

**CITATION:** Prizm Income Fund (Re), 2011 ONSC 2061  
**COURT FILE NO.:** CV-11-915900CL  
**DATE:** 20110331

**SUPERIOR COURT OF JUSTICE - ONTARIO**

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

**AND:**

IN THE MATTER OF A PLAN OF COMPROMISE OR ARRANGEMENT OF  
PRIZM INCOME FUND, PRIZM CANADIAN OPERATING TRUST,  
PRIZM INC. AND KIT FINANCE INC., Applicants

**BEFORE:** MORAWETZ J.

**COUNSEL:** A. J. Taylor and M. Konyukhova, for the Prizm Entities

G. Finlayson, Conflict Counsel for the Prizm Entities

M. Wasserman, for FTI Consulting Canada Inc., Proposed Monitor

P. Shea, for Prudential Insurance

P. Huff, for Directors of Prizm

C. Cosgriffe, for Yum! Restaurants International (Canada) LP

D. Ullmann, for 2279549 Ontario Inc. (Chief Restructuring Officer)

**HEARD:** MARCH 31, 2011

**ENDORSEMENT**

[1] Prizm Income Fund ("Prizm Fund"), Prizm Canadian Operating Trust ("Prizm Trust"), Prizm Inc. ("Prizm GP") and KIT Finance Inc. ("KIT Finance") (collectively, the "Applicants") seek relief under the *Companies' Creditors Arrangements Act*, R.S.C. 1985, c. C-36 (the "CCAA"). The Applicants also seek to have the stay of proceedings and other benefits of an initial order under the CCAA extended to Prizm Limited Partnership ("Prizm LP"). Prizm Fund, Prizm Trust, Prizm GP, Prizm LP and KIT Finance are collectively referred to as the "Prizm Entities".

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## BACKGROUND

[2] The Prizm Entities own and operate 428 KFC, Taco Bell and Pizza Hut restaurants in seven provinces across Canada. As a result of declining sales and the inability to secure additional or alternate financing, the Prizm Entities cannot meet their liabilities as they come due and are therefore insolvent.

[3] The Prizm Entities seek a stay of proceedings under the CCAA to allow them to secure a going concern solution for the business including approximately 6,500 employees and numerous suppliers, landlords and other creditors and to maximize recovery for the Prizm Entities' stakeholders.

[4] On the return of the motion, the only party that took issue with the proposed relief was Yum! Restaurants International (Canada) LP (the "Franchisor"). Counsel to the Franchisor indicated that the Franchisor was not opposing the form of order, but explicitly does not consent to the stated intention of the Prizm Entities not to pay franchise royalties to the Franchisor.

[5] The background facts with respect to this application are set out in the Affidavit of Deborah J. Papernick, sworn March 31, 2011 (the "Papernick Affidavit"). Further details are also contained in a pre-filing report submitted by FTI Consulting Canada Inc. ("FTI") in its capacity as proposed monitor. FTI has been acting as financial advisor to the Prizm Entities since December 13, 2010.

[6] Prizm LP is a franchisee of the Franchisor and is Canada's largest independent quick service restaurant operator. Prizm LP is the largest operator of the KFC concept in Canada, accounting for approximately 60% of all KFC product sales in Canada. In addition, Prizm LP operates a number of multi-branded restaurants that combine a KFC restaurant with either a Taco Bell or a Pizza Hut restaurant.

[7] As of March 25, 2011, the Prizm Entities operated 428 restaurants in seven provinces: British Columbia, Alberta, Manitoba, Ontario, Quebec, Nova Scotia and New Brunswick.

[8] The business of Prizm LP is to develop, acquire, make investments in and conduct the business and ownership, operation and lease of assets and property in connection with the quick service restaurant business in Canada.

[9] Prizm Fund is an income trust indirectly holding approximately 60% of Prizm LP's trust units.

[10] Prizm Trust is an unincorporated, limited purpose trust wholly-owned by Prizm Fund created to acquire and hold 60% of the outstanding partnership units of Prizm LP, as well as approximately 60% of Prizm GP's units, for Prizm Fund.

[11] Prizm GP is a corporation which acts as general partner of Prizm LP.

[12] KIT Finance is a corporation created to act as borrower for the Prudential Loan, described below.

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[13] The principal and head offices of Prizm Fund, Prizm LP and Prizm GP are located in Vaughan, Ontario.

[14] As at March 31, 2011, the Prizm Entities had short-term and long-term indebtedness totalling: \$98.8 million pursuant to the following instruments:

- (a) Note purchase and private shelf agreement dated January 12, 2006 ("Note Purchase Agreement") between KIT Finance, Prizm GP and Prudential Investment Management ("Prudential") - \$67.3 million;
- (b) Subordinated Debentures issued by Prizm Fund due June 30, 2012 - \$30 million - \$31.5 million.

[15] The indebtedness under the Note Purchase Agreement (the "Prudential Loan") is guaranteed by and secured by substantially all of the assets of Prizm GP, KIT Finance and Prizm LP and by limited recourse guarantees and pledge agreements granted by Prizm Fund and Prizm Trust.

[16] In addition, the Prizm Entities have approximately \$39.1 million of accrued and unpaid liabilities.

[17] As a result of slower than forecast sales, on September 5, 2010, Prizm Fund breached the Prudential Financial covenant and remains in non-compliance. As a result, the Prudential Loan became callable.

[18] Prizm Fund has also failed to make an interest payment of \$975,000 due on December 31, 2010 in respect to the Subordinated Debentures.

[19] The Prizm Entities have also ceased paying certain obligations to the Franchisor as they come due.

## FINDINGS

[20] I am satisfied that Prizm GP and KIT Finance are "companies" within the definition of the CCAA. I am also satisfied that Prizm Fund and Prizm Trust fall within the definition of "income trust" under the CCAA and are "companies" to which the CCAA applies.

[21] I am also satisfied that the Prizm Entities are insolvent. In arriving at this determination, I have considered the definition of "insolvent" in the context of the CCAA as set out in *Re Stelco Inc.* (2004), 48 C.B.R. (4<sup>th</sup>) 299 (Ont. S.C.J.), leave to appeal refused, 2004 CarswellOnt 2936, leave to appeal to S.C.C. refused 2004 CarswellOnt. 5200. In *Stelco*, Farley J. applied an expanded definition of insolvent in the CCAA context to reflect the "rescue" emphasis of the CCAA, modifying the definition of "insolvent person" within the meaning of s. 2(1) of the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3 ("BIA") to include a financially troubled corporation that is "reasonably expected to run out of liquidity within reasonable proximity of time as compared with the time reasonably required to implement a restructuring".

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[22] In this case, the Prizm Entities are unable to meet their obligations to creditors and have ceased paying certain obligations as they become due.

[23] Further, the Prizm Entities are affiliated debtor companies with total claims against in excess of \$100 million.

[24] I accept the submission put forth by counsel to the Applicants to the effect that the Applicants are "debtor companies" to which the CCAA applies.

[25] At the present time, the Prizm Entities are in the process of coordinating a sale process for certain assets. In these circumstances, I have been persuaded that a stay of proceedings is appropriate. In arriving at this determination, I have considered *Re Lehndorff General Partner Ltd.* (1993), 17 C.B.R. (3<sup>rd</sup>) 24 (Ont. Gen. Div.) and *Nortel Networks Corporation (Re)* [2009] O.J. No. 3169 (S.C.J.).

[26] The CCAA definition of an eligible company does not expressly include partnerships. However, CCAA courts have exercised their inherent jurisdiction to stay proceedings with respect to partnerships and limited partnerships where it is just inconvenient to do so. See *Lehndorff, supra*, and *Re Canwest Global Communications Corp.*, 2009 CarswellOnt 6184 (S.C.J.).

[27] The courts have held that this relief is appropriate where the operations of the debtor companies are so intertwined with those of the partnerships or limited partnerships in question, that not extending the stay would significantly impair the effectiveness of a stay in respect of the debtor companies.

[28] Having reviewed the affidavit of Ms. Papernick, I have been persuaded that it is appropriate to extend CCAA protection to Prizm LP.

[29] The Prizm Entities are also seeking an order: (a) declaring certain of their suppliers to be critical suppliers within the meaning of the CCAA; (b) requiring such suppliers to continue to supply on terms and conditions consistent with existing arrangements and past practice as amended by the initial order; (c) granting a charge over the Property as security for payment for goods and services supplied after the date of the Initial Order.

[30] Section 11.4 of the CCAA provides the court jurisdiction to declare a person to be a critical supplier. The CCAA does not contain a definition of "critical supplier" but pursuant to 11.4(1), the court must be satisfied that the person sought to be declared a critical supplier "is a supplier of goods or services to the company and that the goods or services that are supplied are critical to the company's continued operations".

[31] Counsel submits that the Prizm Entities' business is virtually entirely reliant on their ability to prepare, cook and sell their products and that given the perishable nature of their products, the Prizm Entities maintain very little inventory and rely on an uninterrupted flow of deliveries and continued availability of various products. In addition, the Prizm Entities are highly dependent on continued and timely provision of waste disposal and information technology services and various utilities.

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[32] With the assistance of the proposed monitor, the Prizm Entities have identified a number of suppliers which are critical to their ongoing operation and have organized these suppliers into five categories:

- (a) chicken suppliers;
- (b) other food and restaurant consumables;
- (c) utility service providers;
- (d) suppliers of waste disposal services;
- (e) providers of appliance repair and information technology services.

[33] A complete list of the suppliers considered critical by the Prizm Entities (the "Critical Suppliers") is attached at Schedule "A" to the proposed Initial Order.

[34] Having reviewed the record, I have been satisfied that any interruption of supply by the Critical Suppliers could have an immediate material adverse impact on the Prizm Entities business, operations and cash flow such that it is, in my view, appropriate to declare the Critical Suppliers as "critical suppliers" pursuant to the CCAA.

[35] Further, I accept the submission of counsel to the Prizm Entities that it is appropriate to grant a Critical Suppliers' Charge to rank behind the Administrative Charge.

[36] The Prizm Entities also seek approval of the DIP Facility in the amount up to \$3 million to be secured by the DIP Lenders' Charge.

[37] Subsection 11.2(4) of the CCAA sets out the factors to be considered by the court in deciding whether to grant a DIP Financing Charge. These factors include:

- (a) the period during which the company is expected to be subject to proceedings under the CCAA;
- (b) how the company's business and financial affairs are to be managed during the proceedings;
- (c) whether the company's management has the confidence of its major creditors;
- (d) whether the loan would enhance the prospects of a viable compromise or arrangement being made in respect of the company;
- (e) the nature and value of the company's property;
- (f) whether any creditor would be materially prejudiced as a result of the security or charge; and
- (g) the monitor's report.

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[38] Counsel submits that the following factors support the granting of the DIP Lenders' Charge:

- (a) the Prizm Entities expect to continue daily operations during the proceedings;
- (b) management will be overseen by the monitor who will oversee spending under the DIP Financing;
- (c) while it is not anticipated that the Prizm Entities will require any additional financing prior to June 30, 2011, actual funding requirements may vary;
- (d) the ability to borrow funds from a court-approved DIP Facility will be crucial to retain the confidence of stakeholders;
- (e) secured creditors have either been given notice of the DIP Lenders' Charge or are not affected by it;
- (f) the DIP Lenders' Charge does not secure an obligation that existed before the granting of the Initial Order; and
- (g) the proposed monitor is supportive of the DIP Facility and the DIP Lenders' Charge.

[39] Based on the foregoing, I am of the view that it is appropriate to approve the DIP Facility and grant the DIP Lenders' Charge.

[40] The trustees and directors of the Prizm Entities have stated their intention to resign. In order to ensure ongoing corporate governance, the Prizm Entities seek an order appointing 2279549 Ontario Inc. as the CRO. They have also requested that the Chief Restructuring Officer be afforded the protections outlined in the draft Initial Order.

[41] The Applicants are seeking an Administration Charge over the property in the amount of \$1.5 million to secure the fees of the proposed monitor, its counsel, counsel to the Prizm Entities and the CRO. It is proposed that this charge will rank in priority to all other security interests in the Prizm assets, other than any "secured creditor", as defined in the CCAA, who has not received notice of the application for CCAA protection.

[42] The authority to provide such a charge is set out in s. 11.5(2) of the CCAA.

[43] The Prizm Entities submit that the following factors support the granting of the Administration Charge:

- (a) the Prizm Entities operate an extensive business;
- (b) the beneficiaries will provide essential legal and financial advice and leadership;
- (c) there is no anticipated unwarranted duplication of roles;
- (d) secured creditors likely to be affected by the charge were provided with notice and do not object to the Administration Charge; and

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(e) the proposed monitor, in its pre-filing report, supports the Administration Charge.

[44] I am satisfied that this is an appropriate case in which to grant the Administration Charge in the form requested.

[45] I am also satisfied that it is appropriate to grant a Directors' Charge in the amount of \$9.8 million to protect directors and officers and the CRO from certain potential liabilities. In arriving at this determination, I have considered the provisions of s. 11.5(1) of the CCAA which addresses the issue of directors' and officers' charges. I have also considered that the Prizm Entities maintain directors' and officers' liability insurance ("D&O Insurance"). The current policy provides a total of \$31 million in coverage. It is expected that the D&O Insurance will provide coverage sufficient to protect the directors and officers and the draft Initial Order provides that the Directors' Charge shall only apply to the extent that the D&O Insurance is not adequate.

[46] For the foregoing reasons, I am satisfied that it is appropriate to grant the CCAA Initial Order in the form requested.

[47] Paragraph 14 of the form of order provides for a stay of proceedings up to and including April 29, 2011. Paragraph 59 provides for the standard comeback provision.

[48] The Initial Order was signed 9:30 a.m. Eastern Daylight Time on March 31, 2011.

  
MORAWETZ J.

**Date:** March 31, 2011