Clerk's stamp:

COURT FILE NUMBER	1601 - 12571
COURT	COURT OF QUEEN'S BENCH OF ALBERTA
JUDICIAL CENTRE	CALGARY
	IN THE MATTER OF THE *COMPANIES' CREDITORS ARRANGEMENT ACT*, RSC 1985, c C-36, as amended AND IN THE MATTER OF A PLAN OF COMPROMISE OR ARRANGEMENT OF LIGHTSTREAM RESOURCES LTD, 1863359 ALBERTA LTD, LTS RESOURCES PARTNERSHIP, 1863360 ALBERTA LTD AND BAKKEN RESOURCES PARTNERSHIP
APPLICANTS	LIGHTSTREAM RESOURCES LTD, 1863359 ALBERTA LTD AND 1863360 ALBERTA LTD
PARTIES IN INTEREST	LTS RESOURCES PARTNERSHIP AND BAKKEN RESOURCES PARTNERSHIP
DOCUMENT	**BENCH BRIEF OF THE APPLICANTS**
ADDRESS FOR SERVICE AND CONTACT INFORMATION OF PARTY FILING THIS DOCUMENT	**BLAKE, CASSELS & GRAYDON LLP** Barristers and Solicitors 3500 Bankers Hall East 855 – 2nd Street SW Calgary, Alberta T2P 4J8 Attention: Kelly Bourassa Telephone No.: 403-260-9697 Email: **kelly.bourassa@blakes.com** Fax No.: 403-260-9700 File: 89691/8

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I. INTRODUCTION

1. Lightstream Resources Ltd. ("**LTS**"), 1863359 Alberta Ltd ("**1863359**") and 1863360 Alberta Ltd. ("**1863360**" and together with LTS and 1863359, the "**Applicants**") seek relief under the *Companies' Creditors Arrangement Act*, RSC 1985, c C-36, as amended (the "**CCAA**"). LTS is the parent company to 1863359, 1863360, LTS Resources Partnership ("**LTS Partnership**") and Bakken Resources Partnership (the "**Bakken Partnership**" and together with LTS Partnership, the "**Partnerships**"). The Applicants and the Partnerships are collectively referred to herein as the "**Lightstream Group**".

2. Although the Partnerships are not Applicants in these proceedings, the Applicants seek to have the stay of proceedings and other protections of the proposed form of initial order under the CCAA (the "**Initial Order**") extend to the Partnerships as they are integrally and closely interrelated to and intertwined with the Applicants.[1]

3. The Lightstream Group has been significantly affected by the sustained decline in global commodity prices and the Canadian dollar since mid-2014.[2] In the early spring of 2016, the Lightstream Group and its advisors began to engage in discussions with certain of the Lightstream Group's main creditors with respect to exploring various strategic alternatives, including alternative first lien financing, the sale of certain assets and negotiated restructuring and/or recapitalization alternatives.[3]

4. Prior to the Lightstream Group commencing these proceedings, LTS (along with a newly incorporated subsidiary 9817158 Canada Ltd. ("**ArrangeCo**")) had commenced proceedings under section 192 of the *Canada Business Corporations Act*, RSC 1985, c C-44, as amended (the "**CBCA**"), in the Court of Queen's Bench of Alberta (the "**Court**"), Action Number 1601–08725 (the "**Arrangement Proceedings**") in relation to a proposed plan of arrangement under the provisions of section 192 of the CBCA (the "**Arrangement**") involving: (i) LTS and ArrangeCo; (ii) holders of 9.875% secured second lien notes maturing on June 15, 2019 (the "**Secured Notes**" and the holders, the "**Secured Noteholders**"); (iii) holders of 8.625% unsecured notes maturing on February 1, 2020 (the "**Unsecured Notes**",

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[1] Affidavit of Peter D. Scott sworn September 21, 2016 at para 100 (the "**Scott Affidavit**").

[2] Scott Affidavit, Exhibit 2 at para 12.

[3] Scott Affidavit, Exhibit 2 at paras 124 - 132.

and the holders, the "**Unsecured Noteholders**"); and (iv) holders of common shares of LTS (the "**Common Shares**", and the holders, "**Shareholders**").[4]

5. As a result of the inability of the Lightstream Group to reach a settlement of outstanding litigation (the "**Unsecured Noteholder Litigation**") with certain holders of the Unsecured Notes by September 16, 2016, pursuant to an amended and restated noteholder support agreement dated as of July 12, 2016 (as amended, the "**Support Agreement**") with members of an *ad hoc* committee of Secured Noteholders (the "***Ad Hoc* Committee of Secured Noteholders**") representing approximately 91.5 percent of the total outstanding principal amount of Secured Notes, the Lightstream Group is required to take all necessary steps to seek the proposed Initial Order and commence these CCAA proceedings for the purpose of implementing a sale of all or substantially all of the Lightstream Group's assets or business.[5]

6. The immediate objective of the proposed CCAA proceedings is to continue a sale and investor solicitation process (the "**SISP**") that commenced on July 13, 2016 in connection with the Arrangement Proceedings, through these CCAA restructuring proceedings by way of proposed sale procedures (the "**Sale Procedures**") attached as Appendix "A" to the proposed Initial Order, to effect a transaction for all of the Lightstream Group's assets.[6]

7. The purpose of this Bench Brief is to outline for the Court the legislation and jurisprudence that is relevant to the relief being sought in the Applicants' originating application filed September 22, 2016, and to demonstrate the necessity of and justification for certain priority charges in favour of the Applicants' lenders, key stakeholders and advisors, among others, which are critical to ensure the Applicants' successful restructuring.

II. FACTS

8. A summary of the facts relevant to this Application are set out below. For a more complete discussion of the facts and circumstances pertaining to the Lightstream Group, please refer to the Scott Affidavit.

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[4] Scott Affidavit at para 4.

[5] Scott Affidavit at para 67.

[6] Scott Affidavit at para 103.

A. Overview of the Lightstream Group

9. Each of the Applicants is a corporation formed pursuant to the *Business Corporations Act*, RSA 2000, c B-9 (the "**ABCA**") and LTS is the parent of the Lightstream Group.[7] The Partnerships are general partnerships formed and registered as general partnerships pursuant to the laws of Alberta and are direct and indirect wholly-owned subsidiaries of LTS.[8]

10. The Lightstream Group is engaged in the exploration, development and production of oil and natural gas reserves in the provinces of Alberta, British Columbia and Saskatchewan, with a focus on light oil.[9]

11. The Lightstream Group's business consists of three business units: (i) the "**Bakken Business Unit**", which is comprised of the Bakken Partnership assets located in southeastern Saskatchewan in the Bakken and Mississippian formations; (ii) the "**Cardium Business Unit**", which is comprised of certain of the LTS Partnership assets in central Alberta, with the majority of the assets in the Cardium formation; and (iii) the "**Alberta/BC Business Unit**" which is comprised of the balance of the LTS Partnership Assets in British Columbia and north-central Alberta. LTS holds legal title to the real property interests of the Partnerships.[10]

12. Through the foregoing three business units, the Lightstream Group is the operator of, and owns varying working interests in approximately 2,582 oil and natural gas wells (gross), an extensive network of pipelines and gathering systems and numerous facilities.[11]

B. Financial Position of the Lightstream Group

13. As at June 30, 2016, the Lightstream Group had total assets with a book value of $1,679,550,000 consisting of current assets with a book value of $77,414,000 and non-current assets with a book value of $1,602,136,000.[12]

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[7] Scott Affidavit at paras 8, 9, 11.

[8] Scott Affidavit at paras 10, 12.

[9] Scott Affidavit at para 18.

[10] Scott Affidavit at para 19.

[11] Scott Affidavit at para 32.

[12] Scott Affidavit at para 43.

14. As at June 30, 2016, the Lightstream Group had total liabilities of $1,912,025,000.[13] Some significant liabilities of the Lightstream Group (collectively, the "**Debt Obligations**") include:

(a) credit facilities provided under a Third Amended and Restated Credit Agreement dated May 29, 2012, as amended by a consent and first amending agreement made as of July 2, 2015, and as further amended by a second amending agreement made as of December 2, 2015 (collectively, as amended, restated, supplemented, replaced or otherwise modified from time to time, the "**Credit Agreement**"), with LTS, as borrower, The Toronto-Dominion Bank, as administration agent (the "**Agent**"), and certain other financial institutions, as lenders (together with the Agent, the "**First Lien Lenders**"). As of September 15, 2016, the aggregate amount of principal outstanding under the credit facilities was approximately $371 million (including issued letters of credit but excluding hedging liabilities). The credit facilities under the Credit Agreement are secured by a first priority security interest over substantially all of the property and assets of LTS;[14]

(b) the Secured Notes issued pursuant to an indenture dated as of July 2, 2015 (the "**Secured Note Indenture**"), among LTS, as issuer, the other members of the Lightstream Group as guarantors, and Computershare Trust Company of Canada as Canadian trustee and collateral agent (the "**Secured Note Indenture Trustee**"). The principal amount outstanding under the Secured Note Indenture as of June 30, 2016 is approximately $845,585,000. The Secured Notes are secured by a second priority lien over all of Lightstream Group's assets pursuant to demand debentures dated July 2, 2015 from each member of the Lightstream Group in favour of the Secured Note Indenture Trustee;[15]

(c) the Unsecured Notes issued pursuant to an indenture dated as of January 30, 2012 (as supplemented by the supplemental indenture dated as of February 25,

[13] Scott Affidavit at para 46.

[14] Scott Affidavit at paras 48, 51, 54.

[15] Scott Affidavit at paras 46, 61, 63.

2015, collectively, the "**Unsecured Note Indenture**") between LTS, as issuer, 1863359, 1863360, LTS Partnership, Bakken Partnership, U.S. Bank National Association (now Wilmington Trust), as trustee, and Computershare Trust Company of Canada, as Canadian trustee). The principal amount outstanding under the Unsecured Note Indenture as of June 30, 2016 is approximately $325,390,000.[16]

C. Circumstances Leading up to these CCAA Proceedings

(i) Decline in the Oil Industry

15. The global decline of oil and gas prices has caused the Lightstream Group financial difficulty and liquidity constraints. The severe decline in commodity prices has also led to a significant reduction in the current value of the Lightstream Group's reserves.[17]

(ii) Defaults under the Credit Agreement, Secured Note Indenture and Unsecured Note Indenture

16. On June 15, 2016, LTS did not make an interest payment in the amount of US$32.1 million to the Secured Noteholders, which as of July 15, 2016, subject to the stay of proceedings in the Preliminary Interim Order, caused an event of default under the Secured Note Indenture, which in turn caused cross-defaults under the Credit Agreement and Unsecured Note Indenture.[18]

17. On July 28, 2016, LTS did not eliminate a borrowing base shortfall under the Credit Agreement and as a result, LTS is in default of the Credit Agreement.[19]

18. LTS did not make the interest payment in the amount of US$10,951,421.26 due on August 2, 2016 as required by the Unsecured Note Indenture, which as of September 1, 2016, subject to the stay of proceedings in the Preliminary Interim Order, caused an event of default

[16] Scott Affidavit at paras 46, 69.
[17] Scott Affidavit at para 78.
[18] Scott Affidavit at para 65.
[19] Scott Affidavit at para 55.

under the Unsecured Note Indenture and cross-defaults under the Credit Agreement and Secured Note Indenture.[20]

(iii) Second Forbearance Agreement and Support Agreement

19. On September 15, 2016, the Lightstream Group reached an agreement (the "**Second Forbearance Agreement**") with the First Lien Lenders in which the First Lien Lenders have agreed to forbear from exercising their rights and remedies in respect of the above mentioned defaults under the Credit Agreement throughout the Relief Period (as defined in the Second Forbearance Agreement), which in the case of the Lightstream Group's commencement of proceedings under the CCAA, extends to 2:00 pm (Calgary time) on December 31, 2016.[21]

20. As noted above, the Lightstream Group has also entered into the Support Agreement with members of the *Ad Hoc* Committee of Secured Noteholders.[22]

21. As a result of the inability of the Lightstream Group to reach a settlement of the Unsecured Noteholder Litigation with certain holders of the Unsecured Notes, the Support Agreement requires that the Lightstream Group take all necessary steps to seek an initial order under the CCAA and commence these CCAA proceedings for the purpose of implementing a sale of all or substantially all of the Lightstream Group's assets or business.[23]

(c) Unsecured Noteholder Litigation

22. LTS is party to the Unsecured Noteholder Litigation commenced against it in the Court by Mudrick Capital Management, LP ("**Mudrick**"), Court File No. 1501-08782 (the "**Mudrick Action**") and by FrontFour Capital Corp ("**FrontFour Capital**") and FrontFour Group LLC ("**FrontFour Group**" and together with FrontFour Capital, "**FrontFour**"), Court File No. 1501-07813 ("**FrontFour Action**" and together with the Mudrick Action, the "**Actions**"). LTS has filed statements of defence in the Actions denying the allegations of Mudrick and FrontFour and that they are entitled to the relief they seek in the Actions. The statements of defence filed by LTS in the Actions are collectively attached at Tab 1, hereto.

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[20] Scott Affidavit at para 71.

[21] Scott Affidavit at para 57.

[22] Scott Affidavit at para 66.

[23] Scott Affidavit at para 67.

23. The Lightstream Group was not able to reach a satisfactory settlement with respect to the Unsecured Noteholder Litigation on or before September 16, 2016 and, in accordance with the Support Agreement, the Lightstream Group has brought an application to commence these CCAA proceedings.[24]

III. LAW AND ARGUMENT

A. The CCAA applies to the Applicants

24. The CCAA applies in respect of a "debtor company" or "affiliated debtor companies" where the total claims against the debtor or its affiliates exceeds five million dollars.[25]

(i) The Applicants are each a "debtor company" under the CCAA

25. Each of the Applicants is incorporated under the ABCA and, accordingly, each is a "company" to which the CCAA applies.[26]

26. Under section 2 of the CCAA, a "debtor company" includes an insolvent company. Insolvency is not defined in the CCAA but courts have interpreted the term with reference to section 2(1) of the *Bankruptcy and Insolvency Act,* RSC 1985, c B-3 (the "**BIA**"),[27] which provides as follows:[28]

> "insolvent person" means a person who is not bankrupt and who resides, carries on business or has property in Canada, and whose liability to creditors provable as claims under this Act amount to one thousand dollars, and
>
> (a) who is for any reason unable to meet his obligations as they generally become due,
>
> (b) who has ceased paying his current obligations in the ordinary course of business as they generally become due, or
>
> (c) the aggregate of whose property is not, at a fair valuation, sufficient, or if disposed of at a fairly conducted sale under legal process, would not be sufficient to enable payment of all his obligations, due and accruing due.

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[24] Scott Affidavit at para 75.

[25] CCAA, s 3(1). [**TAB 2**]

[26] Scott Affidavit at para 99.

[27] BIA, s 2, "insolvent person". [**TAB 3**]

[28] *Re Stelco Inc*, [2004] OJ No 1257 at paras 21-22, 28 (Sup Ct), ("***Stelco***"); leave to appeal to C.A. refused, [2004] OJ No 1903; leave to appeal to S.C.C. refused, [2004] SCCA No 336. [**TAB 4**]

27. A company is deemed to be insolvent if any one of the factors set out above is satisfied.

28. But for the Second Forbearance Agreement, the Support Agreement and the stay of proceedings granted pursuant to the Arrangement Proceedings, all amounts outstanding in respect of the Credit Facility, the Secured Note Indenture and the Unsecured Note Indenture would become immediately due and owing, and the Lightstream Group does not have sufficient liquidity to pay those amounts.[29] Accordingly, each of the Applicants is an "insolvent person" and "debtor company" to which the CCAA applies.

(ii) The Applicants have Claims against them in Excess of $5 Million

29. As set out above, as at June 30, 2016, the Lightstream Group had total liabilities of $1,912,025,000, which is made up of, among other things, amounts owing under the Credit Agreement, the Secured Note Indenture, the Unsecured Note Indenture and decommissioning liabilities.

B. A Broad Stay of Proceedings is Necessary to Preserve the *Status Quo*

(i) The Stay of Proceedings should be Provided to the Applicants

30. Pursuant to Section 11.02 of the CCAA, the Court has discretion to make an order staying proceedings, restraining further proceedings or prohibiting the commencement of proceedings "on any terms that it may impose" and "effective for the period that the court considers necessary" provided the initial stay period is no longer than 30 days.[30]

31. The Applicants seek a stay of proceedings in this case for an initial period of 30 days.

32. The overarching goal of an initial order like the one sought in these proceedings is to maintain the *status quo* for a period while the insolvent company attempts to gain the approval of its creditors for a proposed arrangement which will enable the company to remain in operation for what is, hopefully, the future benefit of both the company and its creditors,[31] or in the absence of a plan, to preserve the going concern value of the insolvent company and

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[29] Scott Affidavit at para 102.

[30] CCAA, s 11.02(1). **[TAB 2]**

[31] *Meridian Developments Inc v Toronto Dominion Bank,* 1984 CarswellAlta 259 at para 21 (QB). **[TAB 5]**

achieve a sale of the insolvent company as a going concern.[32] Proceedings under the CCAA are well-suited to the current economic downturn in Alberta, as they allow companies to restructure their businesses either through a plan of arrangement or through a sale of their business as a going concern to the extent possible.[33]

33. The CCAA has been described as a statute 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." The Court has also expressly recognized one of the purposes of the CCAA to be the facilitation of ongoing operations of a business where its assets have a greater value as part of an integrated system than individually.[34]

34. The power to grant a stay of proceedings should be construed broadly in order to permit the CCAA to accomplish its legislative purpose and to enable continuance of the company seeking CCAA protection.[35]

35. The requested stay of proceedings, which substantially conforms to the stay provisions in the Alberta Template CCAA Initial Order, will allow the Lightstream Group to maintain its operations while giving it the necessary time to facilitate any operational restructuring and the implementation of the Sale Procedures, each with a view to the long-term benefit of the Lightstream Group's creditors and stakeholders.

(ii) The Stay of Proceedings should Extend to the Partnerships

36. The CCAA applies to debtor companies but does not expressly apply to partnerships.[36] Where, however, the operations of partnerships are integrally and closely interrelated to and intertwined with the operations of the Applicants, it is well-established that a Court has the

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[32] *Nortel Networks Corp, Re*, 2009 CarswellOnt 4467 at para 47 (SCJ) [Comm List], ("***Nortel***"). [**TAB 6**]

[33] *Sanjel Corp, Re*, 2016 ABQB 257 at para 66. [**TAB 7**]

[34] *Lehndorff General Partner Ltd, Re*, [1993] OJ No 14 at paras 5-7 (Gen Div) [Comm List], ("***Lehndorff***") [**TAB 8**]; *Nortel* at para 47. [**TAB 6**]

[35] *Lehndorff* at para 10. [**TAB 8**]

[36] CCAA, s 2, "debtor company". [**TAB 2**]

jurisdiction to extend the protection of the stay of proceedings to those partnerships in order to ensure that the purposes of the CCAA can be achieved.[37]

37. The Partnerships are wholly owned by the Applicants. In particular: (i) LTS owns 99.99% of Bakken Partnership and 1863360 owns the remaining 0.01%; and (ii) LTS owns 99.99% of LTS Partnership and 1863359 owns the remaining 0.01%. Further, LTS is the managing partner of both Partnerships.[38]

38. The Partnerships hold the mineral rights to the Bakken Business Unit, the Cardium Business Unit and the Alberta/BC Business Unit, while LTS holds legal title to the real property interests of the Partnerships.[39] Any proceedings commenced against the Partnerships would necessarily require the participation of LTS and the other Applicants.

39. The Partnerships are so integrally and closely interrelated to and intertwined with the Applicants that they are interested parties in these proceedings and the extension of the protections provided in the proposed Initial Order, including the stay, to the Partnerships is necessary in order to safeguard the Lightstream Group against any residual claims that may be asserted against the Partnerships as a result of the Lightstream Group filing these proceedings.

C. The Sale Procedures are Appropriate in the Circumstances

40. On July 13, 2016, the Lightstream Group commenced the SISP, as required by the Support Agreement and the forbearance agreement then in place between the Lightstream Group and the First Lien Lenders dated July 12, 2016.[40]

41. LTS seeks to continue the SISP in these CCAA restructuring proceedings by way of the Sale Procedures.[41]

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[37] *Lehndorff* at para 21 **[TAB 8]**; *Calpine Canada Energy Ltd, Re*, 2006 ABQB 153 at paras 32 – 34 **[TAB 9]**; Initial Order of the Honourable Justice Macleod, granted November 27, 2012, In the matter of Skope Energy Partners *et al*, Action No 1201-14864 at para 2; Initial Order of the Honourable Justice Romaine, granted August 28, 2015, In the matter of COGI Limited Partnership *et al*, Action No 1501-09807 at para 2; Initial Order of the Honourable Justice Yamauchi, granted January 21, 2015, In the matter of Southern Pacific Energy Ltd. *et al*, Action No 1501 - 00570 at para 2, (**"Southern Pacific Initial Order"**); Initial Order of the Honourable Justice Belzil, granted May 26, 2016, In the matter of Allarco Entertainment 2008 Inc *et al*, Action No 1603-09338 at para 2. **[TAB 10]**

[38] Scott Affidavit at paras 8-12.

[39] Scott Affidavit at paras 19, 20, 24, 28.

[40] Scott Affidavit at para 85.

42. Canadian courts have routinely held that when considering whether to approve a marketing process, the following questions ought to be considered:

(a) is a sale warranted at this time;

(b) will the sale be of benefit to the whole "economic community";

(c) do any of the debtors' creditors have a bona fide reason to object to a sale of the business; and

(d) is there a better viable alternative.[42]

43. The Sale Procedures are designed to thoroughly canvas the market to solicit, explore, assess and negotiate possible transactions for the sale of the Lightstream Group or a combination of one or more of its three business units, with a view to the best interests of LTS and its stakeholders.[43]

44. A court will generally approve a proposed sale process under the CCAA when it has been recommended by the Monitor and is supported by disinterested creditors, absent any compelling, exceptional circumstances to the contrary.[44] The Sale Procedures have been reviewed by the proposed Monitor, FTI Consulting Canada Inc., who is of the view that in the circumstances, the Sale Procedures: (i) provide for a broad, open, fair and transparent process for seeking interested buyers of the property, assets and operations of the Lightstream Group; (ii) provide an appropriate level of independent oversight; (iii) encourage and facilitate bidding by interested parties; and (iv) do not discourage parties from submitting offers.[45] The First Lien Lenders and the *Ad Hoc* Committee of Secured Noteholders support the proposed Sale Procedures and no party has raised any objection as at this time. Moreover, the Second Forbearance Agreement and the Support Agreement each require approval of a sale process acceptable to the First Lien Lenders and the *Ad Hoc* Committee of Secured Noteholders, respectively.

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[41] Scott Affidavit at para 88.

[42] *Nortel* at para 49. **[TAB 8]**

[43] Scott Affidavit at para 89.

[44] *Ivaco Inc, Re*, [2004] OJ No 2483 at para 21 (SCJ) [Comm List]. **[TAB 11]**

[45] Pre-Filing Report of FTI Consulting Canada Inc. in its Capacity as Proposed Monitor at para 80 (the **"Proposed Monitors Report"**).

45. The proposed Sale Procedures are appropriate in the circumstances, are recommended by the Monitor and satisfy the test for approval, and, therefore, the Applicants respectfully request that this Honourable Court approve the Sale Procedures.

D. The Priority Charges sought by the Applicants are Necessary and Appropriate

46. The Applicants seek approval of six priority charges in the Initial Order; each securing payment or performance of the Applicants' obligations to various advisors, creditors and stakeholders. Each of the requested charges is essential to the Lightstream Group's prospects of being able to successfully conduct the Sale Procedures for the benefit of all stakeholders.

47. The six charges sought by the Applicants, in order of their requested priority, are:

(a) First — an administration charge (the "**Administration Charge**"), to secure payment of professional fees;

(b) Second — a credit card charge (the "**Credit Card Charge**"), to secure the Applicants' obligations owed to HSBC Bank Canada ("**HSBC**"), one of the First Lien Lenders, in relation to certain credit cards used by the Applicants in the operation of the business (the "**Credit Cards**");

(c) Third — a directors' and officers' charge (the "**Directors' Charge**") to secure the indemnity given by the Applicants to their directors and officers pursuant to the Initial Order;

(d) Fourth — a key employee retention plan charge (the "**KERP Charge**") to secure payments under the Applicants' proposed key employee retention plan (the "**KERP**");

(e) Fifth — a key employee incentive plan charge (the "**KEIP Charge**") to secure payments under the Applicants' proposed key employee incentive plan (the "**KEIP**"); and

(f) Sixth — a financial advisors' charge (the "**Financial Advisors' Charge**") to secure the fees and disbursements of the financial advisors of the Lightstream

Group and the *Ad Hoc* Committee of Secured Noteholders (collectively, the "**Financial Advisors**").

(i) Administration Charge

48. The Applicants seek an Administration Charge in an amount not to exceed $2,000,000 to secure the professional fees and disbursements of the proposed Monitor, counsel to the proposed Monitor, counsel to the Lightstream Group, independent counsel to the Applicants' directors and officers, counsel to the First Lien Lenders, PricewaterhouseCoopers Inc. in its capacity as financial advisor to the First Lien Lenders, counsel to the *Ad Hoc* Committee of Secured Noteholders and BMO Nesbitt Burns Inc. ("**BMO**") in respect of BMO's monthly work fee.[46]

49. Section 11.52 of the CCAA expressly provides this Court with the power to grant a charge in respect of professional fees and disbursements on notice to affected secured creditors.[47]

50. Courts have held that, unless professional advisor fees are protected by way of a charge, the objectives of the CCAA would be frustrated as professionals would be unlikely to risk offering services without any assurance of ultimately being paid. Failing to provide protection for professional fees will "result in the overwhelming likelihood that the CCAA proceedings would come to an abrupt halt, followed, in all likelihood, by bankruptcy proceedings."[48]

51. The Applicants require the expertise, knowledge and continuing participation of the proposed beneficiaries of the Administration Charge in order to complete a successful restructuring, and the Administration Charge is necessary to ensure such continuing assistance and participation.[49]

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[46] Scott Affidavit at para 115.

[47] CCAA, ss 11.52(1), (2). [**TAB 2**]

[48] *Timminco Ltd, Re*, 2012 ONSC 506 at para 66, ("***Timminco***"). [**TAB 12**]

[49] Scott Affidavit at para 116.

52. The factors to be considered by a court in determining whether to approve such a priority charge include:

(a) the size and complexity of the business being restructured;

(b) the proposed role of the beneficiaries of the charge;

(c) whether there is unwarranted duplication of roles;

(d) whether the quantum of the proposed charge appears to be fair and reasonable;

(e) the position of the secured creditors likely to be affected by the charge; and

(f) the position of the Monitor.[50]

53. Consideration of these factors in the present case supports the granting of the proposed Administration Charge.

54. The Lightstream Group's business is large and complex, involving significant assets in various provinces in Western Canada. Each proposed beneficiary of the Administration Charge has a separate and clearly defined role in the proceedings and all are necessary in order to ensure a successful restructuring.

55. The quantum of the proposed charge was determined in consultation with the proposed Monitor and is fair and reasonable in light of the number of beneficiaries and the size, scope and complexity of the proposed restructuring. The proposed Monitor is of the view that the Administration Charge is appropriate.[51] Further, the size of the Administration Charge is comparable with administration charges in other recent CCAA proceedings of large corporate entities in Alberta.[52]

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[50] *Canwest Publishing Inc/Publications Canwest Inc, Re*, 2010 ONSC 222 at para 54 (SCJ) [Comm List], (***"Canwest Publishing"***). **[TAB 13]**

[51] Proposed Monitors Report at para 27.

[52] Initial Order of the Honourable Justice D.B. Nixon, granted March 8, 2016, In the Matter of Quicksilver Resources Canada Inc, Action No 1601-03113 at para 33 ($2.5 million); Southern Pacific Initial Order at para 31 ($3 million); Initial Order of the Honourable Justice B.E.C. Romaine, granted April 4, 2016, In the Matter of Sanjel Corporation *et al*, Action No 1601-03143 at para 37 ($2 million). **[TAB 14]**

(ii) Credit Card Charge

56. The Lightstream group seeks an order authorizing it to continue using and paying amounts owing under the Credit Cards it holds from HSBC in the same manner as they were used and paid pre-filing. HSBC has agreed to continue to extend credit under the Credit Cards, so long as the Lightstream Group continues to make payments on the Credit Cards, including with respect to pre-filing charges, and the Credit Card Charge is approved by the Court.[53]

57. The Lightstream Group's ability to continue using and paying the Credit Cards in this manner is another facet of its ability to carry on business in the normal course during the restructuring process. Further, the size of the Credit Card Charge ($105,000) is minor in light of the nature and value of the Lightstream Group's assets, is supported by the proposed Monitor and is being provided by one of the First Lien Lenders.[54] For these reasons, the Lightstream Group believes the Credit Card Charge is reasonable and appropriate.

(iii) Directors' Charge

58. The Applicants seek the Directors' Charge up to the maximum amount of $2,500,000 to secure the indemnity of the Applicants' directors and officers. The Directors' Charge is proposed to be in priority to all other security interests, trusts, liens, charges and encumbrances, but subordinate to the Administration Charge and the Credit Card Charge.

59. This Court has jurisdiction to grant a charge relating to directors' and officers' indemnification on a priority basis pursuant to section 11.51 of the CCAA, on notice to the affected secured creditors. The Court must be satisfied with the amount of the charge, and the order is not to extend to coverage of wilful misconduct or gross negligence and no order should be granted if adequate insurance at a reasonable cost could be obtained.[55]

60. In *Canwest Global,* Pepall J. set out some of the factors to be considered by the court when applying s. 11.51. In approving the requested directors' charge, Pepall J. stated:

> The purpose of such a charge is to keep the directors and officers in place during the restructuring by providing them with protections against liabilities they could incur during the restructuring: *Re General Publishing Co.* [(2003),

[53] Scott Affidavit at para 118.

[54] Proposed Monitors Report at paras 32 - 34.

[55] CCAA, s 11.51 (3). **[TAB 2]**

> 39 C.B.R. (4th) 216)]. Retaining the current directors and officers of the applicants would avoid destabilization and would assist in the restructuring. The proposed charge would enable the applicants to keep the experienced board of directors supported by experienced senior management. The proposed Monitor believes that the charge is required and reasonable in the circumstances and also observes that it will not cover all of the directors' and officers' liabilities in the worst case scenario. In all of these circumstances, I approved the request.[56]

61. A successful restructuring of the Applicants' business will only be possible with the continued participation of their directors and officers. These individuals have specialized expertise and relationships with the Applicants' stakeholders, as well as historical and current knowledge that cannot be replicated or replaced.[57]

62. The directors and officers of the Applicants have also expressed a desire for certainty with respect to potential personal liability if they continue in their current capacities in the context of a CCAA proceeding.

63. While the Applicants' directors and officers do have the benefit of insurance policies (the "**D&O Insurance Policies**") in respect of their potential liability, the D&O Insurance Policies only insure the directors and officers of the Applicants for certain claims that may arise against them in their capacity as directors and/or officers of the Applicants and such coverage is subject to several exclusions and limitations. There is the potential for insufficient coverage in respect of post-filing liabilities and the directors and officers have requested more certainty in the form of a charge securing any deficiency in insurance coverage. [58]

64. In addition, the Alberta Template CCAA Initial Order contemplates a Directors' Charge that does not duplicate coverage already in place pursuant to the D&O Insurance Policies. That formulation has not been changed in the Initial Order being sought by the Applicants. The proposed Directors' Charge only extends to post-filing liabilities, expressly excludes wilful misconduct and gross negligence, and does not duplicate coverage already in place under the Applicants' existing D&O Insurance Policies.[59]

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[56] *Canwest Global Communications Corp,* Re, [2009] OJ No 4286 at para 48 (SCJ) [Comm List], ("***Canwest Global***"). **[TAB 15]**

[57] Scott Affidavit at para 122.

[58] Scott Affidavit at para 123.

[59] *Canwest Global* at paras 46-48 **[TAB 15]**; *Canwest Publishing* at paras 56-57. **[TAB 13]**

65. As to the quantum of a directors' charge, the Court should also consider whether the proposed Monitor has reviewed the quantum of the charge and whether the proposed Monitor considers the amount to be reasonable.[60] With regard to the proposed Directors' Charge, the proposed Monitor views the amount of the Directors' Charge as reasonable in these circumstances and supports the charge and its quantum.[61]

(iv) KERP and KEIP Charge

66. The Applicants seek the Court's approval of the KERP Charge and the KEIP Charge which have both been designed in consultation with the proposed Monitor to incentivize employees and executives to remain in their employment during this restructuring.[62] Specifically, the proposed priority and quantum of the KERP Charge and the KEIP Charge is as follows:[63]

(a) a fourth priority Court-ordered KERP Charge (subordinate to the indebtedness to the First Lien Lenders under the Credit Agreement) up to the maximum amount of $4,115,250; and

(b) a fifth priority Court-ordered KEIP Charge (subordinate to the indebtedness to the First Lien Lenders under the Credit Agreement) up to the maximum amount of $5,007,417.

67. There is no express statutory jurisdiction in the CCAA for the Court to approve a key employee retention plan. However, courts have recognized that the approval of such plans is within the scope of their discretion under the CCAA, and such charges are regularly granted in CCAA proceedings.[64]

68. Key employee retention and incentive plans have been approved in CCAA proceedings where the continued participation of key employees is crucial to a successful restructuring or where their continued service is important for the stability of the business and

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[60] *iMarketing Solutions Group (Re),* 2013 ONSC 2223 at para 20. **[TAB 16]**

[61] Proposed Monitors Report at para 41.

[62] Scott Affidavit at para 124.

[63] Scott Affidavit at paras 130 -131.

[64] *Grant Forest Products Inc, (Re)* (2009), 57 CBR (5th) 128 at para 8 (Ont SCJ) [Comm List], (***"Grant Forest"***) **[TAB 17]**; *Canwest Global* at paras 49-50 **[TAB 15]**; *Cinram International Inc, (Re),* 2012 ONSC 3767 at paras 91-93, (***"Cinram"***). **[TAB 18]**

could not easily be replaced.[65] Without the retention of key employees and executives, the Lightstream Group's ability to successfully maintain its business operations and preserve asset value while it restructures and carries out these proceedings would be seriously compromised.[66]

69. The following factors have been identified as considerations in determining whether to approve a key employee retention or incentive plan and related charge(s):

(a) whether the Monitor supports the key employee retention or incentive plan and related charge(s);

(b) whether the beneficiaries of the key employee retention or incentive plan are likely to consider other employment opportunities if the plan is not approved;

(c) whether the continued employment of the employees to which the key employee retention or incentive plan applies is important for the stability of the business and to enhance the effectiveness of the marketing process;

(d) the employees' history with and knowledge of the debtor;

(e) the difficulty in finding a replacement to fulfill the responsibilities of the employees to which the key employee retention or incentive plan applies;

(f) whether the key employee retention or incentive plan and related charge(s) were approved by the board of directors, including the independent directors;

(g) whether the key employee retention or incentive plan and related charge(s) are supported or consented to by the secured creditors of the debtor; and

(h) whether the key employee retention or incentive plan payments are payable upon the completion of the restructuring process.[67]

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[65] *Nortel Networks Corp (Re)*, [2009] OJ No 1044 at paras 4, 19 (SCJ) [Comm List] **[TAB 19]**; *US Steel Canada Inc, (Re)*, 2014 ONSC 6145 at paras 27-33 **[TAB 20]**; *Target Canada Co, (Re),* 2015 ONSC 303 at paras 57-59. **[TAB 21]**

[66] Scott Affidavit at para 125.

[67] *Cinram* at para 91 **[TAB 18]**, citing *Grant Forest* at paras 8- 24 **[TAB 17]**; *Canwest Publishing* at para 59 **[TAB 13]**; *Canwest Global* at para 49 **[TAB 15]**; *Timminco* at para 72. **[TAB 12]**

70. Since December 31, 2014, LTS has reduced its staff from 433 employees to less than 300 employees, a reduction of over 30%. The proposed KERP applies to 193 employees of LTS. Without the retention of these employees, the Lightstream Group's ability to successfully maintain its business operations and preserve asset value in these CCAA proceedings would be compromised. The proposed KERP is only payable to beneficiaries thereof if the successful bid pursuant to the Sale Procedures is other than the Secured Noteholder Credit Bid, or in the case that the Secured Noteholder Credit Bid is the successful bid, where employment is not offered to such employees on terms including recognition of seniority consistent with current terms of employment.[68]

71. The KEIP has been designed to incentivize a relatively small number of senior executives of LTS to maximize proceeds of any sale pursuant to the Sale Procedures. The KEIP applies to only nine employees, or approximately 3% of the total number of employees of LTS. Compensation pursuant to the KEIP is only payable to these senior executives if the successful bidder pursuant to the Sale Procedures is a party other than the Secured Noteholders, or in the case that the Secured Noteholder Credit Bid is the successful bid, where employment is not offered to such senior executives on terms including recognition of seniority consistent with current terms of employment, and if certain sale proceeds thresholds are achieved.

72. The beneficiaries of the KEIP are certain senior executives of LTS, who have valuable corporate knowledge that cannot easily be replaced or replicated and/or are engaged in relationships with key clients. In addition, these particular employees have been working diligently for several months to restructure the Lightstream Group to the benefit of all stakeholders. Their continued employment is integral to the Lightstream Group's efforts to maintain its business and improve its financial position, including efforts to source, review and implement a sale, restructuring or recapitalization transaction.[69]

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[68] Scott Affidavit at para 125.

[69] Scott Affidavit at paras 126 - 127.

73. Any amounts received by beneficiaries of the KERP or KEIP are to be applied towards any statutory or contractual severance entitlements of those employees and will mitigate any potential claims that may otherwise by brought by those employees.[70]

74. The proposed Monitor has reviewed the proposed KERP and KEIP and has advised that they are reasonable in the circumstances and their implementation will be beneficial to the Lightstream Group and its stakeholders.[71]

75. Finally, the proposed KERP and KEIP are consistent with current practice for retention plans in the context of a CCAA proceeding and the quantum of the proposed payments under the KERP and KEIP is consistent with the relative size of KERP and KEIP charges granted in other complex CCAA restructurings.[72]

(v) Financial Advisors' Charge

76. The Financial Advisors have been engaged by LTS and its board of directors to assist the Lightstream Group with its strategic review process, the SISP, the Sale Procedures, the Unsecured Noteholder Litigation and to advise the directors and officers of LTS in these restructuring proceedings (and the Arrangement Proceedings which preceded them).[73]

77. In addition, the *Ad Hoc* Committee of Secured Noteholders has engaged BMO as its financial advisor to solicit, explore, assess and negotiate possible transactions for the sale of the Lightstream Group or its assets or any part thereof. The requirement to pay BMO is an obligation of the Company under the Support Agreement and is expressly permitted in the Forbearance Agreement.[74]

78. It is contemplated that the Financial Advisors will be granted a sixth priority Court-ordered charge on the assets, property and undertakings of the Lightstream Group, in priority to all other charges but subordinate to the Administration Charge, Credit Card Charge, the Directors' Charge, the indebtedness to the Agent and First Lien Lenders under the Credit

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[70] Scott Affidavit at para 128.

[71] Proposed Monitors Report at para 51.

[72] Proposed Monitors Report at para 46; *supra*, note 65.

[73] Scott Affidavit at para 132.

[74] Scott Affidavit at para 57.

Agreement, the KERP Charge and the KEIP Charge up to the maximum amount of $19,410,000.[75]

79. As with the Administration Charge, section 11.52 of the CCAA gives this Court jurisdiction to grant the Financial Advisors' Charge. The six factors in *Canwest Publishing*, referenced above at paragraph 53, apply to the determination of whether to grant such a charge.[76] The application of these factors in the present case supports the granting of the proposed Financial Advisors' Charge.

80. The Financial Advisors continue to provide services to the Lightstream Group and the board of directors of LTS and are crucial to the continued negotiations with the Unsecured Noteholders, the *Ad Hoc* Committee of Secured Noteholders as well as with the continuation of the Sale Procedures.

81. The Lightstream Group and *Ad Hoc* Committee of Secured Noteholders require the expertise, knowledge and continuing participation of the proposed beneficiaries of the Financial Advisors' Charge in order to complete a successful restructuring.[77]

82. The appointment of multiple advisors has been recognized as appropriate where there is a coordinated effort that will assist restructuring parties in achieving their goals, and where the joint enterprise is expected to produce a better result overall.[78]

83. Furthermore, the Lightstream Group's operations are large and complex, and the proposed Monitor has found the Financial Advisors' Charge is reasonable and appropriate in the circumstances.[79] Given the foregoing, the priority and quantum of the Financial Advisors' Charge is justified and appropriate in the circumstances.

E. The Lightstream Group should Retain Operatorship

84. As mentioned above, the Lightstream Group is the operator of, and owns varying working interests in approximately 2,582 oil and natural gas wells (gross), an extensive

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[75] Scott Affidavit at para 134.

[76] *Canwest Publishing* at para. 54. **[TAB 13]**

[77] Scott Affidavit at para 135.

[78] *Walter Energy Canada Holdings Inc, Re*, 2016 BCSC 107 at para 44. **[TAB 22]**

[79] Proposed Monitors Report at para 58.

network of pipelines and gathering systems and numerous facilities (collectively, the "**Wells**").[80]

85. Operation of the Wells requires specialty trade and other qualified, experienced personnel in order to comply with licence requirements and to ensure continued safety. There are important rights and obligations that are assumed by operators, including the provision of fees in exchange for the continued operation of the Wells and associated facilities.[81]

86. The CCAA is intended to continue the operations of companies in the normal course during the pendency of proceedings under the CCAA and this Court has found that authority to stay proceedings under the CCAA is broad enough to stay the termination or replacement of an operator where operatorship is essential to maintain the *status quo*.[82]

87. In the case of the Lightstream Group, the continued operatorship of the Wells, which form the core part of the Lightstream Group's business and are an important source of revenue, is necessary in order for it to successfully carry out these proceedings under the CCAA.[83] The Lightstream Group has access to sufficient funds, the necessary employees and the requisite expertise to continue operatorship of the Wells. Moreover, the transition to a new operator of the Wells would require a time consuming and costly transition period.[84]

88. As a result, it is appropriate that this Honourable Court exercise its discretion under section 11 of the CCAA to stay any attempts to remove any of the Lightstream Group entities as operator of the Wells as a result of these CCAA proceedings.

F. The Actions are Claims Capable of being Stayed

89. As noted above, Mudrick and FrontFour (collectively, the "**Plaintiffs**") have brought an application seeking an order: (a) excluding their claims against LTS from the stay of proceedings in the Initial Order; and (b) directing a trial of the issues raised in the Actions

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[80] Scott Affidavit at para 32.

[81] Scott Affidavit at para 33.

[82] *Norcen Energy Resources Ltd v Oakwood Petroleums Ltd* (1988), 92 AR 81 (QB) at para 79. [**TAB 23**]

[83] Scott Affidavit at para 34.

[84] Scott Affidavit at paras 35 - 36.

prior to hearing any further orders or proceedings with respect to LTS' application under the CCAA.[85]

90. There is no basis to exclude the Actions from the stay of proceedings sought in the Initial Order. Upon commencement of the CCAA proceedings, whatever claims the Plaintiffs have against LTS become claims in the CCAA. This is consistent with the purpose of the CCAA and the single proceeding model established for the protection of all creditors. The Plaintiffs' claims should and will be dealt with in the CCAA proceedings.[86]

91. The Plaintiffs each purchased Unsecured Notes in the secondary market, with the contractual rights associated with them, and they plead that these contractual rights have been breached by LTS.[87] The Plaintiffs also allege that based on a misrepresentation, they held on to their Unsecured Notes instead of selling them into the market.[88] The remedy for both of these allegations, if the Plaintiffs are successful in advancing such claims, is an award of damages in the amount of the diminution in value of the Unsecured Notes caused by either the alleged breach of contract or the alleged tort of misrepresentation. These claims, if successfully advanced, would, at best, give rise to an unsecured damages claim in the CCAA proceedings.

92. In the pending Actions, the Plaintiffs also seek a declaration that they were entitled to participate in the transaction in which the Secured Notes were issued and an order requiring Lightstream to issue Secured Notes under section 242(3)(e) of the ABCA to remedy alleged oppressive conduct.[89] This claim, like any other claim of the Plaintiffs against the Lightstream Group, becomes subsumed within the single proceeding model of the CCAA.

93. A threshold issue arises on the facts as pleaded by the Plaintiffs as to whether the specific performance they are seeking under the oppression remedy is available in the CCAA. This is not an issue to be decided outside of the CCAA proceedings, but within them. The Lightstream Group submits that the determination of whether this claim for specific

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[85] Affidavit of David Kirsch sworn September 23, 2016 at paras 28 - 29 (the **"Kirsch Affidavit"**).

[86] CCAA, s 2(1), "claim". **[TAB 2]** See also *AbitibiBowater Inc, Re*, 2012 SCC 67 at paras 21-26. **[TAB 24]**

[87] Kirsch Affidavit at paras 16 -18, 21-22.

[88] Kirsch Affidavit at para 16.

[89] ABCA, s 242(3)(e). **[TAB 25]**

performance is tenable within the CCAA should be the subject of judicial determination on an expedited basis in order to make the most efficient use of the Court's resources.

94. If the Court accepts the Lightstream Group's position that, based upon the pleadings in the Actions, the Plaintiffs could only ever have an unsecured claim for the value of their Unsecured Notes plus interest, in accordance with the Unsecured Note Indenture, there will be no basis to have the underlying lawsuit, which has merged into the CCAA, be the subject of a contested trial-like proceeding.

G. The Deadline for LTS to hold an Annual General Meeting should be Extended

95. Pursuant to section 132(1)(a) of the ABCA, LTS is required to hold its annual general meeting ("**AGM**") within 15 months of its last preceding AGM.

96. LTS held its last AGM on May 14, 2015 and accordingly, LTS was required to hold its next AGM on or before August 14, 2016.[90] On August 5, 2016, the Honourable Mr. Justice C.M. Jones granted an Interim Order (the "**Interim Order**") in the Arrangement Proceedings, which, among other things, extended the time by which LTS must hold the 2016 AGM to on or before September 30, 2016.

97. It is not clear that LTS will have quorum to hold the scheduled AGM on September 30, 2016. As a result, LTD may be required to reschedule the AGM to a later date in any event.[91]

98. LTS applies to this Honourable Court pursuant to subsection 132(2) of the ABCA and section 11 of the CCAA for Court approval pursuant to subsection 132(4) of the ABCA, to postpone its next AGM to as late as March 31, 2017, at which time LTS and the rest of the Lightstream Group expects to have greater clarity regarding the restructured ownership interests in the Lightstream Group and its ability to continue as a going concern.

99. Courts have commonly granted extensions of time for the calling of an annual general meeting in CCAA proceedings where it is found a company's time is better used toward stabilizing business and implementing a plan. [92]

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[90] Supplemental Affidavit of Peter D. Scott sworn September 23, 2016 at para 6 ("**Supplemental Scott Affidavit**").

[91] Supplemental Scott Affidavit at para 8.

100. The shareholders of LTS will not suffer any prejudice should the calling of the AGM be postponed.[93] The proposed extension is reasonable and consistent with other extension requests in CCAA proceedings.[94] Given the forgoing, the Applicants submit that it is appropriate for the time for LTS to hold its AGM to be extended to March 31, 2017, after the conclusion of these CCAA proceedings.

IV. NATURE OF THE ORDER SOUGHT

101. The Applicants seek an Initial Order under the CCAA substantially in the form as attached to the Originating Application.

ALL OF WHICH IS RESPECTFULLY SUBMITTED THIS 26th DAY OF SEPTEMBER, 2016

BLAKE, CASSELS & GRAYDON LLP

Kelly Bourassa
Counsel to the Lightstream Group

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[92] *Canwest Global* at para 54. **[TAB 15]** See also *Sino-Forest Corporation (Re)*, 2012 ONSC 2063 at para 44 in which the Court granting the CCAA initial order also extended the time for the AGM of the debtor. **[TAB 26]**

[93] Supplemental Scott Affidavit at para 10.

[94] *Canwest Global* at para 54 **[TAB 15]**; In the Matter of Growthworks Canada Fund Ltd, Action No 1601-03113 at para 2 (8 Months). **[TAB 27]**

TABLE OF AUTHORITIES

TAB 1

Form 11
[Rule 3.31]

Clerk's stamp:

COURT FILE NUMBER	**1501-07813**
COURT OF QUEEN'S BENCH OF ALBERTA	
JUDICIAL CENTRE	**CALGARY**
PLAINTIFFS	**FRONTFOUR CAPITAL CORP.**
	FRONTFOUR CAPITAL GROUP LLC.
DEFENDANT	**LIGHTSTREAM RESOURCES LTD.**
DOCUMENT	**STATEMENT OF DEFENCE**
PARTY FILING THIS DOCUMENT	**LIGHTSTREAM RESOURCES LTD.**
ADDRESS FOR SERVICE AND CONTACT INFORMATION OF PARTY FILING THIS DOCUMENT	**BLAKE, CASSELS & GRAYDON LLP** **3500, 855 – 2nd Street S.W.** **Calgary, AB T2P 4J8** **Attn: Michael Barrack/Richard D. Bell/Emily Bala** **Telephone/Facsimile: 403-260-9656/403-260-9700** **Email: michael.barrack@blakes.com** **richard.bell@blakes.com** **emily.bala@blakes.com** **File Ref.: 89691/5**

Note: State below only facts and not evidence (Rule 13.6)

Statement of facts relied on:

1. The Defendant, Lightstream Resources Ltd ("**Lightstream**"), admits the facts set out in the following paragraphs in the Statement of Claim: 5, 6, 8, 18, 21 and 22.

2. Lightstream has no knowledge in respect of the facts contained in paragraphs 1, 2, 3, 4, 15, 16, 19, 20, 31, 32 and 33.

3. Except as expressly admitted herein, Lightstream denies all other allegations set out in the Statement of Claim and denies that the Plaintiffs are entitled to any relief.

The Unsecured Notes

4. On January 30, 2012, Lightstream closed a private placement offering of senior unsecured notes (the "**Unsecured Notes**") that bear interest at a rate of 8.625% per

annum and mature February 1, 2020. Offering the Unsecured Notes was in Lightstream's best interests, as it diversified Lightstream's capital and provided ongoing liquidity and the subsequent opportunity to repurchase and cancel certain of its then-outstanding unsecured convertible debentures.

5. The Unsecured Notes are governed by an indenture dated January 30, 2012, as amended by a supplemental indenture (collectively, the "**2012 Indenture**").

6. Section 4.06(a) of the 2012 Indenture specifies that Lightstream may properly incur further indebtedness if a fixed charge coverage ratio test is satisfied.

7. Section 4.06(b) of the 2012 Indenture provides that, notwithstanding s. 4.06(a), there are also several other options through which Lightstream may properly incur further indebtedness (the "**Permitted Debt Baskets**"). These Permitted Debt Baskets are enumerated in the subsections of s. 4.06(b).

8. One of the Permitted Debt Baskets under s. 4.06(b) is set out in s. 4.06(b)(i) (the "**Credit Facility Basket**"). The Credit Facility Basket expressly permits Lightstream to incur further indebtedness in the form of, *inter alia*, notes, debentures, bonds or similar securities or instruments, up to a specified amount.

9. A separate Permitted Debt Basket is set out in s. 4.06(b)(v) (the "**Permitted Refinancing Basket**"). While indebtedness incurred under the Permitted Refinancing Basket may not mature earlier than the Unsecured Notes, there is no such restriction on indebtedness incurred under the Credit Facility Basket.

10. Section 4.06(d) of the 2012 Indenture confirms that where indebtedness falls within more than one of the Permitted Debt Baskets, it can be incurred in whole or in part under any one or more Permitted Debt Baskets and subsequently re-allocated in whole or in part at any time between or among any one or more Permitted Debt Baskets.

11. Section 4.06(c) of the 2012 Indenture deals further with indebtedness. While Section 4.06(c) provides that Lightstream may not incur any further indebtedness that is contractually subordinated in right of payment to other debt unless it is also subordinate to the Unsecured Notes, the provision also provides that indebtedness will <u>not</u> be

deemed contractually subordinated in right of payment to further debt incurred by Lightstream, *inter alia*, solely by virtue of being unsecured.

12. Section 4.08 of the 2012 Indenture specifies the circumstances under which indebtedness may be secured by a lien (the "**Permitted Liens**"). Indebtedness incurred under the Credit Facility Basket is specifically permitted to be secured by a lien under the first clause of the definition of "Permitted Liens".

13. Section 6.06 of the 2012 Indenture prevents holders of Unsecured Notes from commencing proceedings with respect to the 2012 Indenture, or regarding the Unsecured Notes, unless specific preconditions are met. These preconditions include that the Trustee or Canadian Trustee must first be requested to take action itself by holders of at least 25% in aggregate principal amount of the outstanding Unsecured Notes, and that the Trustee or Canadian Trustee must have failed to comply with that request after 60 days.

14. Section 9.02 of the 2012 Indenture states that there are only certain enumerated types of changes to the 2012 Indenture or the Unsecured Notes that require Lightstream to obtain the consent of each affected holder before making the change in question. The Transaction (as defined below) did not involve any such changes to the 2012 Indenture or the Unsecured Notes.

15. The offering memorandum for the Unsecured Notes (the "**Offering Memorandum**") identifies risk factors relevant to the Unsecured Notes. These risk factors arise out of the terms of the 2012 Indenture.

16. As confirmed in the Offering Memorandum's discussion of risk factors, the 2012 Indenture permits Lightstream to incur substantial additional debt, including secured debt, and provides that the Unsecured Notes will be effectively junior in right of payment to existing and future secured debt.

17. Other risk factors of the Unsecured Notes, which are described in the Offering Memorandum, include that there is no assurance of an active trading market for the Unsecured Notes, that holders may be required to bear the risk of their investment

indefinitely, and that if an active trading market does develop, the market price for the Unsecured Notes may be volatile.

18. As permitted under the 2012 Indenture and confirmed in the Offering Memorandum, Lightstream may at any time and from time to time repurchase the Unsecured Notes, in the open market or otherwise.

The Transaction

19. On July 2, 2015, Lightstream announced that it had entered into a privately negotiated agreement (a) to repurchase certain Unsecured Notes from certain holders in exchange for the issuance by Lightstream of new secured notes (the "**Secured Notes**"), and (b) to issue additional Secured Notes to the same holders for $200 million (US) paid to Lightstream (the "**Transaction**"). The Secured Notes bear interest at a rate of 9.875% per annum and mature June 15, 2019.

20. Lightstream issued the Secured Notes under the Credit Facility Basket and granted liens for the benefit of the Secured Notes pursuant to the first clause under the definition of "Permitted Liens", as expressly permitted and contemplated under the terms of the 2012 Indenture.

21. Lightstream did not rely upon the Permitted Refinancing Basket of the 2012 Indenture in order to complete the Transaction, nor upon Section 4.06(a).

22. The Transaction was in Lightstream's best interest. It benefitted Lightstream, *inter alia*, by reducing its debt by approximately $90 million and increasing its credit availability by approximately $250 million.

23. The Transaction closed in two tranches on July 2 and July 14, 2015.

The Plaintiffs' Demand to Join the Transaction

24. In early 2015, the Plaintiffs advised Lightstream that they held Unsecured Notes.

25. On July 3, 2015, following the announcement of the Transaction, representatives of the Plaintiffs spoke with representatives of Lightstream. The Plaintiffs acknowledged that the Transaction was a good transaction and positive for Lightstream, and requested to be included in the Transaction on its terms. Pursuant to its rights under the 2012 Indenture

and having regard to the best interests of the corporation, Lightstream declined this request.

26. On July 6, 2015, the Plaintiffs wrote to Lightstream, confirming that they considered the Transaction attractive and demanding to be included in the Transaction on its terms. In this letter, the Plaintiffs threatened legal proceedings against Lightstream unless Lightstream included the Plaintiffs in the Transaction.

27. On July 8, 2015, as requested, Lightstream replied to the Plaintiffs' demand letter. Lightstream correctly asserted that the Transaction was permissible under the 2012 Indenture and that the Plaintiffs had no legal claim.

28. The Plaintiffs filed the Statement of Claim in the within action on July 9, 2015 with the express objective of pressuring Lightstream into inviting them into the Transaction.

29. Prior to commencing this action, the Plaintiffs failed to follow the procedure required under Section 6.06 of the 2012 Indenture for raising their purported concern to the Trustee or Canadian Trustee.

Any matters that defeat the claim of the Plaintiffs:

No Oppression and No Breach of the 2012 Indenture

30. Lightstream denies that its actions, with respect to the Transaction or at all, were oppressive within the meaning of the *Business Corporations Act*.

31. Lightstream has not contravened any reasonable expectation or right of the Plaintiffs, either through the Transaction – which, as the Plaintiffs acknowledged, was in Lightstream's best interests – or at all.

32. The Plaintiffs had no reasonable expectation that they would be included in, given advance notice of, or consulted on the Transaction. At no time did Lightstream represent to the Plaintiffs that they would be invited to participate in or be given advance notice of the Transaction.

33. The Plaintiffs are sophisticated market participants with experience in negotiating the terms of high-yield indentures and in assessing and valuing securities. The primary

sources of the Plaintiffs' reasonable expectations in this case are the terms of the 2012 Indenture.

34. In reply to paragraph 29 and to the whole of the Statement of Claim, the Transaction is consistent with the terms of the 2012 Indenture.

35. The 2012 Indenture expressly permits the Transaction, pursuant to the Credit Facility Basket provision and its associated Permitted Lien. Under the Credit Facility Basket provision, Lightstream is permitted to secure new indebtedness with a lien, and the Secured Notes may mature earlier than the Unsecured Notes.

36. In reply to paragraphs 10-14 of the Statement of Claim, the allegations with respect to Permitted Refinancing Indebtedness are irrelevant to the Transaction, which did not rely on the Permitted Refinancing Basket. These assertions are also inaccurate. For example, paragraph 12 of the Statement of Claim is incorrect regarding the meaning of "contractually subordinated in right of payment" under s. 4.06(c) of the 2012 Indenture, as set out further below.

37. In reply to paragraphs 12 and 29(b) of the Statement of Claim, s. 4.06(c) of the 2012 Indenture provides that "contractually subordinated in right of payment" does not include subordination by virtue of a lien, as occurred in the Transaction.

38. Subordination in right of payment is distinct from subordination by virtue of security. Under the 2012 Indenture, as expressly noted in the Offering Memorandum, one of the risks of holding the Unsecured Notes is that the right to receive payment is effectively subordinate to not only existing but future permitted secured creditors, to the extent of the value of the security.

39. In reply to paragraph 24 of the Statement of Claim, there was no obligation on Lightstream under the 2012 Indenture to invite all holders of Unsecured Notes to participate in the Transaction, or to notify all holders that the Transaction was being considered.

40. In reply to paragraph 14 of the Statement of Claim, the Transaction did not impair or otherwise affect the rights of any of the holders of Unsecured Notes, including the Plaintiffs. The Transaction did not result in any changes to the Unsecured Notes or to

the 2012 Indenture. The negotiated private repurchase of Unsecured Notes from certain holders is not an impairment of rights under the 2012 Indenture.

41. As the Plaintiffs are aware and as confirmed in the Offering Memorandum, Lightstream may, at any time and from time to time, repurchase notes in the open market or otherwise. Lightstream has the ability under the 2012 Indenture to incur additional secured debt, and the Unsecured Notes can be subordinated accordingly.

42. Provisions similar to the Credit Facility Basket provision are common in a high-yield indenture such as the 2012 Indenture. Other publicly-traded companies with similar high-yield indentures have recently engaged in transactions similar to the Transaction.

43. The Plaintiffs chose to purchase the Unsecured Notes, knowing that the 2012 Indenture did not preclude a transaction such as the Transaction. Both in private discussions with the Plaintiffs and in public statements, Lightstream has confirmed its ability to conduct a second lien transaction such as the Transaction. In seeking to participate in the Transaction on its terms, the Plaintiffs acknowledged the propriety of the Transaction.

44. In reply to paragraph 28 of the Statement of Claim, Lightstream did not attempt to prevent scrutiny of the Transaction by Unsecured Noteholders through the timing of its press release or otherwise. The Transaction is in Lightstream's best interest, and Lightstream had no interest in concealing it. The Transaction was initially scheduled to close June 30, 2015 but was delayed. Consistent with its regulatory obligations, Lightstream promptly announced the Transaction in a press release. Following the press release, Lightstream also discussed the Transaction with the Plaintiffs as well as with other holders of the Unsecured Notes. The Plaintiffs' conversation with Lightstream on July 3, 2015 confirms that neither the Calgary Stampede nor the American Fourth of July holiday prevented the Plaintiffs from learning about the Transaction or discussing it with Lightstream.

45. In reply to paragraph 30 of the Statement of Claim, in purchasing the Unsecured Notes, the Plaintiffs had no reasonable expectation that Lightstream had an obligation to maintain the price of the Unsecured Notes in a secondary market. As evidenced by the Offering Memorandum, there was no assurance under the 2012 Indenture that any

market would develop for trading in the Unsecured Notes, and any trading price that did develop for the Unsecured Notes could be volatile.

46. The Transaction was not oppressive or unfairly prejudicial, nor did it unfairly disregard the Plaintiffs' relevant interests. On the contrary, the Plaintiffs as holders of the Unsecured Notes have benefitted from the Transaction, as it benefits Lightstream.

No Breach of the Duty of Honest Contractual Performance or Good Faith

47. In reply to paragraph 48 of the Statement of Claim, Lightstream did not breach any relevant duty of good faith or honest contractual performance. Lightstream fully performed and continues to perform its obligations under the 2012 Indenture, and with regard to the Transaction, honestly and in good faith.

No Damages

48. In reply to paragraphs 39, 44 and 50(d) and to the whole of the Statement of Claim, the Plaintiffs have not suffered any damages caused by Lightstream. Lightstream has made, and continues to make, all payments of interest to the Plaintiffs pursuant to the terms of the 2012 Indenture and as accepted by the Plaintiffs when they purchased the Unsecured Notes.

No Basis for Injunctive Relief

49. In reply to paragraphs 42, 43 and 50(b) and (c) of the Statement of Claim, Lightstream denies that the Plaintiffs are entitled to any injunctive relief. The Transaction has already closed. The Transaction does not violate any of the Plaintiffs' rights or interests. The Plaintiffs have not suffered and will not suffer any irreparable harm arising from the Transaction and have purported to quantify their damages, which are denied, to the precise dollar amount of $4,524,375.00 (US). Injunctive relief would be a significant hardship for Lightstream, impractical, and would deprive Lightstream of the significant benefits it has achieved through the Transaction.

Remedy sought:

50. Lightstream asks that this action be dismissed with costs on a solicitor-and-own-client basis, or such other elevated basis as this Honourable Court deems just.

Clerk's Stamp:

CLERK OF THE COURT
FILED
OCT 16 2015
JUDICIAL CENTRE OF CALGARY

COURT FILE NUMBER	1501-08782
COURT	COURT OF QUEEN'S BENCH OF ALBERTA
JUDICIAL CENTRE	CALGARY
PLAINTIFF	MUDRICK CAPITAL MANAGEMENT, LP
DEFENDANT	LIGHTSTREAM RESOURCES LTD.
DOCUMENT	**STATEMENT OF DEFENCE**
ADDRESS FOR SERVICE AND CONTACT INFORMATION OF PARTY FILING THIS DOCUMENT	BLAKE, CASSELS & GRAYDON LLP 3500, 855 – 2nd Street S.W. Calgary, AB T2P 4J8 Attention: Michael Barrack/Richard D. Bell/Emily Bala Telephone: 416-863-5280/403-260-9656/416-863-2152 Email: michael.barrack@blakes.com richard.bell@blakes.com emily.bala@blakes.com File Ref.: 89691/5

STATEMENT OF FACTS RELIED ON

1. The Defendant, Lightstream Resources Ltd. ("**Lightstream**"), admits the facts set out in the following paragraphs of the Statement of Claim: 2 and 4.

2. Lightstream has no knowledge in respect of the facts contained in paragraphs 3, 5 and 11.

3. Except as expressly admitted herein, Lightstream denies all other allegations set out in the Statement of Claim and denies that the Plaintiffs are entitled to any relief.

The Unsecured Notes

4. On January 30, 2012, Lightstream closed a private placement offering of senior unsecured notes (the "**Unsecured Notes**") that bear interest at a rate of 8.625% per annum and mature February 1, 2020. The offering of the Unsecured Notes was in Lightstream's best interests, as it diversified Lightstream's capital and provided ongoing liquidity and the subsequent

opportunity to repurchase and cancel certain of its then-outstanding secured convertible debentures.

5. The Unsecured Notes are governed by an indenture dated January 30, 2012, as amended by a supplemental indenture (collectively, the "**2012 Indenture**"). The 2012 Indenture expressly permits the Transaction (as defined below).

6. Section 4.06(b) of the 2012 Indenture provides several options through which Lightstream may properly incur further indebtedness (the "**Permitted Debt Baskets**"). These Permitted Debt Baskets are enumerated in the subsections of s. 4.06(b).

7. One of the Permitted Debt Baskets under s. 4.06(b) is set out in s. 4.06(b)(i) (the "**Credit Facility Basket**"). The Credit Facility Basket expressly permits Lightstream to incur further indebtedness in the form of, among other things, notes, debentures, bonds or similar securities or instruments, up to a specified amount.

8. Section 4.06(d) of the 2012 Indenture confirms that where indebtedness falls within more than one of the Permitted Debt Baskets, it can be incurred in whole or in part under any one or more Permitted Debt Baskets and subsequently re-allocated in whole or in part at any time between or among any one or more Permitted Debt Baskets.

9. Section 4.08 of the 2012 Indenture specifies the circumstances under which indebtedness may be secured by a lien (the "**Permitted Liens**"). Indebtedness incurred under the Credit Facility Basket is specifically permitted to be secured by a lien under the first clause of the definition of "Permitted Liens".

10. Section 6.06 of the 2012 Indenture prevents holders of Unsecured Notes from commencing proceedings with respect to the 2012 Indenture, or regarding the Unsecured Notes, unless specific preconditions are met. These preconditions include that the Trustee or Canadian Trustee must first be requested to take action itself by holders of at least 25% in aggregate principal amount of the outstanding Unsecured Notes, and that the Trustee or Canadian Trustee must have failed to comply with that request after 60 days.

11. The offering memorandum for the Unsecured Notes (the "**Offering Memorandum**") identifies risk factors relevant to the Unsecured Notes. These risk factors arise out of the terms of the 2012 Indenture.

12. As confirmed in the Offering Memorandum's discussion of risk factors, the 2012 Indenture permits Lightstream to incur substantial additional debt, including secured debt, and provides that the Unsecured Notes will be effectively junior in right of payment to existing and future secured debt.

13. Other risk factors of the Unsecured Notes, which are described in the Offering Memorandum, include that there is no assurance of an active trading market for the Unsecured Notes, that holders may be required to bear the risk of their investment indefinitely, and that if an active trading market does develop, the market price for the Unsecured Notes may be volatile.

14. As permitted under the 2012 Indenture and confirmed in the Offering Memorandum, Lightstream may at any time and from time to time repurchase the Unsecured Notes, in the open market or otherwise. As publicly disclosed, in 2014, Lightstream bought back Unsecured Notes through two privately negotiated transactions.

The Transaction

15. On July 2, 2015, Lightstream announced that it had entered into a privately negotiated agreement (a) to repurchase certain Unsecured Notes from certain holders in exchange for the issuance by Lightstream of new secured notes (the "**Secured Notes**"), and (b) to issue additional Secured Notes to the same holders for $200 million (US) paid to Lightstream (the "**Transaction**"). The Secured Notes bear interest at a rate of 9.875% per annum and mature June 15, 2019.

16. Lightstream issued the Secured Notes under the Credit Facility Basket and granted liens for the benefit of the Secured Notes pursuant to the first clause under the definition of "Permitted Liens", as expressly permitted and contemplated under the terms of the 2012 Indenture.

17. The Transaction was in Lightstream's best interest. It benefitted Lightstream by, among other benefits, reducing its debt by approximately $90 million and increasing its credit availability by approximately $250 million.

18. The Transaction closed in two tranches on July 2 and July 14, 2015.

The Plaintiffs' Demand to Join the Transaction

19. On July 6, 2015, following the announcement of the Transaction, the Plaintiff spoke with Lightstream. The Plaintiff demanded to be included in the Transaction on its terms. Pursuant

to its rights under the 2012 Indenture and having regard to the best interests of the corporation, Lightstream declined this request.

20. On July 8, the Plaintiff again demanded to be involved in the Transaction on its terms, and threatened to take legal action otherwise. Lightstream again declined.

21. On July 9, 2015, the Plaintiff then wrote to Lightstream, purporting to raise various legal objections to the Transaction.

22. On July 17, 2015, Lightstream responded to the Plaintiff's letter, explaining that the Plaintiff's purported concerns were without foundation and that the Transaction was compliant with the 2012 Indenture and all applicable law.

23. Prior to commencing this action, the Plaintiff failed to follow the procedure required under Section 6.06 of the 2012 Indenture for raising its purported concern to the Trustee or Canadian Trustee.

ANY MATTERS THAT DEFEAT THE CLAIM OF THE PLAINTIFF

No Oppression and No Breach of the 2012 Indenture

24. Lightstream denies that its actions, with respect to the Transaction or at all, were oppressive within the meaning of the *Business Corporations Act*, Alberta, RSA 2000, c B-9.

25. Lightstream has not contravened any reasonable expectation or right of the Plaintiff, either through the Transaction – which was in Lightstream's best interests – or at all.

26. The Plaintiff had no reasonable expectation that it would be included in, given advance notice of, or consulted on the Transaction. At no time did Lightstream represent to the Plaintiff that it would be invited to participate in or be given advance notice of the Transaction.

27. The Plaintiff is a sophisticated market participant with experience in negotiating the terms of high-yield indentures and in assessing and valuing securities. The primary sources of the Plaintiff's reasonable expectations in this case are the terms of the 2012 Indenture.

28. In reply to paragraphs 9, 13, 18, 21(b) and 21(d) of the Statement of Claim, Lightstream never represented to the Plaintiff or to the public that a transaction such as the Transaction

was not a possibility, nor did Lightstream rule out the possibility that it might acquire additional liquidity or restructure its debt.

29. In reply to paragraph 21(b) of the Statement of Claim, Lightstream entered into the Transaction because it considered the Transaction to be in the best interests of the corporation.

30. In reply to paragraph 21(c) of the Statement of Claim, the Transaction was compliant with the terms of the 2012 Indenture.

31. In reply to paragraph 7 and to the whole of the Statement of Claim, the 2012 Indenture expressly permits the Transaction, pursuant to the Credit Facility Basket provision and its associated Permitted Lien. Under the Credit Facility Basket provision, Lightstream is permitted to secure new indebtedness with a lien.

32. In reply to paragraphs 16, 17, 21(a) and 21(b)(i) of the Statement of Claim, there was no obligation on Lightstream to invite all holders of Unsecured Notes to participate in the Transaction, or to notify all holders that the Transaction was being considered.

33. As the Plaintiff is aware, and as confirmed in the Offering Memorandum, Lightstream may, at any time and from time to time, repurchase notes in the open market or otherwise. As publicly disclosed, Lightstream repurchased certain Unsecured Notes on a privately negotiated basis in 2014. Further, Lightstream has the ability under the 2012 Indenture to incur additional secured debt, and the Unsecured Notes can be subordinated accordingly.

34. Provisions similar to the Credit Facility Basket provision are common in a high-yield indenture such as the 2012 Indenture. Other publicly-traded companies with similar high-yield indentures have recently engaged in transactions similar to the Transaction.

35. Lightstream consistently stated publicly and in private investor meetings that it had the ability to complete a second lien offering or a transaction such as the Transaction. It is clear from the Plaintiff's communications with Lightstream that the Plaintiff was aware of this possibility.

36. In reply to paragraphs 7 and 22(a) of the Statement of Claim, in purchasing the Unsecured Notes, the Plaintiff had no reasonable expectation that Lightstream had an obligation to maintain the price of the Unsecured Notes in the secondary market. As evidenced by the Offering Memorandum, there was no assurance under the 2012 Indenture that any market

would develop for trading in the Unsecured Notes, and any trading price that did develop for the Unsecured Notes could be volatile.

37. The Transaction was not oppressive or unfairly prejudicial, nor did it unfairly disregard the Plaintiff's relevant interests. On the contrary, the Plaintiff as a holder of the Unsecured Notes has benefitted from the Transaction, as it benefits Lightstream.

No Damages

38. In reply to paragraph 23(b)(iv) and to the whole of the Statement of Claim, the Plaintiff has not suffered any damages caused by Lightstream. Lightstream has made, and continues to make, all payments of interest to the Plaintiff pursuant to the terms of the 2012 Indenture and as accepted by the Plaintiff when it purchased the Unsecured Notes.

REMEDY SOUGHT

39. Lightstream asks that this action be dismissed with costs on a solicitor-and-client basis, or such other elevated basis as this Honourable Court deems just.

TAB 2

CANADA

CONSOLIDATION

CODIFICATION

Companies' Creditors Arrangement Act

Loi sur les arrangements avec les créanciers des compagnies

R.S.C., 1985, c. C-36

L.R.C. (1985), ch. C-36

Current to September 18, 2016

Last amended on February 26, 2015

À jour au 18 septembre 2016

Dernière modification le 26 février 2015

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company means any company, corporation or legal person incorporated by or under an Act of Parliament or of the legislature of a province, any incorporated company having assets or doing business in Canada, wherever incorporated, and any income trust, but does not include banks, authorized foreign banks within the meaning of section 2 of the *Bank Act*, railway or telegraph companies, insurance companies and companies to which the *Trust and Loan Companies Act* applies; (*compagnie*)

court means

(a) in Nova Scotia, British Columbia and Prince Edward Island, the Supreme Court,

(a.1) in Ontario, the Superior Court of Justice,

(b) in Quebec, the Superior Court,

(c) in New Brunswick, Manitoba, Saskatchewan and Alberta, the Court of Queen's Bench,

(c.1) in Newfoundland and Labrador, the Trial Division of the Supreme Court, and

(d) in Yukon and the Northwest Territories, the Supreme Court, and in Nunavut, the Nunavut Court of Justice; (*tribunal*)

debtor company means any company that

(a) is bankrupt or insolvent,

(b) has committed an act of bankruptcy within the meaning of the *Bankruptcy and Insolvency Act* or is deemed insolvent within the meaning of the *Winding-up and Restructuring Act*, whether or not proceedings in respect of the company have been taken under either of those Acts,

(c) has made an authorized assignment or against which a bankruptcy order has been made under the *Bankruptcy and Insolvency Act*, or

(d) is in the course of being wound up under the *Winding-up and Restructuring Act* because the company is insolvent; (*compagnie débitrice*)

director means, in the case of a company other than an income trust, a person occupying the position of director by whatever name called and, in the case of an income trust, a person occupying the position of trustee by whatever named called; (*administrateur*)

eligible financial contract means an agreement of a prescribed kind; (*contrat financier admissible*)

compagnie Toute personne morale constituée par une loi fédérale ou provinciale ou sous son régime et toute personne morale qui possède un actif ou exerce des activités au Canada, quel que soit l'endroit où elle a été constituée, ainsi que toute fiducie de revenu. La présente définition exclut les banques, les banques étrangères autorisées, au sens de l'article 2 de la *Loi sur les banques*, les compagnies de chemin de fer ou de télégraphe, les compagnies d'assurances et les sociétés auxquelles s'applique la *Loi sur les sociétés de fiducie et de prêt*. (*company*)

compagnie débitrice Toute compagnie qui, selon le cas :

a) est en faillite ou est insolvable;

b) a commis un acte de faillite au sens de la *Loi sur la faillite et l'insolvabilité* ou est réputée insolvable au sens de la *Loi sur les liquidations et les restructurations*, que des procédures relatives à cette compagnie aient été intentées ou non sous le régime de l'une ou l'autre de ces lois;

c) a fait une cession autorisée ou à l'encontre de laquelle une ordonnance de faillite a été rendue en vertu de la *Loi sur la faillite et l'insolvabilité*;

d) est en voie de liquidation aux termes de la *Loi sur les liquidations et les restructurations* parce que la compagnie est insolvable. (*debtor company*)

contrat financier admissible Contrat d'une catégorie réglementaire. (*eligible financial contract*)

contrôleur S'agissant d'une compagnie, la personne nommée en application de l'article 11.7 pour agir à titre de contrôleur des affaires financières et autres de celle-ci. (*monitor*)

convention collective S'entend au sens donné à ce terme par les règles de droit applicables aux négociations collectives entre la compagnie débitrice et l'agent négociateur. (*collective agreement*)

créancier chirographaire Tout créancier d'une compagnie qui n'est pas un créancier garanti, qu'il réside ou soit domicilié au Canada ou à l'étranger. Un fiduciaire pour les détenteurs d'obligations non garanties, lesquelles sont émises en vertu d'un acte de fiducie ou autre acte fonctionnant en faveur du fiduciaire, est réputé un créancier chirographaire pour toutes les fins de la présente loi sauf la votation à une assemblée des créanciers relativement à ces obligations. (*unsecured creditor*)

R.S.C., 1985, c. C-36

An Act to facilitate compromises and arrangements between companies and their creditors

Short Title

Short title

1 This Act may be cited as the *Companies' Creditors Arrangement Act*.

R.S., c. C-25, s. 1.

Interpretation

Definitions

2 (1) In this Act,

aircraft objects [Repealed, 2012, c. 31, s. 419]

bargaining agent means any trade union that has entered into a collective agreement on behalf of the employees of a company; (*agent négociateur*)

bond includes a debenture, debenture stock or other evidences of indebtedness; (*obligation*)

cash-flow statement, in respect of a company, means the statement referred to in paragraph 10(2)(a) indicating the company's projected cash flow; (*état de l'évolution de l'encaisse*)

claim means any indebtedness, liability or obligation of any kind that would be a claim provable within the meaning of section 2 of the *Bankruptcy and Insolvency Act*; (*réclamation*)

collective agreement, in relation to a debtor company, means a collective agreement within the meaning of the jurisdiction governing collective bargaining between the debtor company and a bargaining agent; (*convention collective*)

L.R.C., 1985, ch. C-36

Loi facilitant les transactions et arrangements entre les compagnies et leurs créanciers

Titre abrégé

Titre abrégé

1 *Loi sur les arrangements avec les créanciers des compagnies.*

S.R., ch. C-25, art. 1.

Définitions et application

Définitions

2 (1) Les définitions qui suivent s'appliquent à la présente loi.

accord de transfert de titres pour obtention de crédit Accord aux termes duquel une compagnie débitrice transfère la propriété d'un bien en vue de garantir le paiement d'une somme ou l'exécution d'une obligation relativement à un contrat financier admissible. (*title transfer credit support agreement*)

actionnaire S'agissant d'une compagnie ou d'une fiducie de revenu assujetties à la présente loi, est assimilée à l'actionnaire la personne ayant un intérêt dans cette compagnie ou détenant des parts de cette fiducie. (*shareholder*)

administrateur S'agissant d'une compagnie autre qu'une fiducie de revenu, toute personne exerçant les fonctions d'administrateur, indépendamment de son titre, et, s'agissant d'une fiducie de revenu, toute personne exerçant les fonctions de fiduciaire, indépendamment de son titre. (*director*)

agent négociateur Syndicat ayant conclu une convention collective pour le compte des employés d'une compagnie. (*bargaining agent*)

biens aéronautiques [Abrogée, 2012, ch. 31, art. 419]

domiciled within or outside Canada, and a trustee for the holders of any unsecured bonds issued under a trust deed or other instrument running in favour of the trustee shall be deemed to be an unsecured creditor for all purposes of this Act except for the purpose of voting at a creditors' meeting in respect of any of those bonds. (*créancier chirographaire*)

a.1) dans la province d'Ontario, la Cour supérieure de justice;

b) dans la province de Québec, la Cour supérieure;

c) dans les provinces du Nouveau-Brunswick, du Manitoba, de la Saskatchewan et d'Alberta, la Cour du Banc de la Reine;

c.1) dans la province de Terre-Neuve-et-Labrador, la Section de première instance de la Cour suprême;

d) au Yukon et dans les Territoires du Nord-Ouest, la Cour suprême et, au Nunavut, la Cour de justice du Nunavut. (*court*)

valeurs nettes dues à la date de résiliation La somme nette obtenue après compensation des obligations mutuelles des parties à un contrat financier admissible effectuée conformément à ce contrat. (*net termination value*)

Meaning of *related* and *dealing at arm's length*

(2) For the purpose of this Act, section 4 of the *Bankruptcy and Insolvency Act* applies for the purpose of determining whether a person is related to or dealing at arm's length with a debtor company.

R.S., 1985, c. C-36, s. 2; R.S., 1985, c. 27 (2nd Supp.), s. 10; 1990, c. 17, s. 4; 1992, c. 27, s. 90; 1993, c. 34, s. 52; 1996, c. 6, s. 167; 1997, c. 12, s. 120(E); 1998, c. 30, s. 14; 1999, c. 3, s. 22, c. 28, s. 154; 2001, c. 9, s. 575; 2002, c. 7, s. 133; 2004, c. 25, s. 193; 2005, c. 3, s. 15, c. 47, s. 124; 2007, c. 29, s. 104, c. 36, ss. 61, 105; 2012, c. 31, s. 419; 2015, c. 3, s. 37.

Définition de *personnes liées*

(2) Pour l'application de la présente loi, l'article 4 de la *Loi sur la faillite et l'insolvabilité* s'applique pour établir si une personne est liée à une compagnie débitrice ou agit sans lien de dépendance avec une telle compagnie.

L.R. (1985), ch. C-36, art. 2; L.R. (1985), ch. 27 (2e suppl.), art. 10; 1990, ch. 17, art. 4; 1992, ch. 27, art. 90; 1993, ch. 34, art. 52; 1996, ch. 6, art. 167; 1997, ch. 12, art. 120(A); 1998, ch. 30, art. 14; 1999, ch. 3, art. 22, ch. 28, art. 154; 2001, ch. 9, art. 575; 2002, ch. 7, art. 133; 2004, ch. 25, art. 193; 2005, ch. 3, art. 15, ch. 47, art. 124; 2007, ch. 29, art. 104, ch. 36, art. 61 et 105; 2012, ch. 31, art. 419; 2015, ch. 3, art. 37.

Application

3 (1) This Act applies in respect of a debtor company or affiliated debtor companies if the total of claims against the debtor company or affiliated debtor companies, determined in accordance with section 20, is more than $5,000,000 or any other amount that is prescribed.

Application

3 (1) La présente loi ne s'applique à une compagnie débitrice ou aux compagnies débitrices qui appartiennent au même groupe qu'elle que si le montant des réclamations contre elle ou les compagnies appartenant au même groupe, établi conformément à l'article 20, est supérieur à cinq millions de dollars ou à toute autre somme prévue par les règlements.

Affiliated companies

(2) For the purposes of this Act,

(a) companies are affiliated companies if one of them is the subsidiary of the other or both are subsidiaries of the same company or each of them is controlled by the same person; and

(b) two companies affiliated with the same company at the same time are deemed to be affiliated with each other.

Application

(2) Pour l'application de la présente loi :

a) appartiennent au même groupe deux compagnies dont l'une est la filiale de l'autre ou qui sont sous le contrôle de la même personne;

b) sont réputées appartenir au même groupe deux compagnies dont chacune appartient au groupe d'une même compagnie.

Company controlled

(3) For the purposes of this Act, a company is controlled by a person or by two or more companies if

Application

(3) Pour l'application de la présente loi, ont le contrôle d'une compagnie la personne ou les compagnies :

(a) securities of the company to which are attached more than fifty per cent of the votes that may be cast to elect directors of the company are held, other than by way of security only, by or for the benefit of that person or by or for the benefit of those companies; and

(b) the votes attached to those securities are sufficient, if exercised, to elect a majority of the directors of the company.

Subsidiary

(4) For the purposes of this Act, a company is a subsidiary of another company if

(a) it is controlled by

(i) that other company,

(ii) that other company and one or more companies each of which is controlled by that other company, or

(iii) two or more companies each of which is controlled by that other company; or

(b) it is a subsidiary of a company that is a subsidiary of that other company.

R.S., 1985, c. C-36, s. 3; 1997, c. 12, s. 121; 2005, c. 47, s. 125.

a) qui détiennent — ou en sont bénéficiaires — , autrement qu'à titre de garantie seulement, des valeurs mobilières conférant plus de cinquante pour cent du maximum possible des voix à l'élection des administrateurs de la compagnie;

b) dont lesdites valeurs mobilières confèrent un droit de vote dont l'exercice permet d'élire la majorité des administrateurs de la compagnie.

Application

(4) Pour l'application de la présente loi, une compagnie est la filiale d'une autre compagnie dans chacun des cas suivants :

a) elle est contrôlée :

(i) soit par l'autre compagnie,

(ii) soit par l'autre compagnie et une ou plusieurs compagnies elles-mêmes contrôlées par cette autre compagnie,

(iii) soit par des compagnies elles-mêmes contrôlées par l'autre compagnie;

b) elle est la filiale d'une filiale de l'autre compagnie.

L.R. (1985), ch. C-36, art. 3; 1997, ch. 12, art. 121; 2005, ch. 47, art. 125.

PART I

Compromises and Arrangements

Compromise with unsecured creditors

4 Where a compromise or an 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, of 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 the shareholders of the company, to be summoned in such manner as the court directs.

R.S., c. C-25, s. 4.

Compromise with secured creditors

5 Where a compromise or an arrangement is proposed between a debtor company and its secured creditors or any class of them, the court may, on the application in a summary way of the company or of 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,

PARTIE I

Transactions et arrangements

Transaction avec les créanciers chirographaires

4 Lorsqu'une transaction ou un arrangement est proposé entre une compagnie débitrice et ses créanciers chirographaires ou toute catégorie de ces derniers, le tribunal peut, à la requête sommaire de la compagnie, d'un de ces créanciers ou du syndic en matière de faillite ou liquidateur de la compagnie, ordonner que soit convoquée, de la manière qu'il prescrit, une assemblée de ces créanciers ou catégorie de créanciers, et, si le tribunal en décide ainsi, des actionnaires de la compagnie.

S.R., ch. C-25, art. 4.

Transaction avec les créanciers garantis

5 Lorsqu'une transaction ou un arrangement est proposé entre une compagnie débitrice et ses créanciers garantis ou toute catégorie de ces derniers, le tribunal peut, à la requête sommaire de la compagnie, d'un de ces créanciers ou du syndic en matière de faillite ou liquidateur de la compagnie, ordonner que soit convoquée, de la

available to any person specified in the order on any terms or conditions that the court considers appropriate.

R.S., 1985, c. C-36, s. 10; 2005, c. 47, s. 127.

peut être communiqué, aux conditions qu'il estime indiquées, à la personne qu'il nomme.

L.R. (1985), ch. C-36, art. 10; 2005, ch. 47, art. 127.

General power of court

11 Despite anything in the *Bankruptcy and Insolvency Act* or the *Winding-up and Restructuring Act*, if an application is made under this Act in respect of a debtor company, the court, on the application of any person interested in the matter, may, subject to the restrictions set out in this Act, on notice to any other person or without notice as it may see fit, make any order that it considers appropriate in the circumstances.

R.S., 1985, c. C-36, s. 11; 1992, c. 27, s. 90; 1996, c. 6, s. 167; 1997, c. 12, s. 124; 2005, c. 47, s. 128.

Pouvoir général du tribunal

11 Malgré toute disposition de la *Loi sur la faillite et l'insolvabilité* ou de la *Loi sur les liquidations et les restructurations*, le tribunal peut, dans le cas de toute demande sous le régime de la présente loi à l'égard d'une compagnie débitrice, rendre, sur demande d'un intéressé, mais sous réserve des restrictions prévues par la présente loi et avec ou sans avis, toute ordonnance qu'il estime indiquée.

L.R. (1985), ch. C-36, art. 11; 1992, ch. 27, art. 90; 1996, ch. 6, art. 167; 1997, ch. 12, art. 124; 2005, ch. 47, art. 128.

Rights of suppliers

11.01 No order made under section 11 or 11.02 has the effect of

(a) prohibiting a person from requiring immediate payment for goods, services, use of leased or licensed property or other valuable consideration provided after the order is made; or

(b) requiring the further advance of money or credit.

2005, c. 47, s. 128.

Droits des fournisseurs

11.01 L'ordonnance prévue aux articles 11 ou 11.02 ne peut avoir pour effet :

a) d'empêcher une personne d'exiger que soient effectués sans délai les paiements relatifs à la fourniture de marchandises ou de services, à l'utilisation de biens loués ou faisant l'objet d'une licence ou à la fourniture de toute autre contrepartie de valeur qui ont lieu après l'ordonnance;

b) d'exiger le versement de nouvelles avances de fonds ou de nouveaux crédits.

2005, ch. 47, art. 128.

Stays, etc. — initial application

11.02 (1) A court may, on an initial application in respect of a debtor company, make an order on any terms that it may impose, effective for the period that the court considers necessary, which period may not be more than 30 days,

(a) staying, until otherwise ordered by the court, all proceedings taken or that might be taken in respect of the company under the *Bankruptcy and Insolvency Act* or the *Winding-up and Restructuring Act*;

(b) restraining, until otherwise ordered by the court, further proceedings in any action, suit or proceeding against the company; and

(c) prohibiting, until otherwise ordered by the court, the commencement of any action, suit or proceeding against the company.

Suspension : demande initiale

11.02 (1) Dans le cas d'une demande initiale visant une compagnie débitrice, le tribunal peut, par ordonnance, aux conditions qu'il peut imposer et pour la période maximale de trente jours qu'il estime nécessaire :

a) suspendre, jusqu'à nouvel ordre, toute procédure qui est ou pourrait être intentée contre la compagnie sous le régime de la *Loi sur la faillite et l'insolvabilité* ou de la *Loi sur les liquidations et les restructurations*;

b) surseoir, jusqu'à nouvel ordre, à la continuation de toute action, poursuite ou autre procédure contre la compagnie;

c) interdire, jusqu'à nouvel ordre, l'introduction de toute action, poursuite ou autre procédure contre la compagnie.

Stays, etc. — other than initial application

(2) A court may, on an application in respect of a debtor company other than an initial application, make an order, on any terms that it may impose,

Suspension : demandes autres qu'initiales

(2) Dans le cas d'une demande, autre qu'une demande initiale, visant une compagnie débitrice, le tribunal peut, par ordonnance, aux conditions qu'il peut imposer et pour la période qu'il estime nécessaire :

company or is acting or is likely to act inappropriately as a director in the circumstances.

Filling vacancy

(2) The court may, by order, fill any vacancy created under subsection (1).

1997, c. 12, s. 124; 2005, c. 47, s. 128.

Security or charge relating to director's indemnification

11.51 (1) On application by a debtor company and on notice to the secured creditors who are likely to be affected by the security or charge, the court may make an order declaring that all or part of the property of the company is subject to a security or charge — in an amount that the court considers appropriate — in favour of any director or officer of the company to indemnify the director or officer against obligations and liabilities that they may incur as a director or officer of the company after the commencement of proceedings under this Act.

Priority

(2) The court may order that the security or charge rank in priority over the claim of any secured creditor of the company.

Restriction — indemnification insurance

(3) The court may not make the order if in its opinion the company could obtain adequate indemnification insurance for the director or officer at a reasonable cost.

Negligence, misconduct or fault

(4) The court shall make an order declaring that the security or charge does not apply in respect of a specific obligation or liability incurred by a director or officer if in its opinion the obligation or liability was incurred as a result of the director's or officer's gross negligence or wilful misconduct or, in Quebec, the director's or officer's gross or intentional fault.

2005, c. 47, s. 128; 2007, c. 36, s. 66.

Court may order security or charge to cover certain costs

11.52 (1) On notice to the secured creditors who are likely to be affected by the security or charge, the court may make an order declaring that all or part of the property of a debtor company is subject to a security or charge — in an amount that the court considers appropriate — in respect of the fees and expenses of

(a) the monitor, including the fees and expenses of any financial, legal or other experts engaged by the monitor in the performance of the monitor's duties;

agit ou agira vraisemblablement de façon inacceptable dans les circonstances.

Vacance

(2) Le tribunal peut, par ordonnance, combler toute vacance découlant de la révocation.

1997, ch. 12, art. 124; 2005, ch. 47, art. 128.

Biens grevés d'une charge ou sûreté en faveur d'administrateurs ou de dirigeants

11.51 (1) Sur demande de la compagnie débitrice, le tribunal peut par ordonnance, sur préavis de la demande aux créanciers garantis qui seront vraisemblablement touchés par la charge ou sûreté, déclarer que tout ou partie des biens de celle-ci sont grevés d'une charge ou sûreté, d'un montant qu'il estime indiqué, en faveur d'un ou de plusieurs administrateurs ou dirigeants pour l'exécution des obligations qu'ils peuvent contracter en cette qualité après l'introduction d'une procédure sous le régime de la présente loi.

Priorité

(2) Il peut préciser, dans l'ordonnance, que la charge ou sûreté a priorité sur toute réclamation des créanciers garantis de la compagnie.

Restriction — assurance

(3) Il ne peut toutefois rendre une telle ordonnance s'il estime que la compagnie peut souscrire, à un coût qu'il estime juste, une assurance permettant d'indemniser adéquatement les administrateurs ou dirigeants.

Négligence, inconduite ou faute

(4) Il déclare, dans l'ordonnance, que la charge ou sûreté ne vise pas les obligations que l'administrateur ou le dirigeant assume, selon lui, par suite de sa négligence grave ou de son inconduite délibérée ou, au Québec, par sa faute lourde ou intentionnelle.

2005, ch. 47, art. 128; 2007, ch. 36, art. 66.

Biens grevés d'une charge ou sûreté pour couvrir certains frais

11.52 (1) Le tribunal peut par ordonnance, sur préavis aux créanciers garantis qui seront vraisemblablement touchés par la charge ou sûreté, déclarer que tout ou partie des biens de la compagnie débitrice sont grevés d'une charge ou sûreté, d'un montant qu'il estime indiqué, pour couvrir :

a) les débours et honoraires du contrôleur, ainsi que ceux des experts — notamment en finance et en droit

(b) any financial, legal or other experts engaged by the company for the purpose of proceedings under this Act; and

(c) any financial, legal or other experts engaged by any other interested person if the court is satisfied that the security or charge is necessary for their effective participation in proceedings under this Act.

— dont il retient les services dans le cadre de ses fonctions;

b) ceux des experts dont la compagnie retient les services dans le cadre de procédures intentées sous le régime de la présente loi;

c) ceux des experts dont tout autre intéressé retient les services, si, à son avis, la charge ou sûreté était nécessaire pour assurer sa participation efficace aux procédures intentées sous le régime de la présente loi.

Priority

(2) The court may order that the security or charge rank in priority over the claim of any secured creditor of the company.

2005, c. 47, s. 128; 2007, c. 36, s. 66.

Priorité

(2) Il peut préciser, dans l'ordonnance, que la charge ou sûreté a priorité sur toute réclamation des créanciers garantis de la compagnie.

2005, ch. 47, art. 128; 2007, ch. 36, art. 66.

***Bankruptcy and Insolvency Act* matters**

11.6 Notwithstanding the *Bankruptcy and Insolvency Act*,

(a) proceedings commenced under Part III of the *Bankruptcy and Insolvency Act* may be taken up and continued under this Act only if a proposal within the meaning of the *Bankruptcy and Insolvency Act* has not been filed under that Part; and

(b) an application under this Act by a bankrupt may only be made with the consent of inspectors referred to in section 116 of the *Bankruptcy and Insolvency Act* but no application may be made under this Act by a bankrupt whose bankruptcy has resulted from

(i) the operation of subsection 50.4(8) of the *Bankruptcy and Insolvency Act*, or

(ii) the refusal or deemed refusal by the creditors or the court, or the annulment, of a proposal under the *Bankruptcy and Insolvency Act*.

1997, c. 12, s. 124.

Lien avec la *Loi sur la faillite et l'insolvabilité*

11.6 Par dérogation à la *Loi sur la faillite et l'insolvabilité* :

a) les procédures intentées sous le régime de la partie III de cette loi ne peuvent être traitées et continuées sous le régime de la présente loi que si une proposition au sens de la *Loi sur la faillite et l'insolvabilité* n'a pas été déposée au titre de cette même partie;

b) le failli ne peut faire une demande au titre de la présente loi qu'avec l'aval des inspecteurs visés à l'article 116 de la *Loi sur la faillite et l'insolvabilité*, aucune demande ne pouvant toutefois être faite si la faillite découle, selon le cas :

(i) de l'application du paragraphe 50.4(8) de la *Loi sur la faillite et l'insolvabilité*,

(ii) du rejet — effectif ou présumé — de sa proposition par les créanciers ou le tribunal ou de l'annulation de celle-ci au titre de cette loi.

1997, ch. 12, art. 124.

Court to appoint monitor

11.7 (1) When an order is made on the initial application in respect of a debtor company, the court shall at the same time appoint a person to monitor the business and financial affairs of the company. The person so appointed must be a trustee, within the meaning of subsection 2(1) of the *Bankruptcy and Insolvency Act*.

Restrictions on who may be monitor

(2) Except with the permission of the court and on any conditions that the court may impose, no trustee may be appointed as monitor in relation to a company

Nomination du contrôleur

11.7 (1) Le tribunal qui rend une ordonnance sur la demande initiale nomme une personne pour agir à titre de contrôleur des affaires financières ou autres de la compagnie débitrice visée par la demande. Seul un syndic au sens du paragraphe 2(1) de la *Loi sur la faillite et l'insolvabilité* peut être nommé pour agir à titre de contrôleur.

Personnes qui ne peuvent agir à titre de contrôleur

(2) Sauf avec l'autorisation du tribunal et aux conditions qu'il peut fixer, ne peut être nommé pour agir à titre de contrôleur le syndic :

TAB 3

CANADA

CONSOLIDATION

CODIFICATION

Bankruptcy and Insolvency Act

Loi sur la faillite et l'insolvabilité

R.S.C., 1985, c. B-3

L.R.C. (1985), ch. B-3

Current to September 18, 2016

Last amended on February 26, 2015

À jour au 18 septembre 2016

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income trust means a trust that has assets in Canada if

(a) its units are listed on a prescribed stock exchange on the date of the initial bankruptcy event, or

(b) the majority of its units are held by a trust whose units are listed on a prescribed stock exchange on the date of the initial bankruptcy event; (*fiducie de revenu*)

insolvent person means a person who is not bankrupt and who resides, carries on business or has property in Canada, whose liabilities to creditors provable as claims under this Act amount to one thousand dollars, and

(a) who is for any reason unable to meet his obligations as they generally become due,

(b) who has ceased paying his current obligations in the ordinary course of business as they generally become due, or

(c) the aggregate of whose property is not, at a fair valuation, sufficient, or, if disposed of at a fairly conducted sale under legal process, would not be sufficient to enable payment of all his obligations, due and accruing due; (*personne insolvable*)

legal counsel means any person qualified, in accordance with the laws of a province, to give legal advice; (*conseiller juridique*)

locality of a debtor means the principal place

(a) where the debtor has carried on business during the year immediately preceding the date of the initial bankruptcy event,

(b) where the debtor has resided during the year immediately preceding the date of the initial bankruptcy event, or

(c) in cases not coming within paragraph (a) or (b), where the greater portion of the property of the debtor is situated; (*localité*)

Minister means the Minister of Industry; (*ministre*)

net termination value means the net amount obtained after netting or setting off or compensating the mutual obligations between the parties to an eligible financial contract in accordance with its provisions; (*valeurs nettes dues à la date de résiliation*)

official receiver means an officer appointed under subsection 12(2); (*séquestre officiel*)

b) il a résidé au cours de l'année précédant l'ouverture de sa faillite;

c) se trouve la plus grande partie de ses biens, dans les cas non visés aux alinéas a) ou b). (*locality of a debtor*)

localité d'un débiteur [Abrogée, 2005, ch. 47, art. 2(F)]

ministre Le ministre de l'Industrie. (*Minister*)

moment de la faillite S'agissant d'une personne, le moment :

a) soit du prononcé de l'ordonnance de faillite la visant;

b) soit du dépôt d'une cession de biens la visant;

c) soit du fait sur la base duquel elle est réputée avoir fait une cession de biens. (*time of the bankruptcy*)

opération sous-évaluée Toute disposition de biens ou fourniture de services pour laquelle le débiteur ne reçoit aucune contrepartie ou en reçoit une qui est manifestement inférieure à la juste valeur marchande de celle qu'il a lui-même donnée. (*transfer at undervalue*)

ouverture de la faillite Relativement à une personne, le premier en date des événements suivants à survenir :

a) le dépôt d'une cession de biens la visant;

b) le dépôt d'une proposition la visant;

c) le dépôt d'un avis d'intention par elle;

d) le dépôt de la première requête en faillite :

(i) dans les cas visés aux alinéas 50.4(8) a) et 57 a) et au paragraphe 61(2),

(ii) dans le cas où la personne, alors qu'elle est visée par un avis d'intention déposé aux termes de l'article 50.4 ou une proposition déposée aux termes de l'article 62, fait une cession avant que le tribunal ait approuvé la proposition;

e) dans les cas non visés à l'alinéa d), le dépôt de la requête à l'égard de laquelle une ordonnance de faillite est rendue;

f) l'introduction d'une procédure sous le régime de la *Loi sur les arrangements avec les créanciers des compagnies*. (*date of the initial bankruptcy event*)

personne

TAB 4

2004 CarswellOnt 1211
Ontario Superior Court of Justice [Commercial List]

Stelco Inc., Re

2004 CarswellOnt 1211, [2004] O.J. No. 1257, [2004] O.T.C. 284, 129 A.C.W.S. (3d) 1065, 48 C.B.R. (4th) 299

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

IN THE MATTER OF A PROPOSED PLAN OF COMPROMISE OR ARRANGEMENT WITH RESPECT TO STELCO INC. AND THE OTHER APPLICANTS LISTED IN SCHEDULE "A"

APPLICATION UNDER THE COMPANIES' CREDITORS ARRANGEMENT ACT, R.S.C. 1985, c. C-36, AS AMENDED

Farley J.

Heard: March 5, 2004
Judgment: March 22, 2004
Docket: 04-CL-5306

Counsel: Michael E. Barrack, James D. Gage, Geoff R. Hall for Applicants
David Jacobs, Michael McCreary for Locals, 1005, 5328, 8782 of the United Steel Workers of America
Ken Rosenberg, Lily Harmer, Rob Centa for United Steelworkers of America
Bob Thornton, Kyla Mahar for Ernst & Young Inc., Monitor of the Applicants
Kevin J. Zych for Informal Committee of Stelco Bondholders
David R. Byers for CIT
Kevin McElcheran for GE
Murray Gold, Andrew Hatnay for Retired Salaried Beneficiaries
Lewis Gottheil for CAW Canada and its Local 523
Virginie Gauthier for Fleet
H. Whiteley for CIBC
Gail Rubenstein for FSCO
Kenneth D. Kraft for EDS Canada Inc.

Subject: Insolvency

MOTION by union that steel company was not "debtor company" as defined in *Companies' Creditors Arrangement Act*.

***Farley J.*:**

1 As argued this motion by Locals 1005, 5328 and 8782 United Steel Workers of America (collectively "Union") to rescind the initial order and dismiss the application of Stelco Inc. ("Stelco") and various of its subsidiaries (collectively "Sub Applicants") for access to the protection and process of the *Companies' Creditors Arrangement Act* ("CCAA") was that this access should be denied on the basis that Stelco was not a "debtor company" as defined in s. 2 of the CCAA because it was not insolvent.

2 Allow me to observe that there was a great deal of debate in the materials and submissions as to the reason(s) that Stelco found itself in with respect to what Michael Locker (indicating he was "an expert in the area of corporate restructuring and a leading steel industry analyst") swore to at paragraph 12 of his affidavit was the "current crisis":

> 12. Contending with weak operating results and resulting tight cash flow, management has deliberately chosen not to fund its employee benefits. By contrast, Dofasco and certain other steel companies have consistently funded both their employee benefit obligations as well as debt service. If Stelco's management had chosen to fund pension obligations, presumably with borrowed money, *the current crisis* and related restructuring plans would focus on debt restructuring as opposed to the reduction of employee benefits and related liabilities. [Emphasis added.]

3 For the purpose of determining whether Stelco is insolvent and therefore could be considered to be a debtor company, it matters not what the cause or who caused the financial difficulty that Stelco is in as admitted by Locker on behalf of the Union. The management of a corporation could be completely incompetent, inadvertently or advertently; the corporation could be in the grip of ruthless, hard hearted and hard nosed outside financiers; the corporation could be the innocent victim of uncaring policy of a level of government; the employees (unionized or non-unionized) could be completely incompetent, inadvertently or advertently; the relationship of labour and management could be absolutely poisonous; the corporation could be the victim of unforeseen events affecting its viability such a as a fire destroying an essential area of its plant and equipment or of rampaging dumping. One or more or all of these factors (without being exhaustive), whether or not of varying degree and whether or not in combination of some may well have been the cause of a corporation's difficulty. The point here is that Stelco's difficulty exists; the only question is whether Stelco is insolvent within the meaning of that in the "debtor company" definition of the CCAA. However, I would point out, as I did in closing, that no matter how this motion turns out, Stelco does have a problem which has to be addressed - addressed within the CCAA process if Stelco is insolvent or addressed outside that process if Stelco is determined not to be insolvent. The status quo will lead to ruination of Stelco (and its Sub Applicants) and as a result will very badly affect its stakeholder, including pensioners, employees (unionized and non-unionized), management, creditors, suppliers, customers, local and other governments and the local communities. In such situations, time is a precious commodity; it cannot be wasted; no matter how much some would like to take time outs, the clock cannot be stopped. The watchwords of the Commercial List are equally applicable in such circumstances. They are communication, cooperation and common sense. I appreciate that these cases frequently invoke emotions running high and wild; that is understandable on a human basis but it is the considered, rational approach which will solve the problem.

4 The time to determine whether a corporation is insolvent for the purpose of it being a "debtor company" and thus able to make an application to proceed under the CCAA is the date of filing, in this case January 29, 2004.

5 The Monitor did not file a report as to this question of insolvency as it properly advised that it wished to take a neutral role. I understand however, that it did provide some assistance in the preparation of Exhibit C to Hap Steven's affidavit.

6 If I determine in this motion that Stelco is not insolvent, then the initial order would be set aside. See *Montreal Trust Co. of Canada v. Timber Lodge Ltd.* (1992), 15 C.B.R. (3d) 14 (P.E.I. C.A.). The onus is on Stelco as I indicated in my January 29, 2004 endorsement.

7 S. 2 of the CCAA defines "debtor company" as:

> "debtor company" means any company that:
>
> (a) is bankrupt or insolvent;
>
> (b) has committed an act of bankruptcy within the meaning of *Bankruptcy and Insolvency Act* ["BIA"] or deemed insolvent within the meaning of the *Winding-Up and Restructuring Act*, whether or not proceedings in respect of the company have been taken under either of those Acts;
>
> (c) has made an authorized assignment against which a receiving order has been made under the *Bankruptcy and Insolvency Act*; or

> (d) is in the course of being wound-up under the *Winding-Up and Restructuring Act* because the company is insolvent.

8 Counsel for the Existing Stelco Lenders and the DIP Lenders posited that Stelco would be able to qualify under (b) in light of the fact that as of January 29, 2004 whether or not it was entitled to receive the CCAA protection under (a) as being insolvent, it had ceased to pay its pre-filing debts. I would merely observe as I did at the time of the hearing that I do not find this argument attractive in the least. The most that could be said for that is that such game playing would be ill advised and in my view would not be rewarded by the exercise of judicial discretion to allow such an applicant the benefit of a CCAA stay and other advantages of the procedure for if it were capriciously done where there is not reasonable need, then such ought not to be granted. However, I would point out that if a corporation did capriciously do so, then one might well expect a creditor-initiated application so as to take control of the process (including likely the ouster of management including directors who authorized such unnecessary stoppage); in such a case, while the corporation would not likely be successful in a corporation application, it is likely that a creditor application would find favour of judicial discretion.

9 This judicial discretion would be exercised in the same way generally as is the case where s. 43(7) of the BIA comes into play whereby a bankruptcy receiving order which otherwise meets the test may be refused. See *Kenwood Hills Development Inc., Re* (1995), 30 C.B.R. (3d) 44 (Ont. Bktcy.) where at p. 45 I observed:

> The discretion must be exercised judicially based on credible evidence; it should be used according to common sense and justice and in a manner which does not result in an injustice: See *Re Churchill Forest Industries (Manitoba) Ltd.* (1971), 16 C.B.R. (NS) 158 (Man. Q.B.).

10 Anderson J. in *MTM Electric Co., Re* (1982), 42 C.B.R. (N.S.) 29 (Ont. Bktcy.) at p. 30 declined to grant a bankruptcy receiving order for the eminently good sense reason that it would be counterproductive: "Having regard for the value of the enterprise and having regard to the evidence before me, I think it far from clear that a receiving order would confer a benefit on anyone." This common sense approach to the judicial exercise of discretion may be contrasted by the rather more puzzling approach in *TDM Software Systems Inc., Re* (1986), 60 C.B.R. (N.S.) 92 (Ont. S.C.).

11 The Union, supported by the International United Steel Workers of America ("International"), indicated that if certain of the obligations of Stelco were taken into account in the determination of insolvency, then a very good number of large Canadian corporations would be able to make an application under the CCAA. I am of the view that this concern can be addressed as follows. The test of insolvency is to be determined on its own merits, not on the basis that an otherwise technically insolvent corporation should not be allowed to apply. However, if a technically insolvent corporation were to apply and there was no material advantage to the corporation and its stakeholders (in other words, a pressing need to restructure), then one would expect that the court's discretion would be judicially exercised against granting CCAA protection and ancillary relief. In the case of Stelco, it is recognized, as discussed above, that it is in crisis and in need of restructuring - which restructuring, if it is insolvent, would be best accomplished within a CCAA proceeding. Further, I am of the view that the track record of CCAA proceedings in this country demonstrates a healthy respect for the fundamental concerns of interested parties and stakeholders. I have consistently observed that much more can be achieved by negotiations outside the courtroom where there is a reasonable exchange of information, views and the exploration of possible solutions and negotiations held on a without prejudice basis than likely can be achieved by resorting to the legal combative atmosphere of the courtroom. A mutual problem requires a mutual solution. The basic interest of the CCAA is to rehabilitate insolvent corporations for the benefit of all stakeholders. To do this, the cause(s) of the insolvency must be fixed on a long term viable basis so that the corporation may be turned around. It is not achieved by positional bargaining in a tug of war between two parties, each trying for a larger slice of a defined size pie; it may be achieved by taking steps involving shorter term equitable sacrifices and implementing sensible approaches to improve productivity to ensure that the pie grows sufficiently for the long term to accommodate the reasonable needs of the parties.

12 It appears that it is a given that the Sub Applicants are in fact insolvent. The question then is whether Stelco is insolvent.

13 There was a question as to whether Stelco should be restricted to the material in its application as presented to the Court on January 29, 2004. I would observe that CCAA proceedings are not in the nature of the traditional adversarial lawsuit usually found in our courtrooms. It seems to me that it would be doing a disservice to the interest of the CCAA to artificially keep the Court in the dark on such a question. Presumably an otherwise deserving "debtor company" would not be allowed access to a continuing CCAA proceeding that it would be entitled to merely because some potential evidence were excluded for traditional adversarial technical reasons. I would point out that in such a case, there would be no prohibition against such a corporation reapplying (with the additional material) subsequently. In such a case, what would be the advantage for anyone of a "pause" before being able to proceed under the rehabilitative process under the CCAA. On a practical basis, I would note that all too often corporations will wait too long before applying, at least this was a significant problem in the early 1990s. In *Inducon Development Corp., Re* (1991), 8 C.B.R. (3d) 306 (Ont. Gen. Div.), I observed:

> Secondly, CCAA is designed to be remedial; it is not, however, designed to be preventative. CCAA should not be the *last* gasp of a dying company; it should be implemented, if it is to be implemented, at a stage prior to the death throe.

14 It seems to me that the phrase "death throe" could be reasonably replaced with "death spiral". In *Cumberland Trading Inc., Re* (1994), 23 C.B.R. (3d) 225 (Ont. Gen. Div. [Commercial List]), I went on to expand on this at p. 228:

> I would also observe that all too frequently debtors wait until virtually the last moment, the last moment, or in some cases, beyond the last moment before even beginning to think about reorganizational (and the attendant support that any successful reorganization requires from the creditors). I noted the lamentable tendency of debtors to deal with these situations as "last gasp" desperation moves in *Re Inducon Development Corp.* (1992), 8 C.B.R. (3d) 308 (Ont. Gen. Div.). To deal with matters on this basis minimizes the chances of success, even if "success" may have been available with earlier spade work.

15 I have not been able to find in the CCAA reported cases any instance where there has been an objection to a corporation availing itself of the facilities of the CCAA on the basis of whether the corporation was insolvent. Indeed, as indicated above, the major concern here has been that an applicant leaves it so late that the timetable of necessary steps may get impossibly compressed. That is not to say that there have not been objections by parties opposing the application on various other grounds. Prior to the 1992 amendments, there had to be debentures (plural) issued pursuant to a trust deed; I recall that in *Nova Metal Products Inc. v. Comiskey (Trustee of)* (1990), 1 C.B.R. (3d) 101, 1 O.R. (3d) 289 (Ont. C.A.), the initial application was rejected in the morning because there had only been one debenture issued but another one was issued prior to the return to court that afternoon. This case stands for the general proposition that the CCAA should be given a large and liberal interpretation. I should note that there was in *Enterprise Capital Management Inc. v. Semi-Tech Corp.* (1999), 10 C.B.R. (4th) 133 (Ont. S.C.J. [Commercial List]) a determination that in a creditor application, the corporation was found not to be insolvent, but see below as to BIA test (c) my views as to the correctness of this decision.

16 In *Lehndorff General Partner Ltd., Re* (1993), 17 C.B.R. (3d) 24 (Ont. Gen. Div. [Commercial List]) I observed at p. 32:

> One of the purposes of the CCAA is to facilitate ongoing operations of a business where its assets have a greater value as part of an integrated system than individually. The CCAA facilitates reorganization of a company where the alternative, sale of the property piecemeal, is likely to yield far less satisfaction to the creditors.

17 In *Anvil Range Mining Corp., Re* (2002), 34 C.B.R. (4th) 157 (Ont. C.A.), the court stated to the same effect:

> The second submission is that the plan is contrary to the purposes of the CCAA. Courts have recognized that the purpose of the CCAA is to enable compromises to be made for the common benefit of the creditors and the company and to keep the company alive and out of the hands of liquidators.

18 Encompassed in this is the concept of saving employment if a restructuring will result in a viable enterprise. See *Diemaster Tool Inc. v. Skvortsoff (Trustee of)* (1991), 3 C.B.R. (3d) 133 (Ont. Gen. Div.). This concept has been a continuing thread in CCAA cases in this jurisdiction stretching back for at least the past 15 years, if not before.

19 I would also note that the jurisprudence and practical application of the bankruptcy and insolvency regime in place in Canada has been constantly evolving. The early jails of what became Canada were populated to the extent of almost half their capacity by bankrupts. Rehabilitation and a fresh start for the honest but unfortunate debtor came afterwards. Most recently, the *Bankruptcy Act* was revised to the BIA in 1992 to better facilitate the rehabilitative aspect of making a proposal to creditors. At the same time, the CCAA was amended to eliminate the threshold criterion of there having to be debentures issued under a trust deed (this concept was embodied in the CCAA upon its enactment in 1933 with a view that it would only be large companies with public issues of debt securities which could apply). The size restriction was continued as there was now a threshold criterion of at least $5 million of claims against the applicant. While this restriction may appear discriminatory, it does have the practical advantage of taking into account that the costs (administrative costs including professional fees to the applicant, and indeed to the other parties who retain professionals) is a significant amount, even when viewed from the perspective of $5 million. These costs would be prohibitive in a smaller situation. Parliament was mindful of the time horizons involved in proposals under BIA where the maximum length of a proceeding including a stay is six months (including all possible extensions) whereas under CCAA, the length is in the discretion of the court judicially exercised in accordance with the facts and the circumstances of the case. Certainly sooner is better than later. However, it is fair to observe that virtually all CCAA cases which proceed go on for over six months and those with complexity frequently exceed a year.

20 Restructurings are not now limited in practical terms to corporations merely compromising their debts with their creditors in a balance sheet exercise. Rather there has been quite an emphasis recently on operational restructuring as well so that the emerging company will have the benefit of a long term viable fix, all for the benefit of stakeholders. See *Sklar-Peppler Furniture Corp. v. Bank of Nova Scotia* (1991), 8 C.B.R. (3d) 312 (Ont. Gen. Div.) at p. 314 where Borins J. states:

> The proposed plan exemplifies the policy and objectives of the Act as it proposes a regime for the court-supervised reorganization for the Applicant company intended to avoid the devastating social and economic effects of a creditor-initiated termination of its ongoing business operations and enabling the company to carry on its business in a manner in which it is intended to cause the least possible harm to the company, its creditors, its employees and former employees and the communities in which its carries on and carried on its business operations.

21 The CCAA does not define "insolvent" or "insolvency". Houlden & Morawetz, *The 2004 Annotated Bankruptcy and Insolvency Act* (Toronto, Carswell; 2003) at p. 1107 (N5) states:

> In interpreting "debtor company", reference must be had to the definition of "insolvent person" in s. 2(1) of the *Bankruptcy and Insolvency Act* . . .
>
> To be able to use the Act, a company must be bankrupt or insolvent: *Reference re Companies' Creditors Arrangement Act (Canada)*, 16 C.B.R. 1, [1934] S.C.R. 659, [1934] 4 D.L.R. 75. The company must, in its application, admit its insolvency.

22 It appears to have become fairly common practice for applicants and others when reference is made to insolvency in the context of the CCAA to refer to the definition of "insolvent person" in the BIA. That definition is as follows:

> s. 2(1) . . .

> "insolvent person" means a person who is not bankrupt and who resides, carries on business or has property in Canada, and whose liability to creditors provable as claims under this Act amount to one thousand dollars, and
>
> (a) who is for any reason unable to meet his obligations as they generally become due,
>
> (b) who has ceased paying his current obligations in the ordinary course of business as they generally become due, or
>
> (c) the aggregate of whose property is not, at a fair valuation, sufficient, or, if disposed of at a fairly conducted sale under legal process, would not be sufficient to enable payment of all his obligations, due and accruing due.

23 Stelco acknowledges that it does not meet the test of (b); however, it does assert that it meets the test of both (a) and (c). In addition, however, Stelco also indicates that since the CCAA does not have a reference over to the BIA in relation to the (a) definition of "debtor company" as being a company that is "(a) bankrupt or insolvent", then this term of "insolvent" should be given the meaning that the overall context of the CCAA requires. See the modern rule of statutory interpretation which directs the court to take a contextual and purposive approach to the language of the provision at issue as illustrated by *Bell ExpressVu Ltd. Partnership v. Rex*, [2002] 2 S.C.R. 559 (S.C.C.) at p. 580:

> Today there is only one principle or approach, namely the words of an Act are to be read in their entire context and in their grammatical and ordinary sense harmoniously with the scheme of the Act, the object of the Act, and the intention of Parliament.

24 I note in particular that the (b), (c) and (d) aspects of the definition of "debtor company" all refer to other statutes, including the BIA; (a) does not. S. 12 of the CCAA defines "claims" with reference over to the BIA (and otherwise refers to the BIA and the *Winding-Up and Restructuring Act*). It seems to me that there is merit in considering that the test for insolvency under the CCAA may differ somewhat from that under the BIA, so as to meet the special circumstances of the CCAA and those corporations which would apply under it. In that respect, I am mindful of the above discussion regarding the time that is usually and necessarily (in the circumstances) taken in a CCAA reorganization restructuring which is engaged in coming up with a plan of compromise and arrangement. The BIA definition would appear to have been historically focussed on the question of bankruptcy - and not reorganization of a corporation under a proposal since before 1992, secured creditors could not be forced to compromise their claims, so that in practice there were no reorganizations under the former *Bankruptcy Act* unless all secured creditors voluntarily agreed to have their secured claims compromised. The BIA definition then was essentially useful for being a pre-condition to the "end" situation of a bankruptcy petition or voluntary receiving order where the upshot would be a realization on the bankrupt's assets (not likely involving the business carried on - and certainly not by the bankrupt). Insolvency under the BIA is also important as to the Paulian action events (eg., fraudulent preferences, settlements) as to the conduct of the debtor *prior* to the bankruptcy; similarly as to the question of provincial preference legislation. Reorganization under a plan or proposal, on the contrary, is with a general objective of the applicant continuing to exist, albeit that the CCAA may also be used to have an orderly disposition of the assets and undertaking in whole or in part.

25 It seems to me that given the time and steps involved in a reorganization, and the condition of insolvency perforce requires an expanded meaning under the CCAA. Query whether the definition under the BIA is now sufficient in that light for the allowance of sufficient time to carry through with a realistically viable proposal within the maximum of six months allowed under the BIA? I think it sufficient to note that there would not be much sense in providing for a rehabilitation program of restructuring/reorganization under either statute if the entry test was that the applicant could not apply until a rather late stage of its financial difficulties with the rather automatic result that in situations of complexity of any material degree, the applicant would not have the financial resources sufficient to carry through to hopefully a successful end. This would indeed be contrary to the renewed emphasis of Parliament on "rescues" as exhibited by the 1992 and 1997 amendments to the CCAA and the BIA.

26 Allow me now to examine whether Stelco has been successful in meeting the onus of demonstrating with credible evidence on a common sense basis that it is insolvent within the meaning required by the CCAA in regard to the interpretation of "debtor company" in the context and within the purpose of that legislation. To a similar effect, see *PWA Corp. v. Gemini Group Automated Distribution Systems Inc.* (1993), 103 D.L.R. (4th) 609 (Ont. C.A.), leave to appeal to S.C.C. dismissed [(1993), 49 C.P.R. (3d) ix (S.C.C.)] wherein it was determined that the trial judge was correct in holding that a party was not insolvent and that the statutory definition of insolvency pursuant to the BIA definition was irrelevant to determine that issue, since the agreement in question effectively provided its own definition by implication. It seems to me that the CCAA test of insolvency advocated by Stelco and which I have determined is a proper interpretation is that the BIA definition of (a), (b) or (c) of insolvent person is acceptable with the caveat that as to (a), a financially troubled corporation is insolvent if it is reasonably expected to run out of liquidity within reasonable proximity of time as compared with the time reasonably required to implement a restructuring. That is, there should be a reasonable cushion, which cushion may be adjusted and indeed become in effect an encroachment depending upon reasonable access to DIP between financing. In the present case, Stelco accepts the view of the Union's affiant, Michael Mackey of Deloitte and Touche that it will otherwise run out of funding by November 2004.

27 On that basis, allow me to determine whether Stelco is insolvent on the basis of (i) what I would refer to as the CCAA test as described immediately above, (ii) BIA test (a) or (iii) BIA test (c). In doing so, I will have to take into account the fact that Stephen, albeit a very experienced and skilled person in the field of restructurings under the CCAA, unfortunately did not appreciate that the material which was given to him in Exhibit E to his affidavit was modified by the caveats in the source material that in effect indicated that based on appraisals, the fair value of the real assets acquired was in excess of the purchase price for two of the U.S. comparators. Therefore the evidence as to these comparators is significantly weakened. In addition at Q. 175-177 in his cross examination, Stephen acknowledged that it was reasonable to assume that a purchaser would "take over some liabilities, some pension liabilities and OPEB liabilities, for workers who remain with the plant." The extent of that assumption was not explored; however, I do note that there was acknowledgement on the part of the Union that such an assumption would also have a reciprocal negative effect on the purchase price.

28 The BIA tests are disjunctive so that anyone meeting any of these tests is determined to be insolvent: see *Optical Recording Laboratories Inc., Re* (1990), 75 D.L.R. (4th) 747 (Ont. C.A.) at p. 756; *Viteway Natural Foods Ltd., Re* (1986), 63 C.B.R. (N.S.) 157 (B.C. S.C.) at p. 161. Thus, if I determine that Stelco is insolvent on *any one* of these tests, then it would be a "debtor company" entitled to apply for protection under the CCAA.

29 In my view, the Union's position that Stelco is not insolvent under BIA (a) because it has not entirely used up its cash and cash facilities (including its credit line), that is, it is not yet as of January 29, 2004 run out of liquidity conflates inappropriately the (a) test with the (b) test. The Union's view would render the (a) test necessarily as being redundant. See *R. v. Proulx*, [2000] 1 S.C.R. 61 (S.C.C.) at p. 85 for the principle that no legislative provision ought to be interpreted in a manner which would "render it mere surplusage." Indeed the plain meaning of the phrase "unable to meet his obligations as they generally become due" requires a construction of test (a) which permits the court to take a purposive assessment of a debtor's ability to meet his future obligations. See *King Petroleum Ltd., Re* (1978), 29 C.B.R. (N.S.) 76 (Ont. S.C.) where Steele J. stated at p. 80:

> With respect to cl. (a), it was argued that at the time the disputed payments were made the company was able to meet its obligations as they generally became due because no major debts were in fact due at that time. This was premised on the fact that the moneys owed to Imperial Oil were not due until 10 days after the receipt of the statements and that the statements had not then been received. I am of the opinion that this is not a proper interpretation of cl. (a). *Clause (a) speaks in the present and future tenses and not in the past.* I am of the opinion that the company was an "insolvent person" within the meaning of cl. (a) because by the very payment-out of the money in question it placed itself in a position that it was unable to meet its obligations as they would generally become due. In other words, it had placed itself in a position that it would not be able to pay the obligations that it knew it had incurred and which it knew would become due in the immediate future. [Emphasis added.]

30 *King Petroleum Ltd.* was a case involving the question in a bankruptcy scenario of whether there was a fraudulent preference during a period when the corporation was insolvent. Under those circumstances, the "immediate future" does not have the same expansive meaning that one would attribute to a time period in a restructuring forward looking situation.

31 Stephen at paragraphs 40-49 addressed the restructuring question in general and its applicability to the Stelco situation. At paragraph 41, he outlined the significant stages as follows:

> The process of restructuring under the CCAA entails a number of different stages, the most significant of which are as follows:
>
> (a) identification of the debtor's stakeholders and their interests;
>
> (b) arranging for a process of meaningful communication;
>
> (c) dealing with immediate relationship issues arising from a CCAA filing;
>
> (d) sharing information about the issues giving rise to the debtor's need to restructure;
>
> (e) developing restructuring alternatives; and
>
> (f) building a consensus around a plan of restructuring.

32 I note that January 29, 2004 is just 9-10 months away from November 2004. I accept as correct his conclusion based on his experience (and this is in accord with my own objective experience in large and complicated CCAA proceedings) that Stelco would have the liquidity problem within the time horizon indicated. In that regard, I also think it fair to observe that Stelco realistically cannot expect any increase in its credit line with its lenders or access further outside funding. To bridge the gap it must rely upon the stay to give it the uplift as to prefiling liabilities (which the Union misinterpreted as a general turnaround in its cash position without taking into account this uplift). As well, the Union was of the view that recent price increases would relieve Stelco's liquidity problems; however, the answers to undertaking in this respect indicated:

> With respect to the Business Plan, the average spot market sales price per ton was $514, and the average contract business sales price per ton was $599. The Forecast reflects an average spot market sales price per ton of $575, and average contract business sales price per ton of $611. The average spot price used in the forecast considers further announced price increases, recognizing, among other things, the timing and the extent such increases are expected to become effective. The benefit of the increase in sales prices from the Business Plan is essentially offset by the substantial increase in production costs, and in particular in raw material costs, primarily scrap and coke, as well as higher working capital levels and a higher loan balance outstanding on the CIT credit facility as of January 2004.

I accept that this is generally a cancel out or wash in all material respects.

33 I note that $145 million of cash resources had been used from January 1, 2003 to the date of filing. Use of the credit facility of $350 million had increased from $241 million on November 30, 2003 to $293 million on the date of filing. There must be a reasonable reserve of liquidity to take into account day to day, week to week or month to month variances and also provide for unforeseen circumstances such as the breakdown of a piece of vital equipment which would significantly affect production until remedied. Trade credit had been contracting as a result of appreciation by suppliers of Stelco's financial difficulties. The DIP financing of $75 million is only available if Stelco is under CCAA protection. I also note that a shut down as a result of running out of liquidity would be complicated in the case of Stelco and that even if conditions turned around more than reasonably expected, start-up costs would be heavy and quite importantly, there would be a significant erosion of the customer base (reference should be had to the Slater Hamilton plant in this regard). One does not liquidate assets which one would not sell in the ordinary course of business to thereby artificially salvage

some liquidity for the purpose of the test: see *Pacific Mobile Corp., Re* (1979), 32 C.B.R. (N.S.) 209 (C.S. Que.) at p. 220. As a rough test, I note that Stelco (albeit on a consolidated basis with all subsidiaries) running significantly behind plan in 2003 from its budget of a profit of $80 million now to a projected loss of $192 million and cash has gone from a positive $209 million to a negative $114 million.

34 Locker made the observation at paragraph 8 of his affidavit that:

> 8. Stelco has performed poorly for the past few years primarily due to an inadequate business strategy, poor utilization of assets, inefficient operations and generally weak management leadership and decision-making. This point is best supported by the fact that Stelco's local competitor, Dofasco, has generated outstanding results in the same period.

Table 1 to his affidavit would demonstrate that Dofasco has had superior profitability and cashflow performance than its "neighbour" Stelco. He went on to observe at paragraphs 36-37:

> 36. Stelco can achieve significant cost reductions through means other than cutting wages, pensions and benefits for employees and retirees. Stelco could bring its cost levels down to those of restructured U.S. mills, with the potential for lowering them below those of many U.S. mills.
>
> 37. Stelco could achieve substantial savings through productivity improvements within the mechanisms of the current collective agreements. More importantly, a major portion of this cost reduction could be achieved through constructive negotiations with the USWA in an out-of-court restructuring that does not require intervention of the courts through the vehicle of CCAA protection.

I accept his constructive comments that there is room for cost reductions and that there are substantial savings to be achieved through productivity improvements. However, I do not see anything detrimental to these discussions and negotiations by having them conducted within the umbrella of a CCAA proceeding. See my comments above regarding the CCAA in practice.

35 But I would observe and I am mystified by Locker's observations at paragraph 12 (quoted above), that Stelco should have borrowed to fund pension obligations to avoid its current financial crisis. This presumes that the borrowed funds would not constitute an obligation to be paid back as to principal and interest, but rather that it would assume the character of a cost-free "gift".

36 I note that Mackey, without the "laundry list" he indicates at paragraph 17 of his second affidavit, is unable to determine at paragraph 19 (for himself) whether Stelco was insolvent. Mackey was unable to avail himself of all available information in light of the Union's refusal to enter into a confidentiality agreement. He does not closely adhere to the BIA tests as they are defined. In the face of positive evidence about an applicant's financial position by an experienced person with expertise, it is not sufficient to displace this evidence by filing evidence which goes no further than raising questions: see *Anvil Range Mining Corp., supra* at p. 162.

37 The Union referred me to one of my decisions *Standard Trustco Ltd. (Trustee of) v. Standard Trust Co.* (1993), 13 O.R. (3d) 7 (Ont. Gen. Div.) where I stated as to the MacGirr affidavit:

> The Trustee's cause of action is premised on MacGirr's opinion that STC was insolvent as at August 3, 1990 and therefore the STC common shares and promissory note received by Trustco in return for the Injection had no value at the time the Injection was made. Further, MacGirr ascribed no value to the opportunity which the Injection gave to Trustco to restore STC and salvage its thought to be existing $74 million investment. In stating his opinion MacGirr defined solvency as:
>
> (a) the ability to meet liabilities as they fall due; and
>
> (b) that assets exceed liabilities.

> On cross-examination MacGirr testified that in his opinion on either test STC was insolvent as at August 3, 1990 since as to (a) STC was experiencing then a negative cash flow and as to (b) the STC financial statements incorrectly reflected values. As far as (a) is concerned, I would comment that while I concur with MacGirr that at some time in the long run a company that is experiencing a negative cash flow will eventually not be able to meet liabilities as they fall due but that is not the test (which is a "present exercise"). On that current basis STC was meeting its liabilities on a timely basis.

38 As will be seen from that expanded quote, MacGirr gave his own definitions of insolvency which are not the same as the s. 2 BIA tests (a), (b) and (c) but only a very loose paraphrase of (a) and (c) and an omission of (b). Nor was I referred to the *King Petroleum Ltd.* or *Proulx* cases *supra*. Further, it is obvious from the context that "*sometime in the long run . . . eventually*" is not a finite time in the foreseeable future.

39 I have not given any benefit to the $313 - $363 million of improvements referred to in the affidavit of William Vaughan at paragraph 115 as those appear to be capital expenditures which will have to be accommodated within a plan of arrangement or after emergence.

40 It seems to me that if the BIA (a) test is restrictively dealt with (as per my question to Union counsel as to how far in the future should one look on a prospective basis being answered "24 hours") then Stelco would not be insolvent under that test. However, I am of the view that that would be unduly restrictive and a proper contextual and purposive interpretation to be given when it is being used for a restructuring purpose even under BIA would be to see whether there is a reasonably foreseeable (at the time of filing) expectation that there is a looming liquidity condition or crisis which will result in the applicant running out of "cash" to pay its debts as they generally become due in the future without the benefit of the say and ancillary protection and procedure by court authorization pursuant to an order. I think this is the more appropriate interpretation of BIA (a) test in the context of a reorganization or "rescue" as opposed to a threshold to bankruptcy consideration or a fraudulent preferences proceeding. On that basis, I would find Stelco insolvent from the date of filing. Even if one were not to give the latter interpretation to the BIA (a) test, clearly for the above reasons and analysis, if one looks at the meaning of "insolvent" within the context of a CCAA reorganization or rescue solely, then of necessity, the time horizon must be such that the liquidity crisis would occur in the sense of running out of "cash" but for the grant of the CCAA order. On that basis Stelco is certainly insolvent given its limited cash resources unused, its need for a cushion, its rate of cash burn recently experienced and anticipated.

41 What about the BIA (c) test which may be roughly referred to as an assets compared with obligations test. See *New Quebec Raglan Mines Ltd. v. Blok-Andersen*, [1993] O.J. No. 727 (Ont. Gen. Div. [Commercial List]) as to fair value and fair market valuation. The Union observed that there was no intention by Stelco to wind itself up or proceed with a sale of some or all of its assets and undertaking and therefore some of the liabilities which Stelco and Stephen took into account would not crystallize. However, as I discussed at the time of the hearing, the (c) test is what one might reasonably call or describe as an "artificial" or notional/hypothetical test. It presumes certain things which are in fact not necessarily contemplated to take place or to be involved. In that respect, I appreciate that it may be difficult to get one's mind around that concept and down the right avenue of that (c) test. See my views at trial in *Olympia & York Developments Ltd. (Trustee of) v. Olympia & York Realty Corp.*, [2001] O.J. No. 3394 (Ont. S.C.J. [Commercial List]) at paragraphs 13, 21 and 33; affirmed [2003] O.J. No. 5242 (Ont. C.A.). At paragraph 33, I observed in closing:

> 33 . . . They (and their expert witnesses) all had to contend with dealing with rambling and complicated facts and, in Section 100 BIA, a section which is difficult to administer when fmv [fair market value] in a notational or hypothetical market involves ignoring what would often be regarded as self evidence truths but at the same time appreciating that this notational or hypothetical market requires that the objects being sold have to have realistic true to life attributes recognized.

42 The Court of Appeal stated at paragraphs 24-25 as follows:

> 24. Nor are the appellants correct to argue that the trial judge also assumed an imprudent vendor in arriving at his conclusion about the fair market value of the OYSF note would have to know that in order to realize value from the note any purchaser would immediately put OYSF and thus OYDL itself into bankruptcy to pre-empt a subsequent triggering event in favour of EIB. While this was so, and the trial judge clearly understood it, the error in this submission is that it seeks to inject into the analysis factors subjected to the circumstances of OYDL as vendor and not intrinsic to the value of the OYSF note. The calculation of fair market value does not permit this but rather must assume an unconstrained vendor.
>
> 25. The Applicants further argue that the trial judge eroded in determining the fair market value of the OYSF note by reference to a transaction which was entirely speculative because it was never considered by OYDL nor would have it been since it would have resulted in OYDL's own bankruptcy. I disagree. The transaction hypothesized by the trial judge was one between a notational, willing, prudent and informed vendor and purchaser based on factors relevant to the OYSF note itself rather than the particular circumstances of OYDL as the seller of the note. This is an entirely appropriate way to determine the fair market value of the OYSF note.

43 Test (c) deems a person to be insolvent if "the aggregate of [its] property is not, at a fair valuation, sufficient, or of disposed at a fairly conducted sale under legal process would not be sufficient to enable payment of all [its] obligations, due and accruing due." The origins of this legislative test appear to be the decision of Spragge V-C in *Davidson v. Douglas* (1868), 15 Gr. 347 (Ont. Ch.) at p. 351 where he stated with respect to the solvency or insolvency of a debtor, the proper course is:

> to see and examine whether all his property, real and personal, be sufficient if presently realized for the payment of his debts, and in this view we must estimate his land, as well as his chattel property, not at what his neighbours or others may consider to be its value, but at what it would bring in the market at a forced sale, or a sale where the seller cannot await his opportunities, but must sell.

44 In *Clarkson v. Sterling* (1887), 14 O.R. 460 (Ont. C.P.) at p. 463, Rose J. indicted that the sale must be fair and reasonable, but that the determination of fairness and reasonableness would depend on the facts of each case.

45 The Union essentially relied on garnishment cases. Because of the provisions relating as to which debts may or may not be garnished, these authorities are of somewhat limited value when dealing with the test (c) question. However I would refer to one of the Union's cases *Bank of Montreal v. I.M. Krisp Foods Ltd.*, [1996] S.J. No. 655 (Sask. C.A.) where it is stated at paragraph 11:

> 11. Few phrases have been as problematic to define as "debt due or accruing due". The Shorter Oxford English Dictionary, 3rd ed. defines "accruing" as "arising in due course", but an examination of English and Canadian authority reveals that not all debts "arising in due course" are permitted to be garnisheed. (See Professor Dunlop's extensive research for his British Columbia Law Reform Commission's Report on Attachment of Debts Act, 1978 at 17 to 29 and is text Creditor-Debtor Law in Canada, 2nd ed. at 374 to 385.)

46 In *Barsi v. Farcas* (1923), [1924] 1 D.L.R. 1154 (Sask. C.A.), Lamont J.A. was cited for his statement at p. 522 of *Webb v. Stenton* (1883), 11 Q.B.D. 518 (Eng. C.A.) that: "an accruing debt, therefore, is a debt not yet actually payable, but a debt which is represented by an existing obligation."

47 Saunders J. noted in *633746 Ontario Inc. (Trustee of) v. Salvati* (1990), 79 C.B.R. (N.S.) 72 (Ont. S.C.) at p. 81 that a sale out of the ordinary course of business would have an adverse effect on that actually realized.

48 There was no suggestion by any of the parties that any of the assets and undertaking would have any enhanced value from that shown on the financial statements prepared according to GAAP.

49 In *King Petroleum Ltd., supra* at p. 81 Steele J. observed:

> To consider the question of insolvency under cl. (c) I must look to the aggregate property of the company and come to a conclusion as to whether or not it would be sufficient to enable payment of all obligations due and accruing due. There are two tests to be applied: First, its fair value and, secondly, its value if disposed of at a fairly conducted sale under legal process. The balance sheet is a starting point, but the evidence relating to the fair value of the assets and what they might realize if disposed of at a fairly conducted sale under legal process must be reviewed in interpreting it. In this case, I find no difficulty in accepting the obligations shown as liabilities because they are known. I have more difficulty with respect to the assets.

50 To my view the preferable interpretation to be given to "sufficient to enable payment of all his obligations, due and accruing due" is to be determined in the context of this test as a whole. What is being put up to satisfy those obligations is the debtor's assets and undertaking *in total*; in other words, the debtor in essence is taken as having sold everything. There would be no residual assets and undertaking to pay off any obligations which would not be encompassed by the phrase "all of his obligations, due and accruing due". Surely, there cannot be "orphan" obligations which are left hanging unsatisfied. It seems to me that the intention of "due and accruing due" was to cover off all obligations of whatever nature or kind and leave nothing in limbo.

51 S. 121(1) and (2) of the BIA, which are incorporated by reference in s. 12 of the CCAA, provide in respect to provable claims:

> S. 121(1) All debts and liabilities, present or future, to which the bankrupt is subject on the day on which the bankrupt becomes bankrupt or to which bankrupt may become subject before the bankrupt's discharge by reason of any obligation incurred before the day on which the bankrupt becomes bankrupt shall be deemed to be claims provable in proceedings under this Act.
>
> (2) The determination whether a contingent or unliquidated claim is a provable claim and the valuation of such claim shall be made in accordance with s. 135.

52 *Houlden and Morawetz 2004 Annotated supra* at p. 537 (G28(3)) indicates:

> The word "liability" is a very broad one. It includes all obligations to which the bankrupt is subject on the day on which he becomes bankrupt except for contingent and unliquidated claims which are dealt with in s. 121(2).

However contingent and unliquidated claims would be encompassed by the term "obligations".

53 In *Gardner v. Newton* (1916), 29 D.L.R. 276 (Man. K.B.), Mathers C.J.K.B. observed at p. 281 that "contingent claim, that is, a claim which may or may not ripen into a debt, according as some future event does or does not happen." See *A Debtor (No. 64 of 1992), Re*, [1993] 1 W.L.R. 264 (Eng. Ch. Div.) at p. 268 for the definition of a "liquidated sum" which is an amount which can be readily ascertained and hence by corollary an "unliquidated claim" would be one which is not easily ascertained, but will have to be valued. In *Gagnier, Re* (1950), 30 C.B.R. 74 (Ont. S.C.), there appears to be a conflation of not only the (a) test with the (c) test, but also the invocation of the judicial discretion not to grant the receiving order pursuant to a bankruptcy petition, notwithstanding that "[the judge was] unable to find the debtor is bankrupt". The debtor was able to survive the (a) test as he had the practice (accepted by all his suppliers) of providing them with post dated cheques. The (c) test was not a problem since the judge found that his assets should be valued at considerably more than his obligations. However, this case does illustrate that the application of the tests present some difficulties. These difficulties are magnified when one is dealing with something more significantly complex and a great deal larger than a haberdashery store - in the case before us, a giant corporation in which, amongst other things, is engaged in a very competitive history including competition from foreign sources which have recently restructured into more cost efficient structures, having shed certain of their obligations. As well, that is without taking into account that a sale would entail significant transaction costs. Even of greater significance would be the severance and termination payments to employees not continued by the new purchaser. Lastly, it was recognized by everyone at the

hearing that Stelco's plants, especially the Hamilton-Hilton works, have extremely high environmental liabilities lurking in the woodwork. Stephen observed that these obligations would be substantial, although not quantified.

54 It is true that there are no appraisals of the plant and equipment nor of the assets and undertaking of Stelco. Given the circumstances of this case and the complexities of the market, one may realistically question whether or not the appraisals would be all that helpful or accurate.

55 I would further observe that in the notional or hypothetical exercise of a sale, then all the obligations which would be triggered by such sale would have to be taken into account.

56 All liabilities, contingent or unliquidated would have to be taken into account. See *King Petroleum Ltd.*, *supra* p. 81; *Salvati*, *supra* pp. 80-1; *Maybank Foods Inc. (Trustee of) v. Provisioners Maritimes Ltd.* (1989), 45 B.L.R. 14 (N.S. T.D.) at p. 29; *Challmie, Re* (1976), 22 C.B.R. (N.S.) 78 (B.C. S.C.), at pp. 81-2. In *Challmie* the debtor ought to have known that his guarantee was very much exposed given the perilous state of his company whose liabilities he had guaranteed. It is interesting to note what was stated in *Maybank Foods Inc. (Trustee of)*, even if it is rather patently obvious. Tidman J. said in respect of the branch of the company at p. 29:

> Mr. MacAdam argues also that the $4.8 million employees' severance obligation was not a liability on January 20, 1986. The *Bankruptcy Act* includes as obligations both those due and accruing due. Although the employees' severance obligation was not due and payable on January 20, 1986 it was an obligation "accruing due". The Toronto facility had experienced severe financial difficulties for some time; in fact, it was the major, if not the sole cause, of Maybank's financial difficulties. I believe it is reasonable to conclude that a reasonably astute perspective buyer of the company has a going concern would have considered that obligation on January 20, 1986 and that it would have substantially reduced the price offered by that perspective buyer. Therefore that obligation must be considered as an obligation of the company on January 20, 1986.

57 With the greatest of respect for my colleague, I disagree with the conclusion of Ground J. in *Enterprise Capital Management Inc.*, *supra* as to the approach to be taken to "due and accruing due" when he observed at pp. 139-140:

> It therefore becomes necessary to determine whether the principle amount of the Notes constitutes an obligation "due or accruing due" as of the date of this application.
>
> There is a paucity of helpful authority on the meaning of "accruing due" for purposes of a definition of insolvency. Historically, in 1933, in *P. Lyall & Sons Construction Co. v. Baker*, [1933] O.R. 286 (Ont. C.A.), the Ontario Court of Appeal, in determining a question of set-off under the *Dominion Winding-Up Act* had to determine whether the amount claimed as set-off was a debt due or accruing due to the company in liquidation for purposes of that Act. Marsten J. at pp. 292-293 quoted from Moss J.A. in *Mail Printing Co. v. Clarkson* (1898), 25 O.R. 1 (Ont. C.A.) at p. 8:
>
> > A debt is defined to be a sum of money which is certainly, and at all event, payable without regard to the fact whether it be payable now or at a future time. And an accruing debt is a debt not yet actually payable, but a debt which is represented by an existing obligation: Per Lindley L.J. in *Webb v. Stenton* (1883), 11 Q.D.D. at p. 529.
>
> Whatever relevance such definition may have had for purposes of dealing with claims by and against companies in liquidation under the old winding-up legislation, it is apparent to me that it should not be applied to definitions of insolvency. To include every debt payable at some future date in "accruing due" for the purposes of insolvency tests would render numerous corporations, with long term debt due over a period of years in the future and anticipated to be paid out of future income, "insolvent" for the purposes of the BIA and therefore the CCAA. For the same reason, I do not accept the statement quoted in the Enterprise factum from the decision of the Bankruptcy Court for the Southern District of New York in *Centennial Textiles Inc., Re*, 220 B.R. 165 (U.S.N.Y.D.C. 1998) that "if the present saleable value of assets are less than the amount required to pay existing debt as they mature, the debtor is insolvent". In my view, the obligations, which are to be measured against the fair valuation of a company's

> property as being obligations due and accruing due, must be limited to obligations currently payable or properly chargeable to the accounting period during which the test is being applied as, for example, a sinking fund payment due within the current year. Black's Law Dictionary defines "accrued liability" as "an obligation or debt which is properly chargeable in a given accounting period, but which is not yet paid or payable". The principal amount of the Notes is neither due nor accruing due in this sense.

58 There appears to be some confusion in this analysis as to "debts" and "obligations", the latter being much broader than debts. Please see above as to my views concerning the floodgates argument under the BIA and CCAA being addressed by judicially exercised discretion even if "otherwise warranted" applications were made. I pause to note that an insolvency test under general corporate litigation need not be and likely is not identical, or indeed similar to that under these insolvency statutes. As well, it is curious to note that the cut off date is the end of the current fiscal period which could have radically different results if there were a calendar fiscal year and the application was variously made in the first week of January, mid-summer or the last day of December. Lastly, see above and below as to my views concerning the proper interpretation of this question of "accruing due".

59 It seems to me that the phrase "accruing due" has been interpreted by the courts as broadly identifying obligations that will "become due". See *Viteway Natural Foods Ltd.* below at pp. 163-4 - at least at some point in the future. Again, I would refer to my conclusion above that *every obligation* of the corporation in the hypothetical or notional sale must be treated as "accruing due" to avoid orphan obligations. In that context, it matters not that a wind-up pension liability may be discharged over 15 years; in a test (c) situation, it is crystallized on the date of the test. See *Optical Recording Laboratories Inc. supra* at pp. 756-7; *Viteway Natural Foods Ltd., Re* (1986), 63 C.B.R. (N.S.) 157 (B.C. S.C.) at pp. 164-63-4; *Consolidated Seed Exports Ltd., Re* (1986), 62 C.B.R. (N.S.) 156 (B.C. S.C.) at p. 163. In *Consolidated Seed Exports Ltd.*, Spencer J. at pp. 162-3 stated:

> In my opinion, a futures broker is not in that special position. The third definition of "insolvency" may apply to a futures trader at any time even though he has open long positions in the market. Even though Consolidated's long positions were not required to be closed on 10th December, the chance that they might show a profit by March 1981 or even on the following day and thus wipe out Consolidated's cash deficit cannot save it from a condition of insolvency on that day. The circumstances fit precisely within the third definition; if all Consolidated's assets had been sold on that day at a fair value, the proceeds would not have covered its obligations due and accruing due, including its obligations to pay in March 1981 for its long positions in rapeseed. The market prices from day to day establish a fair valuation. . . .
>
> The contract to buy grain at a fixed price at a future time imposes a present obligation upon a trader taking a long position in the futures market to take delivery in exchange for payment at that future time. It is true that in the practice of the market, that obligation is nearly always washed out by buying an offsetting short contract, but until that is done the obligation stands. The trader does not know who will eventually be on the opposite side of his transaction if it is not offset but all transactions are treated as if the clearing house is on the other side. It is a present obligation due at a future time. It is therefore an obligation accruing due within the meaning of the third definition of "insolvency".

60 The possibility of an expectancy of future profits or a change in the market is not sufficient; *Consolidated Seed Exports Ltd.* at p. 162 emphasizes that the test is to be done on that day, the day of filing in the case of an application for reorganization.

61 I see no objection to using Exhibit C to Stephen's affidavit as an aid to review the balance sheet approach to test (c). While Stephen may not have known who prepared Exhibit C, he addressed each of its components in the text of his affidavit and as such he could have mechanically prepared the exhibit himself. He was comfortable with and agreed with each of its components. Stelco's factum at paragraphs 70-1 submits as follows:

70. In Exhibit C to his Affidavit, Mr. Stephen addresses a variety of adjustments to the Shareholder's Equity of Stelco necessary to reflect the values of assets and liabilities as would be required to determine whether Stelco met the test of insolvency under Clause C. In cross examination of both Mr. Vaughan and Mr. Stephen only one of these adjustments was challenged - the "Possible Reductions in Capital Assets."

71. The basis of the challenge was that the comparative sales analysis was flawed. In the submission of Stelco, none of these challenges has any merit. Even if the entire adjustment relating to the value in capital assets is ignored, the remaining adjustments leave Stelco with assets worth over $600 million less than the value of its obligations due and accruing due. This fundamental fact is not challenged.

62 Stelco went on at paragraphs 74-5 of its factum to submit:

74. The values relied upon by Mr. Stephen if anything, understate the extent of Stelco's insolvency. As Mr. Stephen has stated, and no one has challenged by affidavit evidence or on cross examination, in a fairly conducted sale under legal process, the value of Stelco's working capital and other assets would be further impaired by: (i) increased environmental liabilities not reflected on the financial statements, (ii) increased pension deficiencies that would be generated on a wind up of the pension plans, (iii) severance and termination claims and (iv) substantial liquidation costs that would be incurred in connection with such a sale.

75. No one on behalf of the USWA has presented any evidence that the capital assets of Stelco are in excess of book value on a stand alone basis. Certainly no one has suggested that these assets would be in excess of book value if the related environmental legacy costs and collective agreements could not be separated from the assets.

63 Before turning to that exercise, I would also observe that test (c) is also disjunctive. There is an insolvency condition if the total obligation of the debtor exceed either (i) a fair valuation of its assets or (ii) the proceeds of a sale fairly conducted under legal process of its assets.

64 As discussed above and confirmed by Stephen, if there were a sale under legal process, then it would be unlikely, especially in this circumstance that values would be enhanced; in all probability they would be depressed from book value. Stephen took the balance sheet GAAP calculated figure of equity at November 30, 2003 as $804.2 million. From that, he deducted the loss for December 2003 - January 2004 of $17 million to arrive at an equity position of $787.2 million as at the date of filing.

65 From that, he deducted, reasonably in my view, those "booked" assets that would have no value in a test (c) sale namely: (a) $294 million of future income tax recourse which would need taxable income in the future to realize; (b) $57 million for a write-off of the Platemill which is presently hot idled (while Locker observed that it would not be prohibitive in cost to restart production, I note that neither Stephen nor Vaughn were cross examined as to the decision not to do so); and (c) the captialized deferred debt issue expense of $3.2 million which is being written off over time and therefore, truly is a "nothing". This totals $354.2 million so that the excess of value over liabilities before reflecting obligations not included in the financials directly, but which are, substantiated as to category in the notes would be $433 million.

66 On a windup basis, there would be a pension deficiency of $1252 million; however, Stephen conservatively in my view looked at the Mercer actuary calculations on the basis of a going concern finding deficiency of $656 million. If the $1252 million windup figure had been taken, then the picture would have been even bleaker than it is as Stephen has calculated it for test (c) purposes. In addition, there are deferred pension costs of $198.7 million which under GAAP accounting calculations is allowed so as to defer recognition of past bad investment experience, but this has no realizable value. Then there is the question of Employee Future Benefits. These have been calculated as at December 31, 2003 by the Mercer actuary as $909.3 million but only $684 million has been accrued and booked on the financial statements so that there has to be an increased provision of $225.3 million. These off balance sheet adjustments total $1080 million.

67 Taking that last adjustment into account would result in a *negative* equity of ($433 million minus $1080 million) or *negative* $647 million. On that basis without taking into account possible reductions in capital assets as dealt with in the somewhat flawed Exhibit E nor environmental and other costs discussed above, Stelco is insolvent according to the test (c). With respect to Exhibit E, I have not relied on it in any way, but it is entirely likely that a properly calculated Exhibit E would provide comparators (also being sold in the U.S. under legal process in a fairly conducted process) which tend to require a further downward adjustment. Based on test (c), Stelco is significantly, not marginally, under water.

68 In reaching my conclusion as to the negative equity (and I find that Stephen approached that exercise fairly and constructively), please note my comments above regarding the possible assumption of pension obligations by the purchaser being offset by a reduction of the purchase price. The 35% adjustment advocated as to pension and employee benefits in this regard is speculation by the Union. Secondly, the Union emphasized cash flow as being important in evaluation, but it must be remembered that Stelco has been negative cash flow for some time which would make that analysis unreliable and to the detriment of the Union's position. The Union treated the $773 million estimated contribution to the shortfall in the pension deficiency by the Pension Benefits Guarantee Fund as eliminating that as a Stelco obligation. That is not the case however as that Fund would be subrogated to the claims of the employees in that respect with a result that Stelco would remain liable for that $773 million. Lastly, the Union indicated that there should be a $155 million adjustment as to the negative equity in Sub Applicants when calculating Stelco's equity. While Stephen at Q. 181-2 acknowledged that there was no adjustment for that, I agree with him that there ought not to be since Stelco was being examined (and the calculations were based) on an unconsolidated basis, not on a consolidated basis.

69 In the end result, I have concluded on the balance of probabilities that Stelco is insolvent and therefore it is a "debtor company" as at the date of filing and entitled to apply for the CCAA initial order. My conclusion is that (i) BIA test (c) strongly shows Stelco is insolvent; (ii) BIA test (a) demonstrates, to a less certain but sufficient basis, an insolvency and (iii) the "new" CCAA test again strongly supports the conclusion of insolvency. I am further of the opinion that I properly exercised my discretion in granting Stelco and the Sub Applicants the initial order on January 29, 2004 and I would confirm that as of the present date with effect on the date of filing. The Union's motion is therefore dismissed.

70 I appreciate that all the employees (union and non-union alike) and the Union and the International have a justifiable pride in their work and their workplace - and a human concern about what the future holds for them. The pensioners are in the same position. Their respective positions can only be improved by engaging in discussion, an exchange of views and information reasonably advanced and conscientiously listened to and digested, leading to mutual problem solving, ideas and negotiations. Negative attitudes can only lead to the detriment to all stakeholders. Unfortunately there has been some finger pointing on various sides; that should be put behind everyone so that participants in this process can concentrate on the future and not inappropriately dwell on the past. I understand that there have been some discussions and interchange over the past two weeks since the hearing and that is a positive start.

Motion dismissed.

APPENDIX

TAB 5

1984 CarswellAlta 259
Alberta Court of Queen's Bench

Meridian Developments Inc. v. Toronto Dominion Bank

1984 CarswellAlta 259, [1984] 5 W.W.R. 215, [1984] A.W.L.D. 609, [1984] A.W.L.D. 611, 11 D.L.R. (4th) 576, 32 Alta. L.R. (2d) 150, 52 C.B.R. (N.S.) 109, 53 A.R. 39

MERIDIAN DEVELOPMENTS INC. v. TORONTO DOMINION BANK; MERIDIAN DVELOPMENTS INC. v. NU-WEST GROUP LTD.

Wachowich J.

Judgment: May 11, 1984
Docket: Edmonton Nos. 8401-10190, 8301-09096

Counsel: *A.Z. Breitman* and *J.G. Shea*, for Meridian Dev. Ltd.
J.L. MacPherson, Q.C., and *K.J. Martens*, for Toronto Dominion Bank.
P.M. Owen, Q.C., and *C. Bodner*, for Nu-West Group Ltd.

Subject: Corporate and Commercial; Insolvency

Application for advice and directions concerning obligation of bank to honour letter of credit.

Wachowich J.:

1 The applicant Meridian Developments Inc. (hereinafter called "Meridian") is an Alberta corporation which has recently been continued under the Alberta Business Corporations Act, 1981 (Alta.), c. B-15. Previously it was known as Meridian Developments Ltd. and it was in that name that Meridian sold land by agreement for sale to 233995 Alberta Ltd. on 16th March 1981. Nu-West Group Ltd. (hereinafter called "Nu-West") is the beneficial owner of all of the shares of 233995 Alberta Ltd. and on 16th March 1981 executed under seal an unconditional guarantee in favour of Meridian Developments Ltd. whereby Nu-West unconditionally guaranteed to Meridian the amounts due from 233995 Alberta Ltd. at the times and in the manner set forth in the agreement for sale.

2 It was a term of the guarantee that if default occurred under the agreement, Nu-West would forthwith on demand pay all of the purchase moneys owed.

3 By cl. 5 of this guarantee it was agreed that Meridian would not be bound to exhaust other resources or to act on other securities before proceeding against Nu-West.

4 On 15th March 1983, 233995 Alberta Ltd. defaulted on the agreement for sale. On 18th March 1983 demand was made to Nu-West as was required under the terms of the guarantee.

5 Nu-West failed to pay the amount owing on demand and, thereafter, Meridian issued a statement of claim on 31st March 1983. Nu-West did not defend this action and, as a result, Meridian obtained default judgment on 3rd May 1983 in the amount of $928,989.33 plus costs. A writ of execution was duly filed on 11th May 1983 and Meridian instructed the sheriff to seize sufficient assets of Nu-West to satisfy the judgment. Seizure of a number of pieces of furniture and office machines was effected on 16th May 1983.

6 Nu-West then made application by notice of motion for a declaration that Meridian was not at liberty to make execution against Nu-West until it had sold the land in question because of the provisions of s. 40(2) and (3) of the Law of Property Act, R.S.A. 1980, c. L-8. This application was dismissed by order of Kirby J. on 24th May 1983. Part of

the debt was then paid but execution on the balance of $463,329.33 was stayed pending Nu-West's appeal of Kirby J.'s order. The stay of execution granted was subject to the following conditions:

7 1. That Nu-West post an irrevocable letter of credit issued by the Toronto-Dominion Bank in favour of Meridian Developments Ltd. in the amount of the unpaid balance of $463,239.33 with interest at 11 $^{1}/_{2}$ per cent per annum calculated thereon from 4th May 1983 to the date of payment.

8 2. That Meridian's solicitors were to hold the letter on the trust conditions imposed in correspondence from solicitors for the defendant to the solicitors for the plaintiff dated 6th June 1983.

9 3. That the defendant would promptly prosecute the appeal of the order.

10 The appeal was subsequently launched on 20th June 1983 and heard on 12th October 1983. The appeal was dismissed with written reasons on 29th March 1984 [31 Alta. L.R. (2d) 1, [1984] 4 W.W.R. 97 (C.A.)].

11 The irrevocable letter of credit was held in trust by solicitors for Meridian throughout the period between Kirby J.'s first order and the dismissal of the appeal. During this period several new orders were made by consent each of which had the effect of continuing the terms and conditions of the original order. The amount of the letter of credit was increased during this period in order to account for the interest on the principal which accrued during the period. The order that was in effect when the decision of the Court of Appeal was released was made by Hetherington J. on 30th January 1984.

12 The letter of credit would have probably been honoured on presentation after 29th March were it not for the ex parte order obtained from myself by Nu-West under the Companies' Creditors Arrangement Act, R.S.C. 1970, c. C-25, as amended. This order was made as a result of Nu-West's insolvency and provided, inter alia, in cl. 2 that:

> further proceedings in any action, suit or proceeding against the Petitioner be restrained until July 31, 1984

and in clause 3 that:

> until July 31, 1984 no suit, action, or other proceeding be proceeded with or commenced against the Petitioner, except with leave of this Court.

As a result of the bank's knowledge of this order, it has not honoured the letter of credit and has, instead, brought interpleader proceedings.

13 Meridian has brought action against the bank alleging breach of contract in their failure to honour the letter of credit.

14 Application for advice and directions was also made by Meridian to entitle them to present the letter of credit for payment and to determine that my order of 21st March 1984 does not enjoin and restrain Meridian from presenting the letter of credit or the bank from honouring it.

15 From this the following issues come before me in this application:

16 1. Is payment of the letter of credit a "proceeding" within the meaning of cl. 2 or 3 of the 21st March order?

17 2. If so, is it a proceeding "against the Petitioner" [Nu-West] so as to be restrained by cl. 2 or 3 of that order?

18 3. If it is found to be a "proceeding", should the court in any case give leave to Meridian in the circumstances to obtain payment of the letter of credit?

19 These are difficult issues to resolve as counsel agree that the law in the area is unclear and the cases cannot all be reconciled. Further, there are good policy arguments to be made for both sides.

20 In order to resolve the issues raised in this application I must consider the scope and intent of my 21st March ex parte order under the Companies' Creditors Arrangement Act. This Act, though little used, is one of a number of federal statutes dealing with insolvency. In common with the various other statutes, it envisages the protection of creditors and the orderly administration of the debtor's affairs or assets: *Wynden Can. Inc. v. Gaz Metro Inc.* (1982), 44 C.B.R. (N.S.) 285 (C.S. Que.). In the words of Duff C.J.C. who spoke for the court in *A.G. Can. v. A.G. Que.*, [1934] S.C.R. 659, 16 C.B.R. 1 at 2, [1934] 4 D.L.R. 75:

> ... the aim of the Act is to deal with the existing condition of insolvency in itself to enable arrangements to be made in view of the insolvent condition of the company under judicial authority which, otherwise, might not be valid prior to the initiation of proceedings in bankruptcy. *Ex facie* it would appear that such a scheme in principle does not radically depart from the normal character of bankruptcy legislation.

21 The legislation is intended to have wide scope and allows a judge to make orders which will effectively maintain the status quo for a period while the insolvent company attempts to gain the approval of its creditors for a proposed arrangement which will enable the company to remain in operation for what is, hopefully, the future benefit of both the company and its creditors.

22 This aim is facilitated by s. 11 of the Act which enables the court to:

> ... restrain further proceedings in any action, suit or proceeding against the company upon such terms as the court sees fit, and the court may also make an order that no suit, action or other proceeding shall be proceeded with or commenced against the company except with the leave of the court and subject to such terms as the court imposes.

It was pursuant to this section that on 21st March I granted the order that restrained "further proceedings in any action, suit, or proceeding" against Nu-West and enjoined creditors and others from proceeding with or commencing any "suit, action, or proceeding".

23 This order is in accord with the general aim of the Companies' Creditors Arrangement Act. The intention was to prevent any manoeuvres for positioning among creditors during the interim period which would give the aggressive creditor an advantage to the prejudice of others who were less aggressive and would further undermine the financial position of the company making it less likely that the eventual arrangement would succeed.

24 The order was obviously intended to cast a wide net and catch all creditors. Therefore Meridian can only succeed if it can establish that the payment of the letter of credit is not a "proceeding" against Nu-West as contemplated by the order.

25 As both counsel have frankly admitted, there are no cases directly on point. One of the few cases which does deal with the meaning of the word "proceeding" in the Companies' Creditors Arrangements Act is *Gray v. Wentworth Canning Co.*, 58 Man. R. 459, 31 C.B.R. 182, [1950] 2 W.W.R. 1285, a decision of the Manitoba Court of King's Bench. In that case Kelly J. determined that the relevant statute section gave the court complete discretion to determine the kinds of proceedings it would restrain. Although because of the wording in the particular order there at issue, Kelly J. determined that it was meant to catch only proceedings, suits, or actions which had not yet been instituted, it is clear from his judgment that he sees the section as allowing orders of much wider range. He points out, in fact, that it is because the draftsman of the order did not see fit to follow the exact words of what was then s. 10 of the Companies' Creditors Arrangement Act, 1932-33 (Can.), c. 36, that the order as given must be seen as restraining only those proceedings commenced after the order was given.

26 A similar provision to s. 11 may be found in the English Companies Act, 1862 (25 & 26 Vict.), c. 89, s. 85, which allowed a court at any time after the presentation of a winding-up petition to:

> ... restrain further Proceedings in any Action, Suit, or Proceeding against the Company, upon such Terms as the Court sees fit; the Court may also make an order that no Suit, Action or other Proceeding shall be proceeded with

or commenced against the Company except with the Leave of the Court and subject to such Terms as the Court imposes.

27 Several cases which have interpreted this provision are useful in determining the scope of the term "proceeding". Jessel M.R. in *Re Artistic Colour Printing Co.* (1880), 14 Ch. D. 502, determined that an order made under this section could restrain the sheriff from selling goods already in his possession after seizure on the judgment of a judgment creditor. At p. 505 he concluded: "The word 'proceeding' in both sections of course includes execution under a judgment in an action." *Re Perkins Beach Lead Mining Co.* (1877), 7 Ch. D. 371, is to the same effect.

28 Counsel for Meridian admits that "proceeding" may have a very general meaning but submits that we must confine ourselves here to proceedings which necessarily involve a court or a court official. There is certainly authority for this proposition. Black's Law Dictionary, 5th ed. (1979), defines the term in the following manner:

> *Proceeding.* In a general sense, the form and manner of conducting juridical business before a court or judicial officer. Regular and orderly progress in form of law, including all possible steps in an action from its commencement to the execution of judgment. Term also refers to administrative proceedings before agencies, tribunals, bureaus, or the like.
>
> An act which is done by the authority or direction of the court, agency, or tribunal, express or implied; an act necessary to be done in order to obtain a given end; a prescribed mode of action for carrying into effect a legal right. All the steps or measures adopted in the prosecution or defense of an action. *Statter v. U.S.* (1933), 66 F. (2d) 819 (Alaska C.C.A.) . The word may be used synonymously with "action" or "suit" to describe the entire course of an action at law or suit in equity from the issuance of the writ or filing of the complaint until the entry of a final judgment, or may be used to describe any act done by authority of a court of law and every step required to be taken in any cause by either party. The proceedings of a suit embrace all matters that occur in its progress judicially.
>
> Term "proceeding" may refer not only to a complete remedy but also to a mere procedural step that is part of a larger action or special proceeding. *Rooney v. Vermont Invt. Corp.* (1973), 10 Cal. (3d) 351, 110 Cal. Rptr. 353, 515 P. (2d) 297 (Cal. S.C.). A "proceeding" includes action and special proceedings before judicial tribunals as well as proceedings pending before quasi-judicial officers and boards. *State ex rel. Johnson v. Independent Sch. Dist. No. 810, Wabasha County* (1961), 260 Minn. 237, 109 N.W. (2d) 596 (Minn. S.C.).

29 Words and Phrases Legally Defined, 2nd ed. (1969), vol. 4, p. 182, similarly restricts the definition to actions before a court or other judicial body:

> **Proceedings**
>
> The term "proceeding" is frequently used to note a step in an action, and obviously it has that meaning in such phrases as "proceeding in any cause or matter". When used alone, however, it is in certain statutes to be construed as synonymous with, or including "action" (1 Hals. (3rd) 4-5, paras. 5, 6).
>
> "By s. 89 of the Judicature Act of 1873 (36 & 37 Vict.), c. 66 [repealed; see now Supreme Court of Judicature (Consolidation) Act, 1925, (15 & 16 Geo. 5), c. 49, s. 202] ... it is said that every inferior court 'shall, as regards all causes of action within its jurisdiction for the time being, have power to grant and shall grant in any proceeding before such Court, such relief, redress, or remedy' in as full and ample a manner as might and ought to be done in the like case by the High Court of Justice ... It can do so 'in any proceeding'. Now what is the meaning there of 'in any proceeding'? ... Now, although if s. 89 stood by itself, there might be some difficulty in determining what is the meaning of the word 'proceeding', yet it seems to me to be clear what is its meaning in s. 90 [repealed; see now Supreme Court of Judicature (Consolidation) Act, 1925, s. 203], and that 'proceeding' in that section is a general word meant to cover every step in an action, and is equivalent to the word 'action'." *Pryor v. City Offices Co.* (1883), 10 Q.B.D. 504 (C.A.), *per* Brett, M.R., at pp. 507, 508.

> "Anything that precedes the final judgment or order is, in my opinion, a 'proceeding' in the action." *Blake v. Summersby*, [1889] W.M. 39, *per* Kay, J. at p. 39.

30 Although this last mentioned definition indicated *Blake v. Summersby* restricts the proceedings to steps in an action preceding judgment, there is ample authority, cited by both counsel, to indicate that the term must be taken to include execution steps taken after judgment. As I indicated earlier, counsel for Meridian would restrict "execution proceedings" to those involving a court or court official. Those cases cited by Nu-West which indicate that an order restraining proceedings restrains a sheriff from conducting a sale following seizure, I am satisfied are in accord with this view inasmuch as the sheriff is an officer of the court. Further, counsel for Meridian cites *Can. Credit Men's Trust Assn. v. Edmonton*, 5 C.B.R. 589, 21 Alta. L.R. 160, [1925] 1 W.W.R. 747, [1925] 2 D.L.R. 525, where the Alberta Appellate Division found that a distress was not a "process against property" within the meaning of s. 11 of the Bankruptcy Act, 1919 (Can.), c. 36. He also cites another Alberta Appellate Division decision, that of *Lee v. Armstrong*, 13 Alta. L.R. 160, [1917] 3 W.W.R. 889, 37 D.L.R. 738, where the court found that the noting on the title by the registrar of a writ of execution was not a "proceeding" within the meaning of the phrase "no proceedings shall be had or taken in respect of any execution already issued on any personal judgment ... until sale of the land mortgaged" as found in the Land Titles Act, 1906 (Alta.), c. 24, s. 62(2) [am. 1917, c. 3, s. 40(2)].

31 Meridian argues further on the basis of the ejusdem generis rule that the interpretation of "other proceeding" in s. 11 of the Companies' Creditors Arrangement Act is limited to proceedings which would fall within the genus indicated by the words "suit" and "action". This, too, indicates that the term as used in the Act ought to be restricted to proceedings which necessarily involve either a court or court official.

32 These arguments are persuasive. Nonetheless, I am mindful of the wide scope of action which Parliament intended for this section of the Act. To narrow the interpretation of "proceeding" could lessen the ability of a court to restrain a creditor from acting to prejudice an eventual arrangement in the interim when other creditors are being consulted. As I indicated earlier, it is necessary to give this section a wide interpretation in order to ensure its effectiveness. I hesitate therefore to restrict the term "proceedings" to those necessarily involving a court or court official because there are situations in which to do so would allow non-judicial proceedings to go against the creditor which would effectively prejudice other creditors and make effective arrangement impossible. The restriction could thus defeat the purpose of the Act. I must consider, for instance, the fact that it may still be possible to make distress without requiring a sheriff or his bailiff, as for example, on a chattel mortgage. It might well be necessary to find that such a distress constitutes a "proceeding" in terms of s. 11 in some future situations. As a result, in the absence of a clear indication from Parliament of an intention to restrict "proceedings" to "proceedings which involve either a court or court official", I cannot find that the term should be so restricted. Had Parliament intended to so restrict the term, it would have been easy to qualify it by saying for instance "proceedings before a court or tribunal".

33 Nor is there anything within the provisions of the order given on 21st March to indicate any intention to so limit the meaning of the word. I conclude, therefore, that payment of a letter of credit drawn on the account of an insolvent company could well come within the meaning of the word "proceeding" in the order.

34 Here, we are dealing with a payment which remains contingent at the date of the order. It awaited the judgment of the Court of Appeal on 21st March and thus, did involve a court or court official. Even if, therefore, I were to accept that payment of a letter of credit is not a proceeding under the Act, it seems clear that a payment which awaits a decision of the court is a proceeding as contemplated by the Act.

35 It must be noted, however, that by the terms of the 21st March 1984 order it is only "further proceedings in any action, suit, or proceeding against the Petitioner" that are restrained. Unless the payment of the letter of credit is a "proceeding against the Petitioner" (Nu-West) it was not restrained by this order. I agree with counsel for Meridian that the payment of the letter of credit cannot be termed a proceeding against Nu-West unless the money to be paid is Nu-West's property.

36 The ownership of the funds represented by the letter of credit is dependent upon the judicial nature of the commercial instrument in question. The nature of a letter of credit has been extensively considered. 3 Hals. (4th) states at p. 100, para. 132 that letters of credit:

> ... create binding contract to accept or pay bills on the specified conditions, enforeable against the banker by any person to whom the letter has been shown by the grantee, and who has acted on the faith of it.

In para. 133 at p. 102 the authors continue:

> The contract thus created between the seller and the banker is separate from, although ancillary to, the original contract between the buyer and the seller, by reason of the banker's undertaking to the seller, which is absolute.

37 The nature of a letter of credit has been explored in both English and Canadian cases. In *Aspen Planners Ltd. v. Commerce Masonry & Forming Ltd.* (1979), 7 B.L.R. 102 at 107 (Ont. H.C.) Henry J. quotes with approval from the English Court of Appeal [who are quoting from *Malas (Hamzch) v. Sons & British Imex Indust.*, [1958] 2 Q.B. 127, [1958] 1 All E.R. 262 at 263, [1958] 2 W.L.R. 100, [1957] 2 Lloyd's Rep. 549 (C.A.)] in *Edward Owen Enrg. Ltd. v. Barclay's Bank Int.*, [1978] 1 All E.R. 976 at 981, [1978] 1 Lloyd's Rep. 166 (C.A.):

> " '.. it seems to be plain that the opening of a confirmed letter of credit constitutes a bargain between the banker and the vendor of the goods, which imposes on the banker an absolute obligation to pay, irrespective of any dispute which there may be between the parties on the question whether the goods are up to the contract or not. An elaborate commercial system has been built up on the footing that bankers' confirmed credits are of that character, and, in my judgment it would be wrong for this court in the present case to interfere with that established practice.' "

38 *Aspen Planners Ltd.*, supra, deals with a situation in which the plaintiffs arranged irrevocable letters of credit to a contractor to ensure payment of a building contract. They later alleged that the contractor had defaulted on the contract and sought to obtain an injunction restraining payment under the letter of credit. The Ontario court refused, citing the irrevocable nature of the bank's obligation to pay the contractor.

39 This case, as do the English cases cited by counsel, exemplifies the more traditional use of the letter to guarantee payment in commercial transactions where goods and services are bought and sold.

40 Here, however, a more novel use has been made of the letter of credit as a security device and to determine whether this use affects the nature of the document we must turn to the American cases where the use of letters of credit, particularly in the way one was used here, is much more prevalent.

41 The nature of a letter of credit was explored in numerous cases relied upon by counsel for Meridian. *East Girard Savings Assn. v. Citizens Nat. Bank and Trust Co. of Bagtown* (1979), 593 F. (2d) 598, a decision of the U.S. Court of Appeals, Fifth Circuit, sets out the nature of the letter of credit at p. 601:

> ... a letter of credit typically involves three separate contracts. First, the issuing bank enters into a contract with its customer to issue the letter of credit. Second, there is a contract between the issuing bank and the party receiving the letter of credit. Third, the customer who procured the letter of credit signs a contract with the person receiving it, usually involving the sale of goods or the provision of some service. *Barclays Bank D.C.O. v. Mercantile Nat. Bank* (1973), 481 F. (2d) 1224, 1239 n.21, cert. dismissed 414 U.S. 1139, 94 S.Ct. 888, 39 L.Ed. (2d) 96; Verkuil, "Bank Solvency and Guaranty Letters of Credit," 25 Stan. L. Rev. 716 at 719.
>
> In recent years, letters of credit have been used for a variety of commercial transactions, Harfield, *The Increasing Domestic Use of the Letter* (1972), 4 U.C.C.L.J. 251. The guaranty letter of credit is one of these recent innovations. The guaranty letter of credit is designed to ensure that one or more parties to a contract will perform their duties under it. In a typical guaranty situation, the future owner of a building requires that the building contractor give him a completion bond providing for the payment of a certain sum of money if the building is not completed on schedule.

At p. 602 the court continues:

> Regardless of which form of letter of credit is used, upon compliance with the conditions contained in the letter, the recipient is entitled to full payment. This entitlement is independent of collateral obligations which may exist under the other underlying contracts. *Pringle-Assoc. Mtge. Corp. v. Southern Nat. Bank of Hattiesburg, Miss.*, 571F. (2d) 871 (Miss. C.A.); *Barclays Bank*, supra, at 1238-39; Vernons Texas Codes, Annotated, 2 Tex. Bus. & Com. Code (1968), p. 534, s. 5.114(a).

At p. 603 the court concludes:

> If the letter of credit is to retain its utility as a commercial instrument, the rights and duties of the issuer, the beneficiary, and the procurer must remain clear. Parties to commercial transactions must be able to rely on the fact that as soon as the conditions contained in a particular letter are satisfied, payment is due.

42 This case, and others cited by counsel for Meridian, clearly indicate that the nature of a letter of credit has not been changed by its use in a greater variety of commercial transactions, notably as a guarantee. It exists as an independent contract between the bank and the person cashing or negotiating the draft and, if it is irrevocable, the bank is bound to honour it.

43 Because of the independent contractual nature of a letter of credit, the analogy which Nu-West attempts to make between money held in court following seizure and a letter of credit cannot be maintained. Money paid into court may well remain the property of the defendants as the Saskatchewan Court of Appeal determined in *Regina Steam Laundry Ltd. v. Sask. Govt. Ins. Office*, [1971] 1 W.W.R. 96, 15 D.L.R. (3d) 121 , although I note that there is also authority to the contrary: *Re Keyworth; Ex parte Banner* (1874), 9 Ch. App. 379 (L.S.); *Re Hansard Spruce Mills Ltd.*, [1954] 1 D.L.R. 326 (B.C.S.C.). Security in the form of an irrevocable letter of credit is not the property of the party arranging the letter of credit. Indeed, I would go so far as to say that it has never been his money. He has contracted with his bank to require the bank to pay out a specific amount of money to a third party on the occurrence of certain events. In return he has promised to repay the bank for the funds so expended. The customer of the bank has, in my view, never had "ownership" of any funds represented by the letter of credit. He can lay claim only to the debt that has been thereby created.

44 Thus, it is my view that even if the payment out of a letter of credit could be termed a "proceeding", as this term is used in s. 11 of the Companies' Creditors Arrangement Act, it cannot be termed "a proceeding against the Petitioner" so as to be caught by the order of 21st March.

45 I am fortified in my view by a recent unreported American case cited by Meridian which seems right on point. The case is *Page v. First Nat. Bank of Maryland*, U.S. Dist. Ct., Dist. of Columbia, 30th March 1982 (not yet reported).

46 The facts are very similar to those found here. Westinghouse Credit Corporation ("W.C.C.") was the beneficiary of a letter of credit drawn on the First National Bank of Maryland ("bank"). The bank was enjoined from payment out on this letter after Page and Associates, a limited partnership and Virginia Page ("Page") its sole general partner, filed voluntary petitions in bankruptcy. W.C.C. was a substantial creditor of Page, holding among its forms of security the letter of credit issued on the bank. W.C.C. presented its letter of credit for payment four days after the petition was filed. Page sought an injunction the next day which was granted on the ground that to pay the letter would be a transfer in violation of the Bankruptcy Code, 11 U.S.C., s. 362(3) or (4). These subsections provide:

> [A] petition [under Title 11] operates as a stay, applicable to all entities, of ...
>
> (3) any act to obtain possession of property of the estate or of property from the estate;
>
> (4) any act to create, perfect or enforce any lien against property of the estate.

W.C.C. appealed the decision to grant the injunction and this appeal was allowed. The court found that cashing the letter of credit was not the type of act contemplated by the provisions of the statute since neither the letter of credit nor its proceeds are the "property of the estate" under the Bankruptcy Code.

47 At p. 4 of the decision the court stated:

> In issuing the letter of credit the bank entered into an independent contractual obligation to pay W.C.C. out of its own assets. Although cashing the letter will immediately give rise to a claim by the bank against the debtors pursuant to the latter's indemnification obligations, that claim will not divest the debtors of any property since any attempt to enforce that claim would be subject to an automatic stay pursuant to 11 U.S.C., para. 362(4).

48 In my view the Toronto-Dominion Bank is in the same position. It is obliged to honour its contract with Meridian even though the cashing of the letter of credit will increase Nu-West's debt to the bank and even though the bank has no method of enforcing its claim against Nu-West because of the 21st March order.

49 It makes no difference that the letter of credit was held in trust by Meridian's solicitors and that the condition precedent for presentation had not been met on 21st March. If the moneys secured were not Nu-West property on 21st March, the order did not affect them. The letter of credit became negotiable when the condition precedent was fulfilled on 29th March with the rendering of the Court of Appeal's decision in Meridian's favour. The bank should be directed to honour it on presentation on the terms and conditions specified in the letter and it is so ordered.

Directions given.

TAB 6

2009 CarswellOnt 4467
Ontario Superior Court of Justice [Commercial List]

Nortel Networks Corp., Re

2009 CarswellOnt 4467, [2009] O.J. No. 3169, 179 A.C.W.S. (3d) 265, 55 C.B.R. (5th) 229

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 NORTEL NETWORKS CORPORATION, NORTEL NETWORKS LIMITED, NORTEL NETWORKS GLOBAL CORPORATION, NORTEL NETWORKS INTERNATIONAL CORPORATION AND NORTEL NETWORKS TECHNOLOGY CORPORATION (Applicants)

APPLICATION UNDER THE COMPANIES' CREDITORS ARRANGEMENT ACT, R.S.C. 1985, c. C-36, AS AMENDED

Morawetz J.

Heard: June 29, 2009
Written reasons: July 23, 2009
Docket: 09-CL-7950

Counsel: Derrick Tay, Jennifer Stam for Nortel Networks Corporation, et al
Lyndon Barnes, Adam Hirsh for Board of Directors of Nortel Networks Corporation, Nortel Networks Limited
J. Carfagnini, J. Pasquariello for Monitor, Ernst & Young Inc.
M. Starnino for Superintendent of Financial Services, Administrator of PBGF
S. Philpott for Former Employees
K. Zych for Noteholders
Pamela Huff, Craig Thorburn for MatlinPatterson Global Advisors LLC, MatlinPatterson Global Opportunities Partners III L.P., Matlin Patterson Opportunities Partners (Cayman) III L.P.
David Ward for UK Pension Protection Fund
Leanne Williams for Flextronics Inc.
Alex MacFarlane for Official Committee of Unsecured Creditors
Arthur O. Jacques, Tom McRae for Felske & Sylvain (de facto Continuing Employees' Committee)
Robin B. Schwill, Matthew P. Gottlieb for Nortel Networks UK Limited
A. Kauffman for Export Development Canada
D. Ullman for Verizon Communications Inc.
G. Benchetrit for IBM

Subject: Insolvency; Estates and Trusts

MOTION by company for approval of bidding procedures for sale of business and asset sale agreement.

Morawetz J.:

Introduction

1 On June 29, 2009, I granted the motion of the Applicants and approved the bidding procedures (the "Bidding Procedures") described in the affidavit of Mr. Riedel sworn June 23, 2009 (the "Riedel Affidavit") and the Fourteenth

Report of Ernst & Young, Inc., in its capacity as Monitor (the "Monitor") (the "Fourteenth Report"). The order was granted immediately after His Honour Judge Gross of the United States Bankruptcy Court for the District of Delaware (the "U.S. Court") approved the Bidding Procedures in the Chapter 11 proceedings.

2 I also approved the Asset Sale Agreement dated as of June 19, 2009 (the "Sale Agreement") among Nokia Siemens Networks B.V. ("Nokia Siemens Networks" or the "Purchaser"), as buyer, and Nortel Networks Corporation ("NNC"), Nortel Networks Limited ("NNL"), Nortel Networks, Inc. ("NNI") and certain of their affiliates, as vendors (collectively the "Sellers") in the form attached as Appendix "A" to the Fourteenth Report and I also approved and accepted the Sale Agreement for the purposes of conducting the "stalking horse" bidding process in accordance with the Bidding Procedures including, the Break-Up Fee and the Expense Reimbursement (as both terms are defined in the Sale Agreement).

3 An order was also granted sealing confidential Appendix "B" to the Fourteenth Report containing the schedules and exhibits to the Sale Agreement pending further order of this court.

4 The following are my reasons for granting these orders.

5 The hearing on June 29, 2009 (the "Joint Hearing") was conducted by way of video conference with a similar motion being heard by the U.S. Court. His Honor Judge Gross presided over the hearing in the U.S. Court. The Joint Hearing was conducted in accordance with the provisions of the Cross-Border Protocol, which had previously been approved by both the U.S. Court and this court.

6 The Sale Agreement relates to the Code Division Multiple Access ("CMDA") business Long-Term Evolution ("LTE") Access assets.

7 The Sale Agreement is not insignificant. The Monitor reports that revenues from CDMA comprised over 21% of Nortel's 2008 revenue. The CDMA business employs approximately 3,100 people (approximately 500 in Canada) and the LTE business employs approximately 1,000 people (approximately 500 in Canada). The purchase price under the Sale Agreement is $650 million.

Background

8 The Applicants were granted CCAA protection on January 14, 2009. Insolvency proceedings have also been commenced in the United States, the United Kingdom, Israel and France.

9 At the time the proceedings were commenced, Nortel's business operated through 143 subsidiaries, with approximately 30,000 employees globally. As of January 2009, Nortel employed approximately 6,000 people in Canada alone.

10 The stated purpose of Nortel's filing under the CCAA was to stabilize the Nortel business to maximize the chances of preserving all or a portion of the enterprise. The Monitor reported that a thorough strategic review of the company's assets and operations would have to be undertaken in consultation with various stakeholder groups.

11 In April 2009, the Monitor updated the court and noted that various restructuring alternatives were being considered.

12 On June 19, 2009, Nortel announced that it had entered into the Sale Agreement with respect to its assets in its CMDA business and LTE Access assets (collectively, the "Business") and that it was pursuing the sale of its other business units. Mr. Riedel in his affidavit states that Nortel has spent many months considering various restructuring alternatives before determining in its business judgment to pursue "going concern" sales for Nortel's various business units.

13 In deciding to pursue specific sales processes, Mr. Riedel also stated that Nortel's management considered:

(a) the impact of the filings on Nortel's various businesses, including deterioration in sales; and

(b) the best way to maximize the value of its operations, to preserve jobs and to continue businesses in Canada and the U.S.

14 Mr. Riedel notes that while the Business possesses significant value, Nortel was faced with the reality that:

(a) the Business operates in a highly competitive environment;

(b) full value cannot be realized by continuing to operate the Business through a restructuring; and

(c) in the absence of continued investment, the long-term viability of the Business would be put into jeopardy.

15 Mr. Riedel concluded that the proposed process for the sale of the Business pursuant to an auction process provided the best way to preserve the Business as a going concern and to maximize value and preserve the jobs of Nortel employees.

16 In addition to the assets covered by the Sale Agreement, certain liabilities are to be assumed by the Purchaser. This issue is covered in a comprehensive manner at paragraph 34 of the Fourteenth Report. Certain liabilities to employees are included on this list. The assumption of these liabilities is consistent with the provisions of the Sale Agreement that requires the Purchaser to extend written offers of employment to at least 2,500 employees in the Business.

17 The Monitor also reports that given that certain of the U.S. Debtors are parties to the Sale Agreement and given the desire to maximize value for the benefit of stakeholders, Nortel determined and it has agreed with the Purchaser that the Sale Agreement is subject to higher or better offers being obtained pursuant to a sale process under s. 363 of the U.S. Bankruptcy Code and that the Sale Agreement shall serve as a "stalking horse" bid pursuant to that process.

18 The Bidding Procedures provide that all bids must be received by the Seller by no later than July 21, 2009 and that the Sellers will conduct an auction of the purchased assets on July 24, 2009. It is anticipated that Nortel will ultimately seek a final sales order from the U.S. Court on or about July 28, 2009 and an approval and vesting order from this court in respect of the Sale Agreement and purchased assets on or about July 30, 2009.

19 The Monitor recognizes the expeditious nature of the sale process but the Monitor has been advised that given the nature of the Business and the consolidation occurring in the global market, there are likely to be a limited number of parties interested in acquiring the Business.

20 The Monitor also reports that Nortel has consulted with, among others, the Official Committee of Unsecured Creditors (the "UCC") and the bondholder group regarding the Bidding Procedures and is of the view that both are supportive of the timing of this sale process. (It is noted that the UCC did file a limited objection to the motion relating to certain aspects of the Bidding Procedures.)

21 Given the sale efforts made to date by Nortel, the Monitor supports the sale process outlined in the Fourteenth Report and more particularly described in the Bidding Procedures.

22 Objections to the motion were filed in the U.S. Court and this court by MatlinPatterson Global Advisors LLC, MatlinPatterson Global Opportunities Partners III L.P. and Matlin Patterson Opportunities Partners (Cayman) III L.P. (collectively, "MatlinPatterson") as well the UCC.

23 The objections were considered in the hearing before Judge Gross and, with certain limited exceptions, the objections were overruled.

Issues and Discussion

24 The threshold issue being raised on this motion by the Applicants is whether the CCAA affords this court the jurisdiction to approve a sales process in the absence of a formal plan of compromise or arrangement and a creditor vote. If the question is answered in the affirmative, the secondary issue is whether this sale should authorize the Applicants to sell the Business.

25 The Applicants submit that it is well established in the jurisprudence that this court has the jurisdiction under the CCAA to approve the sales process and that the requested order should be granted in these circumstances.

26 Counsel to the Applicants submitted a detailed factum which covered both issues.

27 Counsel to the Applicants submits that one of the purposes of the CCAA is to preserve the going concern value of debtors companies and that the court's jurisdiction extends to authorizing sale of the debtor's business, even in the absence of a plan or creditor vote.

28 The CCAA is a flexible statute and it is particularly useful in complex insolvency cases in which the court is required to balance numerous constituents and a myriad of interests.

29 The CCAA has been described as "skeletal in nature". It has also been described as a "sketch, an outline, a supporting framework for the resolution of corporate insolvencies in the public interest". *ATB Financial v. Metcalfe & Mansfield Alternative Investments II Corp.* (2008), 45 C.B.R. (5th) 163 (Ont. C.A.) at paras. 44, 61, leave to appeal refused [2008] S.C.C.A. No. 337 (S.C.C.). ("ATB Financial").

30 The jurisprudence has identified as sources of the court's discretionary jurisdiction, *inter alia*:

> (a) the power of the court to impose terms and conditions on the granting of a stay under s. 11(4) of the CCAA;
>
> (b) the specific provision of s. 11(4) of the CCAA which provides that the court may make an order "on such terms as it may impose"; and
>
> (c) the inherent jurisdiction of the court to "fill in the gaps" of the CCAA in order to give effect to its objects. *Canadian Red Cross Society / Société Canadienne de la Croix-Rouge, Re* (1998), 5 C.B.R. (4th) 299 (Ont. Gen. Div. [Commercial List]) at para. 43; *PSINET Ltd., Re* (2001), 28 C.B.R. (4th) 95 (Ont. S.C.J. [Commercial List]) at para. 5, *ATB Financial, supra*, at paras. 43-52.

31 However, counsel to the Applicants acknowledges that the discretionary authority of the court under s. 11 must be informed by the purpose of the CCAA.

> Its exercise must be guided by the scheme and object of the Act and by the legal principles that govern corporate law issues. *Re Stelco Inc.* (2005), 9 C.B.R. (5th) 135 (Ont. C.A.) at para. 44.

32 In support of the court's jurisdiction to grant the order sought in this case, counsel to the Applicants submits that Nortel seeks to invoke the "overarching policy" of the CCAA, namely, to preserve the going concern. *Residential Warranty Co. of Canada Inc., Re* (2006), 21 C.B.R. (5th) 57 (Alta. Q.B.) at para. 78.

33 Counsel to the Applicants further submits that CCAA courts have repeatedly noted that the purpose of the CCAA is to preserve the benefit of a going concern business for all stakeholders, or "the whole economic community":

> The purpose of the CCAA is to facilitate arrangements that might avoid liquidation of the company and allow it to continue in business to the benefit of the whole economic community, including the shareholders, the creditors (both secured and unsecured) and the employees. *Citibank Canada v. Chase Manhattan Bank of Canada* (1991), 5 C.B.R. (3rd) 167 (Ont. Gen. Div.) at para. 29. *Re Consumers Packaging Inc.* (2001) 27 C.B.R. (4th) 197 (Ont. C.A.) at para. 5.

34 Counsel to the Applicants further submits that the CCAA should be given a broad and liberal interpretation to facilitate its underlying purpose, including the preservation of the going concern for the benefit of all stakeholders and further that it should not matter whether the business continues as a going concern under the debtor's stewardship or under new ownership, for as long as the business continues as a going concern, a primary goal of the CCAA will be met.

35 Counsel to the Applicants makes reference to a number of cases where courts in Ontario, in appropriate cases, have exercised their jurisdiction to approve a sale of assets, even in the absence of a plan of arrangement being tendered to stakeholders for a vote. In doing so, counsel to the Applicants submits that the courts have repeatedly recognized that they have jurisdiction under the CCAA to approve asset sales in the absence of a plan of arrangement, where such sale is in the best interests of stakeholders generally. *Canadian Red Cross Society / Société Canadienne de la Croix-Rouge, Re, supra, Re PSINet, supra, Consumers Packaging Inc., Re* [2001 CarswellOnt 3482 (Ont. C.A.)], *supra, Stelco Inc., Re* (2004), 6 C.B.R. (5th) 316 (Ont. S.C.J. [Commercial List]) at para. 1, *Tiger Brand Knitting Co., Re* (2005), 9 C.B.R. (5th) 315 (Ont. S.C.J.), *Caterpillar Financial Services Ltd. v. Hard-Rock Paving Co.* (2008), 45 C.B.R. (5th) 87 (Ont. S.C.J.) and *Lehndorff General Partner Ltd., Re* (1993), 17 C.B.R. (3d) 24 (Ont. Gen. Div. [Commercial List]).

36 In *Re Consumers Packaging, supra,* the Court of Appeal for Ontario specifically held that a sale of a business as a going concern during a CCAA proceeding is consistent with the purposes of the CCAA:

> The sale of Consumers' Canadian glass operations as a going concern pursuant to the Owens-Illinois bid allows the preservation of Consumers' business (albeit under new ownership), and is therefore consistent with the purposes of the CCAA.
>
> ...we cannot refrain from commenting that Farley J.'s decision to approve the Owens-Illinois bid is consistent with previous decisions in Ontario and elsewhere that have emphasized the broad remedial purpose of flexibility of the CCAA and have approved the sale and disposition of assets during CCAA proceedings prior to a formal plan being tendered. *Re Consumers Packaging, supra, at paras. 5, 9.*

37 Similarly, in *Canadian Red Cross Society / Société Canadienne de la Croix-Rouge, Re, supra,* Blair J. (as he then was) expressly affirmed the court's jurisdiction to approve a sale of assets in the course of a CCAA proceeding before a plan of arrangement had been approved by creditors. *Canadian Red Cross Society / Société Canadienne de la Croix-Rouge, Re, supra,* at paras. 43, 45.

38 Similarly, in *PSINet Limited, supra,* the court approved a going concern sale in a CCAA proceeding where no plan was presented to creditors and a substantial portion of the debtor's Canadian assets were to be sold. Farley J. noted as follows:

> [If the sale was not approved,] there would be a liquidation scenario ensuing which would realize far less than this going concern sale (which appears to me to have involved a transparent process with appropriate exposure designed to maximize the proceeds), thus impacting upon the rest of the creditors, especially as to the unsecured, together with the material enlarging of the unsecured claims by the disruption claims of approximately 8,600 customers (who will be materially disadvantaged by an interrupted transition) plus the job losses for approximately 200 employees. *Re PSINet Limited, supra,* at para. 3.

39 In *Re Stelco Inc., supra,* in 2004, Farley J. again addressed the issue of the feasibility of selling the operations as a going concern:

> I would observe that usually it is the creditor side which wishes to terminate CCAA proceedings and that when the creditors threaten to take action, there is a realization that a liquidation scenario will not only have a negative effect upon a CCAA applicant, but also upon its workforce. Hence, the CCAA may be employed to provide stability during a period of necessary financial and operational restructuring - and if a restructuring of the "old company" is

not feasible, then there is the exploration of the feasibility of the sale of the operations/enterprise as a going concern (with continued employment) in whole or in part. *Re Stelco Inc*, *supra*, at para. 1.

40 I accept these submissions as being general statements of the law in Ontario. The value of equity in an insolvent debtor is dubious, at best, and, in my view, it follows that the determining factor should not be whether the business continues under the debtor's stewardship or under a structure that recognizes a new equity structure. An equally important factor to consider is whether the case can be made to continue the business as a going concern.

41 Counsel to the Applicants also referred to decisions from the courts in Quebec, Manitoba and Alberta which have similarly recognized the court's jurisdiction to approve a sale of assets during the course of a CCAA proceeding. *Boutiques San Francisco Inc., Re* (2004), 7 C.B.R. (5th) 189 (C.S. Que.), *Winnipeg Motor Express Inc., Re* (2008), 49 C.B.R. (5th) 302 (Man. Q.B.) at paras. 41, 44, and *Calpine Canada Energy Ltd., Re* (2007), 35 C.B.R. (5th) 1 (Alta. Q.B.) at para. 75.

42 Counsel to the Applicants also directed the court's attention to a recent decision of the British Columbia Court of Appeal which questioned whether the court should authorize the sale of substantially all of the debtor's assets where the debtor's plan "will simply propose that the net proceeds from the sale...be distributed to its creditors". In *Cliffs Over Maple Bay Investments Ltd. v. Fisgard Capital Corp.* (2008), 46 C.B.R. (5th) 7 (B.C. C.A.) ("*Cliffs Over Maple Bay*"), the court was faced with a debtor who had no active business but who nonetheless sought to stave off its secured creditor indefinitely. The case did not involve any type of sale transaction but the Court of Appeal questioned whether a court should authorize the sale under the CCAA without requiring the matter to be voted upon by creditors.

43 In addressing this matter, it appears to me that the British Columbia Court of Appeal focussed on whether the court should grant the requested relief and not on the question of whether a CCAA court has the jurisdiction to grant the requested relief.

44 I do not disagree with the decision in *Cliffs Over Maple Bay*. However, it involved a situation where the debtor had no active business and did not have the support of its stakeholders. That is not the case with these Applicants.

45 The *Cliffs Over Maple Bay* decision has recently been the subject of further comment by the British Columbia Court of Appeal in *Asset Engineering LP v. Forest & Marine Financial Ltd. Partnership*, 2009 BCCA 319 (B.C. C.A.).

46 At paragraphs 24 - 26 of the *Forest and Marine* decision, Newbury J.A. stated:

> 24. In *Cliffs Over Maple Bay*, the debtor company was a real estate developer whose one project had failed. The company had been dormant for some time. It applied for CCAA protection but described its proposal for restructuring in vague terms that amounted essentially to a plan to "secure sufficient funds" to complete the stalled project (Para. 34). This court, per Tysoe J.A., ruled that although the Act can apply to single-project companies, its purposes are unlikely to be engaged in such instances, since mortgage priorities are fully straight forward and there will be little incentive for senior secured creditors to compromise their interests (Para. 36). Further, the Court stated, the granting of a stay under s. 11 is "not a free standing remedy that the court may grant whenever an insolvent company wishes to undertake a "restructuring"...Rather, s. 11 is ancillary to the fundamental purpose of the CCAA, and a stay of proceedings freezing the rights of creditors should only be granted in furtherance of the CCAA's fundamental purpose". That purpose has been described in *Meridian Developments Inc. v. Toronto Dominion Bank* (1984) 11 D.L.R. (4th) 576 (Alta. Q.B.):
>
> > The legislation is intended to have wide scope and allow a judge to make orders which will effectively maintain the status quo for a period while the insolvent company attempts to gain the approval of its creditors for a proposed arrangement which will enable the company to remain in operation for what is, hopefully, the future benefit of both the company and its creditors. [at 580]
>
> 25. The Court was not satisfied in *Cliffs Over Maple Bay* that the "restructuring" contemplated by the debtor would do anything other than distribute the net proceeds from the sale, winding up or liquidation of its business.

> The debtor had no intention of proposing a plan of arrangement, and its business would not continue following the execution of its proposal - thus it could not be said the purposes of the statute would be engaged...
>
> 26. In my view, however, the case at bar is quite different from *Cliffs Over Maple Bay*. Here, the main debtor, the Partnership, is at the centre of a complicated corporate group and carries on an active financing business that it hopes to save notwithstanding the current economic cycle. (The business itself which fills a "niche" in the market, has been carried on in one form or another since 1983.) The CCAA is appropriate for situations such as this where it is unknown whether the "restructuring" will ultimately take the form of a refinancing or will involve a reorganization of the corporate entity or entities and a true compromise of the rights of one or more parties. The "fundamental purpose" of the Act - to preserve the *status quo* while the debtor prepares a plan that will enable it to remain in business to the benefit of all concerned - will be furthered by granting a stay so that the means contemplated by the Act - a compromise or arrangement - can be developed, negotiated and voted on if necessary...

47 It seems to me that the foregoing views expressed in *Forest and Marine* are not inconsistent with the views previously expressed by the courts in Ontario. The CCAA is intended to be flexible and must be given a broad and liberal interpretation to achieve its objectives and a sale by the debtor which preserves its business as a going concern is, in my view, consistent with those objectives.

48 I therefore conclude that the court does have the jurisdiction to authorize a sale under the CCAA in the absence of a plan.

49 I now turn to a consideration of whether it is appropriate, in this case, to approve this sales process. Counsel to the Applicants submits that the court should consider the following factors in determining whether to authorize a sale under the CCAA in the absence of a plan:

> (a) is a sale transaction warranted at this time?
>
> (b) will the sale benefit the whole "economic community"?
>
> (c) do any of the debtors' creditors have a *bona fide* reason to object to a sale of the business?
>
> (d) is there a better viable alternative?

I accept this submission.

50 It is the position of the Applicants that Nortel's proposed sale of the Business should be approved as this decision is to the benefit of stakeholders and no creditor is prejudiced. Further, counsel submits that in the absence of a sale, the prospects for the Business are a loss of competitiveness, a loss of value and a loss of jobs.

51 Counsel to the Applicants summarized the facts in support of the argument that the Sale Transaction should be approved, namely:

> (a) Nortel has been working diligently for many months on a plan to reorganize its business;
>
> (b) in the exercise of its business judgment, Nortel has concluded that it cannot continue to operate the Business successfully within the CCAA framework;
>
> (c) unless a sale is undertaken at this time, the long-term viability of the Business will be in jeopardy;
>
> (d) the Sale Agreement continues the Business as a going concern, will save at least 2,500 jobs and constitutes the best and most valuable proposal for the Business;
>
> (e) the auction process will serve to ensure Nortel receives the highest possible value for the Business;

(f) the sale of the Business at this time is in the best interests of Nortel and its stakeholders; and

(g) the value of the Business is likely to decline over time.

52 The objections of MatlinPatterson and the UCC have been considered. I am satisfied that the issues raised in these objections have been addressed in a satisfactory manner by the ruling of Judge Gross and no useful purpose would be served by adding additional comment.

53 Counsel to the Applicants also emphasize that Nortel will return to court to seek approval of the most favourable transaction to emerge from the auction process and will aim to satisfy the elements established by the court for approval as set out in *Royal Bank v. Soundair Corp.* (1991), 7 C.B.R. (3d) 1 (Ont. C.A.) at para. 16.

Disposition

54 The Applicants are part of a complicated corporate group. They carry on an active international business. I have accepted that an important factor to consider in a CCAA process is whether the case can be made to continue the business as a going concern. I am satisfied having considered the factors referenced at [49], as well as the facts summarized at [51], that the Applicants have met this test. I am therefore satisfied that this motion should be granted.

55 Accordingly, I approve the Bidding Procedures as described in the Riedel Affidavit and the Fourteenth Report of the Monitor, which procedures have been approved by the U.S. Court.

56 I am also satisfied that the Sale Agreement should be approved and further that the Sale Agreement be approved and accepted for the purposes of conducting the "stalking horse" bidding process in accordance with the Bidding Procedures including, without limitation the Break-Up Fee and the Expense Reimbursement (as both terms are defined in the Sale Agreement).

57 Further, I have also been satisfied that Appendix B to the Fourteenth Report contains information which is commercially sensitive, the dissemination of which could be detrimental to the stakeholders and, accordingly, I order that this document be sealed, pending further order of the court.

58 In approving the Bidding Procedures, I have also taken into account that the auction will be conducted prior to the sale approval motion. This process is consistent with the practice of this court.

59 Finally, it is the expectation of this court that the Monitor will continue to review ongoing issues in respect of the Bidding Procedures. The Bidding Procedures permit the Applicants to waive certain components of qualified bids without the consent of the UCC, the bondholder group and the Monitor. However, it is the expectation of this court that, if this situation arises, the Applicants will provide advance notice to the Monitor of its intention to do so.

Motion granted.

End of Document

TAB 7

2016 ABQB 257
Alberta Court of Queen's Bench

Sanjel Corp., Re

2016 CarswellAlta 900, 2016 ABQB 257

In the Matter of the Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36, as amended

In the Matter of the Compromise or Arrangement of Sanjel Corporation, Sanjel Canada Ltd., Terracor Group Ltd., Suretech Group Ltd., Suretech Completions Canada Ltd., Sanjel Energy Services (USA) Inc., Sanjel (USA) Inc., Suretech Completions (USA) Inc., Sanjel Capital (USA) Inc., Terracor (USA) Inc., Terracor Resources (USA) Inc., Terracor Logistics (USA) Inc., Sanjel Middle East Ltd., Sanjel Latin America Limited and Sanjel Energy Services DMCC

B.E. Romaine J.

Heard: April 28, 2016
Judgment: May 16, 2016
Docket: Calgary 1601-03143

Counsel: Chris Simard, Alexis Teasdale, for Sanjel Group

Subject: Insolvency

B.E. Romaine J.:

I. Introduction

1 The Sanjel debtors seek orders approving certain sales of assets generated through a SISP that was conducted prior to the debtors filing under the *Companies' Creditors Arrangement Act*. The proceeds of the sales will be insufficient to fully payout the secured creditor, and will generate no return to unsecured creditors, including the holders of unsecured Bonds.

2 The Trustee of the Bonds challenged the process under which the SISP was conducted, and the use of what he characterized as a liquidating CCAA in this situation. He alleged that the use of the CCAA to effect a pre-packaged sale of the debtors' assets for the benefit of the secured creditor was an abuse of the letter and spirit of the CCAA. He also alleged that bad faith and collusion tainted the integrity of the SISP.

3 After reviewing extensive evidence and hearing submissions from interested parties, I decided to allow the application to approve the sales, and dismiss the application of the Trustee. These are my reasons.

II. Facts

4 On April 4, 2016, the Sanjel Corporation and its affiliates were granted an Initial Order under the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c.C-36, as amended. PricewaterhouseCoopers Inc., ("PWC") was appointed as Monitor of the applicants.

5 Sanjel and its affiliates (the "Sanjel Group" or "Sanjel") provide fracturing, cementing, coiled tubing and reservoir services to the oil and gas industry in Canada, the United States and Saudi Arabia. Sanjel Corporation, the parent company, is a private corporation, the shares of which are owned by the MacDonald Group Ltd. It was incorporated under the *Alberta Business*

Corporations Act in 1980, and its principal executive and registered office is located in Calgary. Four of the other members of the group were incorporated in Alberta, seven in various American states and three in offshore jurisdictions.

6 The sole director of all Canadian and US Sanjel companies resides in Calgary, as do all of the officers of these companies. The affidavit in support of the Initial Order sets out a number of factors relevant to the Sanjel Group's ability to file under the CCAA and that would be relevant to a determination of a Centre of Main Interest ("COMI") of the Sanjel Group. In subsequent Chapter 15 proceedings in the United States, the US Court declared COMI to be located in Canada and the CCAA proceedings to be a "foreign main proceeding." It is clear that the Sanjel Group is a fully integrated business centralized in Calgary.

7 Sanjel Corporation and Sanjel (USA) Inc. are borrowers under a credit agreement (the "Bank Credit Facility") dated April 21, 2015 with a banking syndicate (the "Syndicate") led by Alberta Treasury Branches as agent. The total amount outstanding under the Bank Credit Facility at the time of the CCAA filing was approximately $415.5 million. The Syndicate has perfected security interests over substantially all of the assets of the Sanjel Group, and is the principal secured creditor of the Sanjel Group in these CCAA proceedings.

8 On June 18, 2014, Sanjel Corporation issued US $300 million 7.5% Callable Bonds due June 19, 2019. Interest is payable on the Bonds semi-annually on June 19 and December 19. The Bonds are unsecured. Nordic Trust ASA (the "Trustee") is the trustee under the Bond Agreement.

9 The Sanjel Group has been severely impacted by the catastrophic drop in global oil and gas prices since mid-2014. Over the last 18 months, the Sanjel Group has taken aggressive steps to cut costs, including by reducing staffing levels by more than half. However, by late October, 2015, Sanjel Corporation was in breach of certain covenants under the Bank Credit Facility. By late December, 2016, the Syndicate was in a position to exercise enforcement rights. In addition, an interest payment of USD $11,250,000 was due on the Bonds on December 19, 2015. Since late 2015, the Sanjel Group has been in negotiations with both the Syndicate and two bondholders, Ascribe Capital LLC and Clearlake Capital Group L.P., (the "Ad Hoc Bondholders"). The Ad Hoc Bondholders hold over 45% of the Bonds.

10 In the fall of 2015, Sanjel Corporation engaged Bank of America Merrill Lynch ("BAML") to identify strategic partners and attempt to raise additional capital for the Sanjel Group. BAML contacted 28 private equity firms; 19 non-disclosure agreements were executed and 9 management presentations were made. However, the BAML process did not result in a successful transaction.

11 In December, 2015, the Ad Hoc Bondholders retained a New York law firm, Fried Frank, as their legal advisor and Moelis & Company as their financial advisor.

12 On December 10, 2015, Fried Frank conveyed a proposal from the Ad Hoc Bondholders to Sanjel. Under this proposal, Sanjel would be required to pay the USD $11,250,000 interest payment. Provided that the interest payment was made, the bondholders would agree to a standstill agreement for the same period as may be agreed with the Syndicate. In return, the Ad Hoc Bondholders would lend back their pro rata share of that interest payment to Sanjel in return for secured notes ranking *pari passu* with the Bank Credit Facility, bearing interest at the same rate as the Bank Credit Facility plus 2%. The new notes would not be repaid until the Bank Credit Facility was repaid.

13 The Ad Hoc Bondholders indicated that they would consider acting as standby lenders to Sanjel for the remainder of the interest payment and would offer the other bondholders the option of lending back their pro-rata share to Sanjel on the same basis. If they agreed to be standby lenders, the Ad Hoc Bondholders would receive a commitment fee equal to 10% of their standby commitment, payable in new notes.

14 The proposal letter indicated that the Ad Hoc Bondholders were aware that Sanjel had been engaged in a process to address liquidity and leverage issues over the past few months, including attempting to raise equity to sell assets. In their view, Sanjel had exhausted those efforts, and the only remaining option was a deal negotiated with the bondholders. However, the Ad Hoc Bondholders would only embark on such a process if the December 19, 2015 interest payment was made.

15 Sanjel rejected the proposal on December 14, 2015. It is noteworthy that the Bank Credit Facility includes a negative covenant prohibiting Sanjel from granting a security interest over its assets. The Syndicate advised Sanjel that the Ad Hoc Bondholders' proposal to have their existing unsecured position elevated to rank *pari passu* with the Bank Credit Facility was unacceptable, and that it would not provide its consent.

16 On December 15, 2015, the Ad Hoc Bondholders advised counsel to the Syndicate that they wished to work towards a restructuring, which they envisaged would involve paying down a portion of the Syndicate's debt "in an amount to be mutually agreed on". They also suggested that Sanjel would implement a rights offering to holders of Bonds and then to existing equity, with a conversion of the Bonds into new debt and equity.

17 On or about December 15, 2015, the Ad Hoc Bondholders sent Sanjel a draft waiver and standstill agreement, which required the payment of part of the December 19 interest payment by December 23, 2015 and the payment of the fees and disbursements of Fried Frank and Moelis in return for arranging for a bondholder meeting to be called to consider a period of forbearance to March 31, 2016.

18 Fried Frank and Moelis executed Non-Disclosure Agreements ("NDAs") on December 24, 2015, but the Ad Hoc Bondholders did not, thus not restricting their right to trade the Bonds. Fried Frank and Moelis were granted access to a Sanjel virtual database ("VDR") on January 9, 2016.

19 By January, 2016, given the prolonged downturn in oil and gas prices, Sanjel's liquidity was limited. Events of default under the Bank Credit Facility that had occurred as of October 31, 2015 were exacerbated by a cross-default based on the non-payment of interest under the Bond Agreement. As of January 31, 2016, the Sanjel Group had total consolidated liabilities of approximately $1.064 billion.

20 Sanjel was facing very significant negative cash flow projections over the next few months. As of early January, 2016, Sanjel's projected cash flows showed that its cash position would deteriorate by more than half as of the first week of April, 2016, and would be further reduced by anticipated forbearance payments.

21 In the circumstances, Sanjel agreed with the Syndicate to implement a Sales and Investment Solicitation Process ("SISP"). Sanjel states that it hoped that if a SISP was implemented, it might find a transaction that preserved the business as a going concern, which would maximize stakeholder value and preserve goodwill and jobs.

22 In mid-January, 2016, Sanjel engaged PWC as a proposed Monitor in the event it would become necessary to file under the CCAA.

23 The SISP was commenced on behalf of Sanjel by its financial advisors, PJT Partners Inc. ("PJT") and Credit Suisse Securities (CANADA), Inc. ("CS") on January 17, 2016. The advisors contacted prospective bidders, many of whom had already been identified through the BAML process of late 2015.

24 The process of soliciting non-bidding indications of interest ran from January 17, 2016 to February 22, 2016. On January 26, 2016, the advisers updated and opened a VDR available to anyone who had signed a NDA. A teaser letter was distributed and meetings and conference calls were held with bidders. A process letter was distributed on January 28, 2016. Nine indications of interest were submitted on or about February 22, 2016.

25 Before and during the SISP process, Sanjel was negotiating with both the Syndicate and the Ad Hoc Bondholders with respect to separate forbearance agreements, and with the Ad Hoc Bondholders with respect to NDAs to be signed by the Ad Hoc Bondholders. The Ad Hoc Bondholders complain that there was a delay of almost a month before Sanjel's counsel responded to a mark-up of a NDA provided by Fried Frank, but negotiations were stymied by the Ad Hoc Bondholders' insistence that the December interest payment be paid. Until this issue was settled, there was no reason to finalize the NDAs. In addition, it was not until January 29, 2016 that representatives of the Ad Hoc Bondholders advised Sanjel that they were prepared to be restricted

from trading and therefore able to receive confidential information. During this period of time, the Ad Hoc Bondholders refused to meet with Sanjel management when they travelled to New York on January 20, 2016.

26 On February 1, 2016, counsel to Sanjel sent counsel to the Ad Hoc Bondholders a copy of the draft forbearance agreement between the Syndicate and Sanjel, which set out the key dates of the SISP, including the completion of definitive purchase and sales agreements by March 24, 2016. It would have been clear to the Ad Hoc Bondholders from this draft that Sanjel was proceeding on a dual track basis, considering both a potential stand-alone restructuring of the company and a sales process.

27 The Ad Hoc Bondholders made a second proposal to Sanjel on February 2, 2016, very shortly after the NDAs were signed. This proposal involved the Syndicate recovering a portion of its loan from Sanjel's existing cash reserves and a rights offering backstopped by the Ad Hoc Bondholders. A portion of the Bonds would be converted into equity. The December interest payment would have to be paid. Sanjel's management team met with the Ad Hoc Bondholders and their advisors in New York on February 3, 2016 and Sanjel's team, the Syndicate and its advisors and the Ad Hoc Bondholders met on February 8, 2016.

28 Sanjel delivered an indicative restructuring term sheet to the Ad Hoc Bondholders on February 12, 2016, as required by the forbearance agreement that the parties were negotiating. The restructuring term sheet emphasized that a bondholder-led restructuring would require significant new money, a significant capital commitment and ongoing capital, with a significant pay-down of the Syndicate's debt.

29 Commencing on February 15, 2016, Sanjel allowed representatives of Alverez and Marsal ("A&M"), advisors to the Ad Hoc Bondholders, to attend in Calgary and conduct due diligence.

30 On February 18, 2016, Sanjel uploaded to its VDR the final, unsigned versions of the Syndicate Amending and Forbearance Agreement and the Bondholders Forbearance Agreement.

31 Under the SISP, preliminary, non-binding indications of interest were delivered to the advisors and the company by February 22, 2016. Six such indications of interest were received, all of which were materially superior to the Ad Hoc Bondholders proposal of February 2, 2016. The Ad Hoc Bondholders have admitted that they were aware of the milestones under the SISP and the Bank Forbearance Agreement by mid-February, 2016, although it is clear that their advisors would have been aware of these milestones from February 1, 2016.

32 As part of finalizing the form of Bond Forbearance Agreement, counsel for Sanjel and for the Ad Hoc Bondholders had negotiated a form of summons that would be used to call a bondholder meeting to consider the agreement. The only item for consideration to be considered at the meeting was to be the Bond Forbearance Agreement. The plan was to have 2/3 of the bondholders approve and execute the Bond Forbearance Agreement, and then to hold a bondholders meeting.

33 Instead, on February 25, 2016, the Ad Hoc Bondholders caused the Trustee to issue a summons for a meeting on March 10, 2016 to consider and vote on a) whether to declare the Bonds in default, accelerate them and exercise remedies, including commencing involuntary bankruptcy proceedings against Sanjel under Chapter 11 of the *United States Bankruptcy Code*, including claims against the MacDonald family and MacBain Properties Ltd., which owns the business premises that are leased by the Sanjel Group or b) approve the Bond Forbearance Agreement.

34 On March 2, 2016, the Ad Hoc Bondholders submitted a restructuring proposal to Sanjel. This proposal provided no cash recovery to the Syndicate. Instead, a portion of the debt owed to the Syndicate would be converted to a new loan and the remainder extinguished, with the Syndicate receiving warrants in a reorganized company. There would be a Chapter 11 filing and the bondholders would provide a debtor-in-possession ("DIP") facility to rank *pari passu* with the Syndicate debt. Bondholders who contributed to the DIP would receive new 2nd lien notes for part of their previous notes, the remainder being extinguished. The DIP facility would be converted into 100% of the equity of the reorganized company. Sanjel would be required to appoint a Chief Restructuring Officer ("CRO") designated by the Ad Hoc Bondholders.

35 On March 4, 2016, in a follow-up letter to a telephone meeting on March 3, 2016, US counsel to the Syndicate wrote to Fried Frank requesting that the March 10 bondholders meeting be adjourned to March 31, 2016. Canadian counsel to Sanjel made the same request of the Trustee.

36 Also on March 4, 2016, a template Asset Purchase Agreement ("APA") for SISP bidders was posted on the VDRs, which disclosed a CCAA/Chapter 15 filing with PWC as designated Monitor. This template agreement was available to the Ad Hoc Bondholders and their advisors.

37 Counsel for the Ad Hoc Bondholders replied on March 5, 2016 that they would advise the Trustee to postpone the March 10 meeting subject to:

a) a response to their March 2 proposal by March 10, 2016;

b) full disclosure of company records for A&M's representative, "so that [that representative] is ready and best positioned to commence his duties as Chief Restructuring Officer for the Company".

c) payment by March 7, 2016 of roughly USD $2.2 million in fees and disbursements for the Ad Hoc Bondholders' legal and financial advisors.

38 After some negotiation, Sanjel agreed to these terms for an adjournment, other than with respect to a small deduction in fees and disbursements. Sanjel made it clear that it reserved all rights with respect to the appointment of a CRO and a filing under Chapter 11, which it would not agree to at that time. On March 8, 2016 the Trustee confirmed that the meeting would be postponed to March 31.

39 On March 9, 2016, second round bids under the SISP were received. Five bids were received, all of which were materially superior to the Ad Hoc Bondholders' March 2, 2016 proposal in terms of cash recovery for the Syndicate.

40 An information update conference for bondholders was scheduled to be held on March 11, 2016, at which Sanjel, the Trustee and the Ad Hoc Bondholders would provide an update to any bondholder that wished to call in. This was rescheduled by the Trustee to March 31, 2016.

41 On March 11, 2016, the Syndicate sent the counter-offer required by the postponement of meeting agreement to the Ad Hoc Bondholders. This counter-proposal made it clear that there would be a CCAA/Chapter 15 process, rather than a Chapter 11 process. While this counter-proposal is confidential, it is fair to say that the parties were far apart in their negotiations, particularly with respect to treatment of the Syndicate indebtedness.

42 Also on March 11, 2016, a representative of Sanjel met with A&M's representative and discussed Sanjel's intention to disclaim certain leases in the anticipated CCAA proceedings.

43 Following receipt of the second round bids, Sanjel and its advisors identified the top three bidders and began negotiations with them with the goal of finalizing due diligence and being in a position to execute final APAs on March 24, 2016, as indicated in the Bank Forbearance Agreement.

44 In the meantime, Sanjel continued meetings with the A&M representative, who asked for, and was provided with:

a) access to the newly created VDR for second stage bidders/investors in the SISP on March 12, 2016.

b) draft materials relating to the CCAA filing, including current drafts of cash flow projections and drafts of stakeholder communication regarding the CCAA, on March 21, 2016.

45 On March 20, 2016, the Ad Hoc Bondholders provided Sanjel and the Syndicate with a third restructuring proposal. This one provided for some paydown of the Syndicate's debt, but involved less than half of that recovery in new money, about the same amount in debt secured by accounts receivable and a substantial amount of bank debt rolled over into a new loan. It also

provided for a DIP facility to rank *pari passu* with a new bank credit facility in the event of a liquidation and the conversion of some bondholder debt into secured notes.

46 On March 23, 2016, counsel for Sanjel requested that the Trustee postpone the bondholder meeting scheduled for March 31, 2016 to April 14, 2016. He also proposed to set up the requested informational update on March 31, 2016. On March 25, 2016, counsel for the Trustee consented to this request.

47 In the SISP, final bids were received from the three top bidders on March 24, 2016, with negotiations to continue on final APAs. On the same day, Sanjel and its advisors hosted a call with A&M and Moelis, during which they walked through a 13 week cash forecast.

48 On March 31, 2016 the Syndicate and the Ad Hoc Bondholders had discussions with respect to the Ad Hoc Bondholders' March 20 proposal. In previous correspondence, the Syndicate's counsel had questioned the adequacy of the proposed DIP financing in the proposal and noted Sanjel's significant cash needs following exit from an insolvency proceeding, as opposed to the proposal's assumption that there would be better cash flow. At the conclusion of the call, the Ad Hoc Bondholders indicated that they would provide further modelling with respect to their proposal.

49 On April 3, 2016, Sanjel entered into final APAs with the proposed purchasers, STEP and Liberty. On April 4, 2016, the Sanjel Group filed for CCAA protection. Counsel for Sanjel Group disclosed that the application was made without notice to the Ad Hoc Bondholders He submitted that notice would imperil the CCAA proceedings as the bondholders may, with notice, have pre-empted the CCAA filing by an involuntary filing under Chapter 11. There is no requirement to give notice to unsecured creditors of a CCAA filing. There are circumstances, and this was one of them, where it is appropriate to seek an initial order on an ex parte basis:

> This may be an appropriate — even necessary — step in order to prevent "creditors from moving to realize on their claims, essentially a 'stampede to the assets' once creditors learn of the debtor's financial distress": J.P. Sarra, *Rescue! The Companies' Creditors Arrangement Act* (2007), at p. 55 ("Rescue!"); see also *Algoma Steel Inc , Re* (2001), 25 C.B.R. (4th) 194 (Ont. C.A.), at para. 7

50 On April 11, 2016, the Ad Hoc Bondholders presented their fourth proposal for restructuring, not to Sanjel but to the Syndicate. This proposal increases the amount the bondholders would contribute to Sanjel for new equity, which would be used to repay a portion of the Syndicate's loan.

51 According to Fried Frank, the Syndicate's counsel responded on April 13, 2016 advising that while they appreciated the work done by the Ad Hoc Bondholders, the Syndicate preferred the sale route. The Syndicate proposed alternatives that it might consider involving a higher pay-out of the Syndicate's debt than offered by the April 11, 2016 proposal. The Ad Hoc Bondholders have not responded.

52 The Sanjel Group apply for an order approving the sales transactions generated through the SISP, being a sales agreement between Sanjel and STEP Energy Services Ltd., including an assignment of the sale of the debtor's cementing assets in favour of 1961531 Alberta Ltd., and a sales agreement between Sanjel and Liberty.

53 The Trustee applied for an order dismissing the application for approval of these transactions, allowing the Ad Hoc Bondholders to propose a plan of arrangement, lifting the stay to allow the Trustee to commence a Chapter 11 filing and directing a new Court-monitored SISP, among other applications

III. Applicable Law

54 Section 36(3) of the CCAA sets out six non-exhaustive factors that must be considered in approving a sale by a CCAA debtor of assets outside the ordinary course of business. They are:

(a) whether the process leading to the proposed sale was reasonable in the circumstances;

(b) whether the Monitor approved the process leading to the proposed sale;

(c) whether the Monitor filed with the court a report stating that in its opinion the sale would be more beneficial to creditors than a sale or disposition under a bankruptcy;

(d) the extent to which the creditors were consulted;

(e) the effects of the proposed sale on creditors and other interested parties; and

(f) whether the consideration to be received for the assets is reasonable and fair, taking into account their market value.

55 In this case, the Monitor was not in place at the time of the process leading to the proposed sales, nor at the time the SISP was commenced. However, the Monitor has given an opinion on the process, which I will consider as part of my review.

56 Prior to the enactment of section 36, CCAA courts considered what are known as the Soundair principles in considering approval application, and they are still useful guidelines:

a) Was there a sufficient effort made to get the price at issue? Did the debtor company act improvidently?

b) Were the interests of all parties considered?

c) Are there any questions about the efficacy and integrity of the process by which offers were obtained?

d) Was there unfairness in the working out of the process?

Royal Bank v Soundair, 1991 Carswell Ont (Ont CA) at para 20.

57 Gascon, J. (as he then was) suggested in *Re AbitibiBowater, Inc*, 2010 QCCS 1742 (C.S. Que) at paras 70-72 that a court should give due consideration to two further factors:

a) the business judgment rule, in that a court will not lightly interfere with the exercise of the commercial and business judgment of the debtor company and the monitor in the context of an asset sale where the marketing and sale process was fair, reasonable, transparent and efficient; and

b) the weight to be given to the recommendation of the monitor.

58 As noted by Gascon, J., it is not desirable for a bidder to wait to the last minute, even up to a court approval stage, to submit its best offer. However, a court can consider such an offer, if it is evidence that the debtor company did not properly carry out its duty to obtain the best price for creditors.

IV. Analysis

59 The Trustee has raised a number of objections to the proposed sales, many of which relate to the factors and principles set out in section 36 of the CCAA, the Soundair principles and the AbitibiBowater factors:

A. The Trustee submits that the CCAA can only be used to liquidate the assets of a debtor company and distribute the proceeds where such use is uncontested or where there is clear evidence that the CCAA provides scope for greater recoveries than would be available on a bankruptcy.

60 Most of the cases relied upon by the Trustee with respect to this submission predate the 2009 enactment of section 36 of the CCAA. While prior to this change to the CCAA, there was some authority that questioned whether the CCAA should be used to carry out a liquidation of a debtors' assets, there was also authority that accepted this as a proper use of the statute.

61 An analysis of the pre-section 36 state of the law on this issue, and support for the latter view, is well summarized in *Re Nortel Networks Corp.*, [2009] O.J. No. 3169. As noted by Morawetz, J. at para 28 of that decision, the CCAA is a flexible statute, particularly useful in complex insolvency cases in which the court is required to balance numerous constituents and myriad interests. This is such a case.

62 Section 36 now provides that a CCAA court may authorize the sale or disposition of assets outside the ordinary course of business if authorized to do so by court order. There is thus no jurisdictional impediment to the sale of assets where such sales meet the requisite tests, even in the absence of a plan of arrangement.

63 Morawetz, J in *Re Target Canada Co.*, 2015 ONSC 303 at paras 32 and 33, describes the change brought about by section 36:

> Prior to the 2009 amendments to the CCAA, Canadian courts accepted that, in appropriate circumstances, debtor companies were entitled to seek the protection of the CCAA where the outcome was not going to be a going concern restructuring, but instead, a "liquidation" or wind-down of the debtor companies' assets or business.
>
> The 2009 amendments did not expressly address whether the CCAA could be used generally to wind-down the business of a debtor company. However, I am satisfied that the enactment of section 36 of the CCAA, which establishes a process for a debtor company to sell assets outside the ordinary course of business while under CCAA protection, is consistent with the principle that the CCAA can be a vehicle to downsize or wind-down a debtor company's business.
>
> See also *Re Brainhunter Inc.*, 2009 CarswellOnt 8207 at para 15.

64 Whether before or after the enactment of section 36, Canadian courts have approved en bloc sales of a debtor company, recognizing that such sales are consistent with the broad remedial purpose and flexibility of the CCAA.

65 What the provisions of the CCAA can provide in situations such as those facing the Sanjel Group is a court-supervised process of the execution of the sales, with provision for liquidity and the continuation of the business through the process provided by interim financing, a Key Employee Retention Plan that attempts to ensure that key employees are given an incentive to ensure a seamless transition, critical supplier relief that keeps operations functioning pending the closing of the sales and a process whereby a company with operations in Canada, the United States and internationally is able to invoke the aid of both Canadian and US courts during the process. It is true that the actual SISP process preceded the CCAA filing, and I will address that factor later in this decision.

66 As counsel to the Sanjel Group notes, this type of insolvency proceeding is well-suited to the current catastrophic downturn of the economy in Alberta, with companies at the limit of their liquidity. It allows a business to be kept together and sold as a going concern to the extent possible. There have been a number of recent similar filings in this jurisdiction: the filing in Southern Pacific and Quicksilver are examples.

67 The Monitor supports the sales, and is of the view, supported by investigation into the likely range of forced sale liquidation recoveries with financial advisors and others with industry knowledge, that a liquidation of assets would not generate a better result than the consideration contemplated by the proposed sales. The Monitor's investigations were hampered by the lack of recent sales of similar businesses, but I am satisfied by its thorough report that the Monitor's investigation of likely recoveries is the best estimate available. A CS estimate provided a different analysis, but I am satisfied by the evidence that it has little probative value.

68 In summary, this is not an inappropriate use of the CCAA arising from the nature of the proposed sales.

B. The Trustee submits that the proposed sales are the product of a defective SISP conducted outside of the CCAA.

69 It is true that the SISP, and the restructuring negotiations with the Ad Hoc Bondholders, took place prior to the filing under the CCAA, that this was a "pre-pack" filing.

70 A pre-filing SISP is not of itself abusive of the CCAA. Nothing in the statute precludes it. Of course, a pre-filing SISP must meet the principles and requirements of section 36 of the CCAA and must be considered against the Soundair principles. The Trustee submits that such a SISP should be subject to heightened scrutiny. It may well be correct that a pre-filing SISP will be subject to greater challenges from stakeholders, and that it may be more difficult for the debtor company to establish that it was conducted in a fair and effective manner, given the lack of supervision by the Court and the Monitor, who as a court officer has statutory duties.

71 Without prior court approval of the process, conducting a SISP outside of the CCAA means that both the procedure and the execution of the SISP are open to attack by aggrieved stakeholders and bitter bidders, as has been the case here. Any evidence or reasonable allegations of impropriety would have to be investigated carefully, whereas in a court-approved process, comfort can be obtained through the Monitor's review and the Court's approval of the process in advance. However, in the end, it is the specific details of the SISP as conducted that will be scrutinized.

72 Similar issues were considered in *Re Nelson Education Ltd.*, 2015 ONSC 5557 at paras 31-32, and in *Re Bloom Lake*, [p.1], 2015 QCCS 1920 at para 21.

73 The Trustee submits that the SISP was defective in that its timelines were truncated and that it was destined not to generate offers that maximized value for all stakeholders. The Trustee filed an affidavit of a representative of Moelis indicating that it would be typical in a SISP to establish a deadline for non-binding offers one or two months following commencement of the process, while in this SISP, participants had only 12 to 25 days to evaluate the business and provide non-binding indications of interest. This opinion did not address the previous BAML process that identified likely purchasers and thus lengthened the review process for these parties who participated in the first process. The Trustee's advisor was also critical that the SISP provided only 16 days for final offers, suggesting that it is more typical to provide two months.

74 While likely correct for normal-course SISP's, this analysis does not take into account the high cash burn situation of these debtors, nor the deteriorating market. The Moelis opinion suggests that potential purchaser would have a heightened diligence requirement in the current unfavourable market conditions, requiring extra time for due diligence. However, despite the speed of the SISP, it appears to have generated a range of bids significantly above liquidation value. The process was not limited to the SISP, but included the previous BAML process and the negotiations with the Ad Hoc Bondholders.

75 The evidence discloses a thorough and comprehensive canvassing of the relevant markets for the debtors and their assets despite the aggressive timelines. The BAML process identified some interested parties and Sanjel's financial advisors built on that process by re-engaging with 28 private equity firms that had already expressed interest in these unique assets as well as identifying new potential purchasers, reaching out to 85 potential buyers.

76 Of those 85 parties, 37 executed NDAs, 25 conducted due diligence and 17 met with the management team. Eight submitted non-binding indications of interest, five were invited to submit second-round bids and finally the top three were chosen for the continuation of negotiations to final agreements.

77 While some interested parties may have found the time limits challenging, a reasonable number were able to meet them and submit bids. I am satisfied from the evidence that, despite a challenging economic environment, the process was competitive and robust.

78 I also note the comments of the Monitor in its First Report dated April 12, 2016. While it was not directly involved in the SISP, the Monitor reports that the financial advisors advised the Monitor, that given the size and complexity of the Sanjel Group's operations and the time frames involved, all strategic and financial sponsors known to the advisors were contacted during the SISP and that it is unlikely that extending the SISP time frames in the current market would have resulted in materially better offers.