities firms, are assigned into bankruptcy, and if Part XII of the *Bankruptcy and Insolvency Act* applies, then the court must also address whether securities, held for the Goudey Group[1], are "customer name securities" within the meaning of s. 253 of the *Act* or whether they would fall into the "customer pool fund" for distribution among all customers on a *pro rata* basis. It must also decide if certain limited partnership units held for the Benson Group[2] and Mr. Eden should be registered in their names prior to a bankruptcy.

3 In addition to the analysis of these broad issues, the court must also consider receiving the Receiver's Third Report, the Supplement to it, and the Receiver's Fourth Report and approving the Receiver's activities described in them. It must also determine whether to authorize the Receiver to assign the defendants other than Terrence W. Marlow into bankruptcy, and whether, in doing so, the court should procedurally and substantively consolidate their bankrupt estate$ into one bankruptcy estate, so that the assets of all would form one pool against which the creditors of all could claim.

General Factual Background and the Various Stakeholders:

4 The corporate defendants collectively referred to themselves as the "Marlow Group" or the "Marlow Financial Group". The companies making up the group are Marlow Group Private Portfolio Management Inc. (Management Inc."), Marlow Group Securities Inc. ("Securities Inc."), Marlow Group Inc. ("Group Inc.") and Marlow Private Estate Builders Inc. ("Estate Builders Inc."). I am advised that the proper name of Estate Builders Inc. is "Private Estate Builders Inc.". The title of proceedings will be amended to reflect this correction. The defendant Terrence W. Marlow is the sole shareholder, officer and director of each of these corporate entities.

5 Mr. Marlow operated the four companies out of one office, with one telephone number, one fax number, one set of staff, one bank account, and one set of poorly kept books. He referred to them collectively as Marlow Group, and used letterhead styled "Marlow Financial Group".

6 Through the companies, Mr. Marlow provided a number of investor services. Management Inc. is an investment advisor and securities dealer that was registered as an investment counsel, portfolio manager and limited market dealer with the Ontario Securities Commission (the "OSC"). Securities Inc. is a securities dealer and registered investment dealer that was registered With the, Investment Dealers. Association of Canada (the "IDA"). Securities Inc, was also, until it ceased to be a member of the IDA, a member of the Canadian Investor Protection Fund (the "CIPF"). Estate Builders Inc. is a life insurance agency, and Group Inc, is a management company that provided services to the other

three companies.

7 Mr. Marlow was registered with the OSC as a director and advising and trading officer of Management Inc., as well as its chief compliance officer. Mr. Marlow was also registered with the OSC as a trading officer of both Management Inc. and Securities Inc. Unfortunately, Mr. Marlow apparently suffers from an addiction to crack cocaine, for which he is currently receiving rehabilitative treatment.

8 Because it was a registered investment counsel and portfolio manager, Management Inc. was required to file annual audited financial statements with the OSC within 90 days of its fiscal year ended December 31. It failed to do so following its 2003 year end. After that, the OSC imposed some conditions on Management Inc. One of these was to file a satisfactory reconciliation of its client accounts.

9 Management Inc. then hired a chartered accountant, Wally Rudensky, to help meet the OSCs demand. Mr. Rudensky's reconciliation concluded there was a significant deficiency between the actual cash that Management Inc. had in its accounts, and the amount it was supposed to be holding in trust for its clients. Mr. Rudensky concluded there. would be a trust cash shortfall of about $3.3 million. As a result, the OSC immediately suspended Management Inc.'s operations until an audit was complete.

10 Mr. Rudensky worked to complete an audited version of his reconciliation. It disclosed that Management Inc. held a large number of securities for its customers, but very few of these were registered in their clients' names. Management Inc. mostly purchased large blocks of securities, and then allocated them to individual investors, although they did not register them in the clients' names. Some securities were registered in clients' names, but were held in their own personal accounts, unaffiliated with the Marlow Group.

11 The plaintiffs, who are referred to as the "Ashley Group" comprise a group of customers all of whom were essentially in a cash position at this time. They tried to reach an agreement to have Management Inc, return their securities and cash. When that failed, they moved to have the Receiver appointed. Justice Campbell made a Receivership Order on March 9, 2005, appointing A. Farber & Partners Inc. as Receiver over the corporate defendants' assets.

12 This motion began as the Receiver's motion to assign each of the corporate defendants into bankruptcy. Ancillary to that relief, the Receiver suggests that Management Inc. is a "securities firm" as defined in section 253 of the *Act*, and, as a result, the special provisions of Part XII of the *Act* would apply to this bankruptcy. The Receiver seeks a declaration that only those securities that were actually registered, or in the process of being registered, in the name of customers are to be considered as "customer name securities". It also wishes the bankruptcies of the corporate defendants to be consolidated both procedurally and substantively, so that the assets of all would be available to the creditors of all, and the estates would be administered as one estate. In this regard, it asks the court to consider all the corporate defendants as one entity, operating as a securities firm, and subject to Part XII on bankruptcy.

13 In response to the Receiver's motion, other parties and stakeholders responded, and filed cross motions. The Ashley Group supports the Receiver's position completely.

14 The other participants on this motion are other stakeholders. The Goudey Group comprises a group of customers where were in a securities position at the time of the receivership. The Benson Group was similarly situated, as was Mr Eden, The Benson and Eden holdings were in two limited partnerships. Management Inc. holds sufficient securities to meet all its obligations to hold securities for its customers, It is only in the trust cash area that there is a significant shortfall, The Goudey and Benson Groups, along with Mr. Eden, have all brought cross-motions and oppose the Receiver's motion.

15 The Canadian investor Protection Fund (CIPF) is a fund that covers customers of CIPF members that have suffered or may suffer financial loss solely as a result of the insolvency of a member. CIPF is a "customer compensation body" under Part XII of the *Bankruptcy and Insolvency Act*. Of all the companies making up the Marlow Group, only

Securities Inc. was a CIPF member. CIPF has participated on the motion in response to the Receiver's request for a substantive consolidation of the bankruptcies of the corporate defendants.

16 Finally, the Superintendent of Bankruptcy has intervened pursuant to the provisions of section 5(4)(a) of the Act. The guiding principles for the Superintendents Intervention under s. 5(4)(a) are set out in subsection 2 of Section VII of the *Superintendent of Bankruptcy's Programs Effective April 1, 1994*. The guiding principle is stated as:

> The Superintendent may intervene in court under this paragraph where it is a question of national Interest or importance concerning the bankruptcy process or where the Superintendent feels it is in the public interest to do so.

17 The Superintendent intervenes here to make submissions on various questions of law relating to the interpretation of Part XII of the *Bankruptcy and Insolvency Act*. The Superintendent is of the view that the legal issues of what constitutes a securities firm, whether trust claims can be advanced under Part XII of the Act, and whether a creditor should be able to require a re-registration of securities in order to circumvent Part XII are issues of national importance.

Positions of the various stakeholders:

18 In order to understand the motion and cross motions, it Is important to understand the positions of the various stakeholders on the various issues.

The Receiver

19 The Receiver takes the position that the corporate defendants should be assigned into bankruptcy, and that bankruptcy should proceed under the provisions of Part XII of the *Act* because Management Inc. Is a securities firm as that term is defined in the *Bankruptcy and Insolvency Act*, and all the companies acted essentially as one entity. The Receiver also says that Part XII prevails in any conflict between it and any other provisions of the *Act*, For that reason, the Receiver suggests that trust claims are not permitted in security firm bankruptcies.

20 The Receiver says that apart from some shares of Stealth Minerals Ltd. actually registered in individual clients' names, the securities that Management Inc. held for the Goudey Group, the Benson Group, and Mr. Eden are not "customer name securities" as that term is defined in the Act. Thus, they say that these securities should, with the remaining cash, be placed in the customer pool fund, to be shared proportionally among all the customers.

21 The Receiver says that it would be contrary to public policy to permit the Benson Group and Mr. Eden to require that their shares be transferred into their names prior to a bankruptcy, and thus convert them into customer name securities in order to avoid their pooling with those of other customers.

The Superintendent of Bankruptcy

22 The Superintendent of Bankruptcy has intervened on this motion In order to support the Receiver's interpretation of the definition of "securities firm", the Receiver's position that trust claims cannot be made to cash or securities under Part XII, and the Receiver's position that the court should not order the registration of certain securities in the names of certain investors on the eve of bankruptcy. The Superintendent says these legal issues are of national importance and require adjudication.

The Plaintiffs (the Ashley Group)

23 The Ashley Group supports the Receivers position, and that of the Superintendent in Bankruptcy.

The Goudey Group

24 The Goudey Group puts forward a number of arguments. First, it suggests that Management Inc. is not a securities

firm. Second, they say that even if it is, and Part XII applies, their securities are customer name securities, because they can be identified as "theirs". Finally, even if the securities are not customer name securities, the Goudey Group says that they can assert a trust claim to the securities which should be returned to them, and not form part of the customer pool to be shared with other investors.

The Benson Group

25 The Benson Group wants to have Benson's name and address entered on the Register of the CMP 2003 Resource Limited Partnership and the CMP 2004 Resource Limited Partnership ("CMP"). The Benson group has added Goodman & Company, Investment Counsel Ltd. to the motion. Goodman & Company is the Manager appointed by CMP to provide investment, management, administrative and other services in relation to these two limited partnerships. The Benson Group points to these securities being a particular type of tax shelter/limited partnership investment. They say that pursuant to the Limited Partnership Agreement and the provisions of the Prospectus, Goodman & Company is required to list them as the owners of their respective percentage holdings and has failed to do so. They want the court to make an order compelling this registration, prior to the bankruptcy, in order to become customer name securities, and not fall into the customer pool fund.

Mr. Eden

26 Mr. Eden wants to be treated similarly to the Benson Group if they have success, or the: Goudey Group, if they have success. Simply put, Mr. Eden wants securities to be returned to him, however that may be accomplished.

Goodman & Company

27 Goodman & Company takes no position on whether it should re-register the CMP partnership units or not. However, it denies that it has acted improperly in failing to register any CMP units in the names of the Benson Group or Mr. Eden. It says that the actual subscriber for the limited partnership units was Management Inc. and that is who is recorded as the subscriber for CMP 2003 and CMP 2004 on the Partnership Register. Goodman & Company wishes to be exonerated of any wrongdoing or impropriety.

Canadian Investor Protection Fund

28 The Canadian Investor Protection Fund has participated on this motion only to oppose the substantive consolidation of the bankruptcies. A substantive consolidation, it says, could prejudice their position. It also takes the position that there are no compelling reasons to order substantive consolidation.

The Law and analysis:

29 In order to put the issues into context, it is important to consider Part XII of the *Bankruptcy and Insolvency Act*, and its purpose. It is a relatively new part of the Act, having come Into force in 1997, in response to what were seen as undue complexities involved in the bankruptcies of securities firms.

30 Part XII of the *Bankruptcy and Insolvency Act* was enacted to simplify and streamline the administration of a bankrupt securities firm's estate. Before Part XII, administration of these estates was time-consuming, complex, uncertain, and costly to both investors and creditors. Customers of the bankrupt firm would raise trust and tracing concepts, which proved difficult to determine. Often, while waiting for adjudication of these trust claims, the Trustee would have to continue to hold potentially volatile securities, whose value could plummet, while customers battled over their entitlement to them,

31 What Part XII does is to create a particular class of securities that are to be returned to customers. These are called "customer name securities". All other securities and cash held by the bankrupt firm are to be pooled in a "customer pool fund", and distributed among all the customers of the firm on a *pro rata* basis. It is easy to see why some customers

would like to avoid the application of Part XII altogether, or, alternatively, have their securities designated as customer name securities, in order to avoid pooling them with other customers.

32 It should be noted that the customer pool fund is paid out before any creditors are paid at all. If significant securities are returned to customers and do not fall into the pool, the pool will obviously be smaller. Here, if the Receiver's position prevails, the customer pool fund of securities and cash will give all the customers a return of about 60 cents on the dollar. If the Goudey/Benson/Eden positions prevail, they will have securities returned to them, and realize about 95 cents on the dollar for their claims, while the Ashley Group customers will receive less than 5 cents on the dollar.

Bankruptcy?

33 Under the terms of the Receivership Order, the Receiver has the power to assign all the corporate defendants, apart from Securities Inc., into bankruptcy. Securities Inc.'s exclusion from this general power was made part of the Receivership Order at CIPFs request, presumably because of CIPFs particular potential obligations on the bankruptcy of one of Its members. As a result, an order is required to put Securities Inc. into bankruptcy. As far as the other corporate defendants are concerned, the Receiver seeks approval of its decision to assign them into bankruptcy.

34 There is no question that all the corporate defendants are insolvent, and that it would be in the interests of all the customers and creditors for them to be assigned into bankruptcy. No one now opposes an assignment. The only issue is whether the bankruptcy should proceed under Part XII of the Act, or whether it should be a "regular" bankruptcy. Determination of this issue will depend on whether some or all of the corporate defendants are "securities firms", or indeed, whether the Marlow Group should be considered as a single entity which itself is a securities firm.

35 The "securities firm" issue has focused primarily on Management Inc., since it is the company that seems to holding the bulk of the securities, and cash for the customers. As to the other corporate defendants, there is no question that Securities Inc. is a securities firm. It, however, has virtually no assets. Estate Builders Inc. is clearly not Itself a securities firm. This may be relevant on the issue of substantive consolidation, but is essentially moot, since the company apparently has no assets either. Group Inc. simply provided management services to the other companies. It has some assets. This leaves the question of whether Management Inc. is a securities firm. If the bankruptcies are substantively consolidated, and Management Inc. is a securities firm, then presumably a consolidated bankruptcy would proceed under Part XII.

Securities Firm?

36 Section 258 of the *Bankruptcy and Insolvency Act* defines the term "securities firm" as follows:

> "securities firm" means a person who carries on the business of buying and selling securities from, to or for a customer, whether or not as a member of an exchange, as principal or agent, and includes any person required to, be registered to enter into securities transactions with the public, but does not include a corporate entity that is not a corporation within the meaning of section 2.

37 The French version of the statute contains the following definition:

> <<courtier en valeurs mobilières>> Toute personne, membre ou non d'une bourse de valeurs, qui achète des titres a un client ou pour celui-ci ou vend des titres a un client ou pour celui-ci, pour son compte ou en qualité de mandataire, et notamment celle qui a l'obligation de s'inscrire pour avoir le droit de conclure avec le public des opérations sur les titres, a l'exception des personnes qui sont exclues de la définition de "personne morale" a l'article 2.

38 The Goudey Group sets much store in the phrase "carries on the business" in the English definition. It takes the position that in order to qualify for treatment under Part XII, a firm's primary business must be the buying and selling of

securities. It says that Management Inc. held itself out primarily as an advisor. It was registered as an investment counsel, portfolio manager and limited market dealer with the OSC. Since Management Inc. never carried on business as a limited market dealer, the Goudey Group concludes that this necessarily Implies Management Inc. was no more than an investment counsel and portfolio manager, and thus cannot be considered a securities firm. While the Goudey Group concedes that Management Inc. did buy securities on their behalf, they say it was only incidental to their primary business of investment counsellors. Thus, they say Management Inc. cannot be held to be a securities firm.

39 The Superintendent points to the absence of the phrase "carries on the business" in the French version of the *Act*. Section 18 of the *Charter of Rights and Freedoms* provides in section 18 that both the English and French language versions of a Federal statute are equally authoritative. Therefore, the court must examine both to determine Parliament's intention. Each version "forms part of the context in which the other must be read,[3] The court must therefore find a common interpretation for both equally authoritative versions.

40 While the English version includes the term "carries on the business". the French version does not. A literal translation of the phrase *"Toute personne, membre ou non d'une bourse de valeurs, qui achète des titres a un client ou pour celui-ci ou vend des titres a un client ou pour celui-ci",*" from the French version is "Every person, whether or not a member of an exchange, who buys securities from a customer or for him or sells securities to a customer or for him, ...".

41 The French version does not contain any language to suggest that buying and selling securities must be the person's *primary* business. This forms part of the context in which one must read the English version.

42 The Superintendent suggests[4] that "[u]nderstanding the definition of "securities firm" to include a corporation that buys and sells securities for its customers in the course of doing business even if it also engages in other commercial activities is both a reasonable interpretation of the English version and one that Is consistent with the French version". I agree.

43 The Goudey Group says that this approach is equivalent to "reading out" the phrase "carries on the business" in the English version, and thus cannot comply with the "shared meaning rule."[5] I disagree. What the Goudey Group really wants the court to do is to read in the word "primarily" into the English definition. There is no need to do this. When one gives the usual meaning to all the words in both English and French versions, there is no inconsistency between them. Part of the firm's business must be the buying -and selling of securities; it may be its primary business, or it may simply be a part of its overall business. If it is, it is a "securities firm" within the meaning of Part XII, in both English and French. This interpretation is a reasonable interpretation of the English version, and is also consistent with the French version.

44 The Goudey Group goes on to suggest that "securities firm" should be interpreted to be consistent with the securities law definition of a securities dealer. in this regard, it points to section 1(1) of the *Securities Act*[6] and the definition there of the term "dealer" as "a person or company who trades in securities in the capacity of principal or agent." They point out that this definition differs from the definition of an "advisor", namely "a person or company engaging in or holding himself, herself or itself out as engaging in the business of advising others as to the investing in or the buying or selling of securities." They suggest that since Management Inc. was registered as an advisor under Ontario legislation, and the Goudey Group retained Management Inc. to provide them with investment advice, Management Inc. must therefore be an advisor, not a dealer, and hence not a securities firm.

45 It would have been an easy matter for Parliament to define "securities firm" in a parallel fashion to provincial securities, legislation. It did not. It has created a broad definition in Part XII. The definition carries, no ambiguity.

46 Management Inc, clearly bought and sold securities for all of its customers, whether it did so as its primary business. or as ancillary to its primary business of providing investment advice. In this regard, I note that some of the customers signed Private Client Account Agreements with Management Inc. These agreements provided: "Individual

Securities, including stocks and bonds may be purchased from time to time." The Agreements authorized the Marlow Group "to place orders with brokers, investment dealers, banks or trust companies for the purchase and sale of securities."

47 It is important to note that the definition of "securities firm" under the Bankruptcy and insolvency *Act* includes a person "required to be registered to enter into securities transactions with the public". This, no doubt, includes firms the Goudey Group describes as brokerage firms, or stockbrokers, who must, of course be registered as dealers. Such firms are firms defined as "dealers" under Ontario securities law. However, by stating that the definition includes such persons, it must, by implication be taken to mean that the definition is not limited to such persons. Thus, the definition must include persons who need not be registered in this way. This would encompass a firm like Management Inc.

48 As a result, it is clear that Management Inc. "carried on the business of buying and selling securities from, to or for a customer, whether or not as a member of an exchange, as principal or agent, and includes any person required to be registered to enter into securities transactions with the public". I thus conclude they are a securities firm, and therefore Part XII will apply to their bankruptcy.

Customer Name Securities?

49 Part XII carves out a very limited class of securities that are to be returned to customers when a securities firm goes bankrupt. These are defined as "customer name securities" in section 253 in the following way:

> "customer name securities" means securities that on the date of bankruptcy of a securities firm are held by or on behalf of the securities firm for the account of a customer and are registered in the name of the customer or are in the process of being so, registered.

50 The Goudey Group points to the fact that the term "registered" is nowhere defined in Part XII. They suggest that as a result, it is enough for the securities to be identifiable as belonging to a customer, in order to be a customer name security. They reason that since Management Inc. made allocations of various securities among its customers, those securities can be Identified as belonging to the customers. They say that Mr. Rudensky's Account Balance Reconciliation confirms that all of the customer assets held by the Marlow Group have been identified, and the respective owners of those assets have confirmed their ownership, They conclude their argument by stating that this ability to identify the respective owners is equivalent to registration, as contemplated by section 253. To bolster this position, they rely on the re-wording of the section proposed in Bill C-55[7]. There, the definition of customer name securities reads as follows:

> "customer name securities" means securities that on the date of bankruptcy of a securities firm are held by or on behalf of the securities firm for the account of a customer and are registered <u>or recorded in the appropriate manner</u> in the name of the customer or are in the process of being so registered <u>or recorded</u>. but does not include securities registered <u>or recorded in the appropriate manner</u> in the name of the customer that, by endorsement or otherwise, <u>are</u> negotiable <u>by the securities firm.</u> [underlining in the original]

51 The Goudey Group suggests that this new definition clearly supports their view that it is enough simply to be able to identify the beneficial owner of a security, since this would constitute "recording in the appropriate manner" In the records of the securities firm, As a result, they say that their securities are customer name securities and must be returned to them. I disagree with this analysis.

52 In my view, the addition of the words "or recorded in the appropriate manner" in the amendments in Bill C-55 are designed to cover situations where there is no actual registration of securities, but there is another specified method of recording ownership. This, for example, would cover limited partnerships for whom the Limited Partnership *Act* requires that general partner to maintain a record of the limited partners. This would be a name "recorded in the appropriate manner."

53 Here, there is no evidence that any particular securities were recorded in any fashion in the names of the Goudey Group. Bill C-55 offers no assistance, The Ashley Group's securities are not customer name securities. They will form part of the customer pool fund, unless they can be excluded on the basis of a trust claim,

Trust Claims allowed under Part XII?

54 The provisions of Part XII of the *Act* are paramount if there is a conflict with other parts of the Act. Section 255 of Part XII says:

> All the provisions of this Act, in so far as they are applicable, apply in respect of bankruptcies under this Part, but if a conflict arises between the application of the provisions of this Part and the other provisions of this Art, the provisions of this Part prevail.

55 In regular bankruptcies, section 67 of the *Act* applies. It clearly states that assets held In trust by the bankrupt do not form part of the bankrupt estate. In securities firm bankruptcies, Part XII creates a kind of "super-priority" for customers, Section 261(1) vests in the trustee any securities held by the firm itself, as well as any securities and cash held by or for the account of the securities firm for a customer. The trustee is then directed to use these securities and cash to create what is called the "customer pool fund". All other assets form what is called the "general fund".

56 By virtue of s. 262(1), the customer pool fund is allocated first to the costs of administration, if there are insufficient funds in the general fund to pay the costs, and then to distribute the balance to all the firm's customers (except deferred customers) on a *pro rata* basis. Any funds remaining after that distribution are paid into the general fund, which is disbursed according to s. 262(2.1).

57 What does the concept of the customer pool fund do to the notion of trust claims in a Part XII bankruptcy? To date, there is only one reported case in Canada dealing with this issue.[8]

58 In *Vantage*, Brenner J. considered a Trustee's position that any trust claim to either cash or securities held by a securities firm at the date of bankruptcy vests in the Trustee. Justice Brenner held that the plain wording of the language of the section supported that view. In coming to this conclusion he considered both the plain language of the section, as well as the underlying policy of Part XII.

59 In order to discern the policy, Justice Brenner relied on an article by B.D. Turcotte, entitled "Securities Firm Bankruptcies"[9]. That article outlined the historical complexities of securities firm bankruptcies prior to Part XII, particularly the difficulties of sorting out ownership of, or claims to securities that securities firms generally hold in many different ways for their customers. Justice Brenner concluded:

> By passing Part XII, Parliament decided to try to simplify securities firm bankruptcies by doing away with the myriad of competing trust claims and the associated legal costs and time delays In securities firm bankruptcies. Parliament recognized that securities firms deal in principally two assets: cash and securities, and so for those two asset classes, Parliament enacted the new rules In Part XII. Under s. 261, Parliament removed the entire concept of trust law for securities (except where those securities are "customer named securities) and cash.

60 In the context of the *Vantage* case, Justice Brenner was dealing with the issue of cash. He concluded that by virtue of s. 261, all cash held by a securities firm at the date of bankruptcy vested in the trustee, not just the cash owned beneficially by the securities firm. Section 261 is equally applicable to securities, and I thus agree with Brenner J.'s analysis, and find that all securities held by a securities firm at the date of bankruptcy vest it the trustee, not just the securities owned beneficially by the firm. The only exclusion from the pool is those securities that fall into the definition of "customer name securities". Surely the plain reading of the section suggests that cash and securities "held ... for a customer" must mean cash and securities held in trust or for the benefit of a customer. If cash and securities held In trust for a customer are to vest in the trustee in a securities firm bankruptcy, then clearly this provision is in conflict

with the general provisions of section 67 that exclude trust assets from the estate. Since there is a conflict, Part XII prevails, and trust claims must be prohibited.

61 Since I have held that Management Inc. is a securities firm, the Goudey Group's securities are not customer name securities, and have also found that they cannot assert a trust claim to them, their securities must vest in the trustee, and form part of the customer pool. This addresses the Goudey Group motion. I turn now to the arguments advanced by the Benson Group and Mr. Eden.

Require registration of the Benson Group and Eden securities?

62 The Benson Group and Mr. Eden were also Management Inc. customers. They invested in two limited partnerships, CMP 2003 Resource Limited Partnership and CMP 2004 Resource Limited Partnership ("CMP"), as well as earlier CMP limited Partnerships for prior years. The CMP limited partnership units are not registered in the Benson Group or Mr. Eden's names. They say their units should be registered in their names, and ask the court to require Goodman & Company to effect this registration, before any bankruptcy occurs. This, of course, would make their CMP units customer name securities that would be returned to them, since they would be registered in their names prior to bankruptcy.

63 Simply put, the Benson Group and Mr. Eden say that both the Limited Partnership Agreement and the *Limited Partnership Act*[10] require that the names and addresses of all limited partners of the Limited Partnership must be registered in the records of the limited partnership. They also say that Prospectuses for these two limited partnerships state that shares will be registered in the name of a partner, if the partner requests it. They say they have a right to demand registration, and they are doing so now. They go further, and say that Goodman & Company has acted improperly in failing to maintain their names as owners In the records, and further, has made a misrepresentation in the prospectus, namely that it would keep a record of the limited partners.

64 The Benson Group and Mr. Eden say that in the years before 2003, their investments in the CMP limited partnerships for the prior years were registered in their names. They also received their expected tax benefits from the investments, received tax receipts, and were acknowledged by the Limited Partnerships to be limited partners.

65 In the years since, they also received their expected tax receipts for CMP 2003 and 2004. They say that the Receiver says Marlow's records show Marlow was holding 4500 CMP units on behalf of its customers. They point to these facts to support their view that they must therefore be limited partners of the 2003 and 2004 CMP limited partnerships, and thus are entitled to registration of their interests. This will make the investments customer name securities.

66 Goodman & Company points out that as far as CMP and its records are concerned, in prior years, the Benson Group and Eden subscribed for the partnership units in their own names. They were recorded as limited partners for these investments. However, it was Management Inc. that subscribed for units in CMP 2003 and 2004. In compliance with its obligations under the *Limited Partnership Act*, and the Limited Partnership Agreement, CMP kept registers for unit subscribers for CMP 2003 and 2004. These register show Management Inc. as the subscriber for these units.

67 As it did for many other securities, Management Inc. purchased blocks of CMP as subscriber, and was thus registered as the holder in its own name. It later allocated them to clients. In my view, this puts the CMP units in exactly the same position as the other securities, which I have found, are not customer name securities. Although the Benson Group and Eden do not assert a trust claim to the CMP units, it is clear to me, on the basis of who subscribed for the units, that Management Inc. was the registered holder, and held the units in trust for the Benson Group and Eden. I see no basis upon which they can require the register to be altered, since they were not the subscribers for these units. I deny their request on this basis. As a result, I need not address whether there are also public policy grounds upon which to deny it as well.

68 This leaves the last issue; that is whether there should be both a procedural and substantive consolidation of the bankruptcies of the corporate defendants, essentially treating them as one bankruptcy of one securities firm.

Procedural and Substantive Consolidation?

69 All the stakeholders support procedural consolidation of the bankruptcy of all the corporate defendants. No one opposes a substantive consolidation apart from the CIPF. In order to assess its position, it is important to consider what the effect of a substantive consolidation would be.

70 Essentially, a substantive consolidation would treat all of the corporate defendants as one entity. The assets of each would fall into one common pool, to be shared by all their creditors on a *pari passu* basis.

71 There is no specific authority in the *Bankruptcy and Insolvency Act* to grant an order for substantive consolidation. It is common ground, however, that the court has the authority to do so under its equitable jurisdiction under section 183 of the Act.

72 Few Canadian cases have dealt with substantive consolidation, although the American courts have written extensively on the subject, setting out various, and disparate, tests to support an order for substantive consolidation. We have no such assistance here.

73 The Receiver seeks a substantive consolidation for a number of reasons. Just as it said the "Marlow Group" as a whole should be treated as a securities firm, so it says, the four corporate defendants should be treated as one legal entity for the purposes of bankruptcy. They say it is appropriate to consolidate bankrupt estates in order to avoid multiplicity of proceedings, and where the bankrupt companies have shared or pooled resources, assets, and bank accounts. Also, they say where related companies are organized in an intertwined manner, It will be reasonable that the estates be dealt with *en bloc* to realize the greatest value for all interested parties.[11]

74 The Receiver goes on to say that all four companies operated as an interrelated entity, with shared premises, telephone, fax, bank accounts and accounting records. The Receiver says that they were operated as a single, consolidated enterprise, and should be treated as such for bankruptcy purposes, because to do so would be most expedient and cost-effective.

75 What emerges from the few Canadian cases, however, is that although expediency is an appropriate consideration In deciding whether to grant consolidation, it should not be done at the expense or possible prejudice of any particular creditor.[12] I take this to include any possible prejudice to someone like the CIPF, which as a customer compensation body under the *Act* has some concerns about possible additional exposure to claims if there Is substantive consolidation, and all creditors, and perhaps customers, then have potential claims against Securities Inc., and thus against the Fund. While there is no evidence of this actually occurring, it is a concern.

76 CIPF also points out that the Receiver wishes to use the only assets of Securities Inc., some cash, to fund the bankruptcy, and thus there is no practical advantage to any of Securities Inc.'s creditors to having a substantive consolidation of all the estates.

77 CIPF says that substantive consolidation profoundly affects the substantive rights of debtors and creditors, and thus should be considered an extreme remedy and carefully scrutinized. It involves more than procedural convenience, which of course can be accomplished by the procedural consolidation that everyone supports.

78 The Receiver has not provided evidence concerning the effect on all the creditors of all the corporate defendants if there is a substantive consolidation, and whether this will adversely affect the eights of any creditor of any individual company. Without that evidence, I cannot determine whether a consolidation would occur at the expense or to the prejudice of any particular creditor. I echo the concerns of Chadwick 3 in Re J.P. Capital Corp.[13] where he stated:

> I am concerned with consolidating the actions which will provide for pari passu distribution without knowing the effect that such an order will have on all creditors. Although expediency is an appropriate consideration it should not be done at the possible prejudice or expense of any particular creditor."

79 I am also concerned about whether there can be a substantive consolidation where Part XII clearly applies to two of the bankrupt companies (Management Inc. and Securities Inc.), but not to Estate Builders Inc. It is a life insurance agency - there is no suggestion that It is also a securities firm. Because of this, I am not persuaded, on the record I have, that all four companies should be treated as a single securities firm for the purposes of Part XII. This has an impact on the claim for consolidation. Although Estate Builders Inc. may not have any assets, or indeed any creditors, substantive consolidation may have the unintended effect of attempting to deal with Estate Builder's bankruptcy under Part XII. Counsel for the receiver was not able to provide me with sufficient evidence to, address either of my concerns.

80 For these reasons, the motion for substantive consolidation is dismissed, without prejudice to its being renewed on further and better material. The motion for procedural consolidation of all the corporate bankrupt estates is granted.

Receiver's Third and Fourth Reports

81 There is no objection to the receipt of the Receiver's Third Report, the Supplement to it, and the Receiver's Fourth Report. There is no objection to approving the actions taken by the receiver to date. Accordingly, an order will go as requested in that regard.

82 The receiver raised an issue concerning paragraph 28 of the Receivership Order. It is of particular relevance now, given my disposition of the motion for substantive consolidation. That paragraph relates to the Receiver's use of the assets of Securities Inc. The only asset Securities Inc. has is cash of about $120,000. The Receiver needs access to this money in order to fund its fees as the Trustee on the bankruptcies. Without substantive consolidation, this may create some difficulty. No one opposes these funds being used by the Trustee to administer all the estates. An order will therefore go deleting paragraph 28 of the Receivership Order so that the receiver can access all the money in Securities Inc. to cover trustee's fees on the procedurally consolidated bankruptcy of the corporate defendants.

Disposition:

83 For all these reasons, an order will go as follows:

(a) Receiving the Third Report of the Receiver dated August 15, 2005, the Supplement to the Third report of the Receiver dated August 17, 2005, and the Fourth Report of the Receiver dated September 30, 2005, and approving the activities of the Receiver set out in them;

(b) Authorizing and directing the Receiver to assign all of the corporate defendants Into bankruptcy, and that A. Farber & Partners Inc. shall be the trustee in bankruptcy ("Trustee");

(c) The bankruptcy estates of the corporate defendants shall be procedurally consolidated and administered together;

(d) Dismissing the Receiver's motion for substantive consolidation, without prejudice to its being renewed on further and better material;

(e) The bankruptcies of Management Inc. and Securities Inc. will proceed under Part XII of the *Bankruptcy and Insolvency Act*,

(f) The Goudey Group's motion to have certain securities declared to be customer name securities, or alternatively for a trust to be imposed on them and their being returned is dismissed;

(g) The Benson Group's and Eden's motion for the re-registration of CMP 2003 and 2004 Limited Partnership units Into their names is dismissed;

(h) Declaring the 3,346,667 shares in the capital of Stealth Minerals Limited described in paragraph 7 of the Third Report are the only "customer name securities" held by Management Inc. and

Securities Inc., and that the remainder of the securities they hold are not customer name securities and shall be grouped into either the "customer pool fund" or the "general fund" as appropriate in accordance with Part XII of the *Bankruptcy and Insolvency Act*,

(i) Deleting paragraph 28 of the Receivership Order of Campbell J. dated March 9, 2005;

(j) That the Trustee shall be authorized to sell sufficient securities and any other property from the bankruptcy estates in order to realize up to $250,000 of net proceeds to fund the costs of the bankruptcy, including without limitation the fees and costs of the Trustee and its counsel, and that the Trustee may apply to the Court at any time and from time to time to sell any further securities or other property from the bankruptcy estate as it may deem necessary to fund the ongoing costs of the bankruptcy;

(k) That after the assigning the corporate defendants into bankruptcy, the Receiver is authorized and directed to bring a motion before this Court to terminate the Receivership in respect of the corporate defendants and to seek approval of its final statement of receipts and disbursements as Receiver, including approval of its fees and costs and fees and costs of its counsel and the costs payable from the estate pursuant to the Order of this Court made on March 9, 2005 to counsel for the Plaintiffs and to seek a discharge of the Receiver in respect of the corporate defendants;

(l) That the Receiver and the Trustee, upon its appointment, shall incur no liability or obligation as a result of the carrying out the provisions of this Order, except for any gross negligence or wilful misconduct on its part. Nothing in this Order shall derogate from the protections afforded the Receiver by the Order dated March 9, 2005, or by section 14.06 of the *Bankruptcy and Insolvency Act*, or any other applicable legislation.

(m) Amending the title of proceedings to change the name "Marlow Private Estate Builders Inc." to "Private Estate Builders Inc.".

84 If the parties are unable to agree on the disposition of costs of the motion and cross motions, they may make brief written submissions to me. The Receiver's are to be delivered Within 15 days of the release of these reasons, with all other parties delivering their responses within 15 days following.

R.E. MESBUR J.

1 John Goudey, Thomas Abel, Shobana Ananth, Shane Anderson, Donald Bayer, Michael Caicco, Charles Cutts, John Coudey, Arnold H. Hochman, Mark Irwin, Gary Levy, Karen Malatest, Hamish McEwan, Pierre Meunier, Paul Oakley, Barry Reiter, Mike Stroud, Michelle Szames, Stephen Szames, James Turner, John Unger, and 2044102 Ontario Inc.

2 Paul Benson, Brenda Benson and 145403 Ontario Inc.

3 *Re Estabrooks Pontiac Buick* (1982) 44 N.B.R. (2d) 201, (C.A) at paragraph 19, and *Aeric Inc. v. Canada Post Corp* (1985), 16 D.L.R. (4th) 686 (F.C.A.) at p. 707

4 Superintendent's factum, paragraph 12.

5 see Ruth Sullivan, *Sullivan and Driedger on the Construction of Statutes*, 4th ed. (Markham, Ont.: Butterworths, 2002) at 80.

6 see R.S.O. 1990 c. S.5.

7 *An Act to establish the Wage Earner Protection Program Act, to amend the Bankruptcy and Insolvency Act and the Companies' Creditors Arrangement Act and to make consequential amendments to other Acts*

8 Re *Vantage Securities* (1998), 9 C.B.R. (4th) 169

9 (1997) 17:3 *Insolvency Bulletin* 75.

10 See s. 4(1) of the *Limited Partnership Act*, R.S.O. 1990 c. L.16, and s. 3a of Regulation 713 made under the *Limited Partnership Act*

11 Re J.P. Capital Corp., (1995), 31 C.B.R. (3d) 102 (Ont. Gen. Div.), and Re Associated Freezers of Canada Inc. [1995] O.J. No. 2862 (Ont. Gen. Div. In Bankruptcy)

12 Re Associated Freezers, above, at paragraph 5

13 Note 10, above, at paragraph 19

IN THE MATTER OF THE *COMPANIES' CREDITORS ARRANGEMENT ACT*, R.S.C. 1985, C. C-36, AS AMENDED

Court File No. CV-16-11257-00CL

AND IN THE MATTER OF A PLAN OF COMPROMISE OR ARRANGEMENT OF PRIMUS TELECOMMUNICATIONS CANADA INC., PRIMUS TELECOMMUNICATIONS, INC. AND LINGO, INC.

ONTARIO
SUPERIOR COURT OF JUSTICE
COMMERCIAL LIST

Proceeding commenced at Toronto

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