COURT FILE NO.	2503 00016	Clerk's Stamp
COURT	Court of King's Bench of Alberta	
JUDICIAL CENTRE	Edmonton	

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

AND IN THE MATTER OF **KMC MINING CORPORATION**

DOCUMENT **BRIEF OF LAW IN SUPPORT OF APPLICATION FOR SALE APPROVAL AND VESTING ORDER and ANCILLARY RELIEF**

ADDRESS FOR SERVICE AND CONTACT INFORMATION OF PARTY FILING THIS DOCUMENT	DARREN R. BIEGANEK, KC/ ZACHARY SOPROVICH Barrister & Solicitor Phone: 780.441.4386 Fax: 780.428.9683 Email: dbieganek@dcllp.com	File # 204-219113 **DUNCAN CRAIG LLP** LAWYERS MEDIATORS 2800 Rice Howard Place 10060 Jasper Avenue Edmonton, Alberta T5J 3V9

TABLE OF CONTENTS

I. INTRODUCTION and SUMMARY OF CCAA PROCEEDINGS

1. In this Application, KMC Mining Corporation ("**KMC**" or the "**Applicant**") seeks:

   a) a Sale Approval and Vesting Order ("**SAVO**") approving a sale of substantially all of the assets of the Applicant ("**Property**", as more specifically described within the Transaction) to 2122256 Alberta Ltd. o/a Heavy Metal Equipment & Rentals (the "**Purchaser**") (and the sale herein referred to as the "**Transaction**") arising out of the Sales and Investment Solicitation Process ("**SISP**") previously approved by the Court with the SAVO specifically including:

      i) assignment of certain contracts to which the Applicant is a party to with Syncrude Canada Ltd., Suncor Energy Inc. ("**Suncor**") and the Government of Alberta - Forestry and Parks (collectively the "**Assumed Contracts**"); and

      ii) authorizing the sale of assets which the Applicant leased from certain equipment lessors;

   b) an Order modifying the key employee retention plan ("**KERP**") to provide for certain adjustments as to who would be entitled to certain payments in respect of the KERP without modification to the total amounts payable thereunder;

   c) an Order affirming the continued applicability of the *Wage Earner Protection Program Act* (Canada) SC 2005, c 47 ("**WEPPA**") to the Applicant;

   d) an Order authorizing an interim distribution of up to 50% net sale proceeds to secured creditors and equipment lessors ("**Interim Distribution**"); and

   e) a Sealing Order with respect to the Supplementary Confidential Affidavit of Bryn Jones sworn April 7, 2025 ("**Fifth Confidential Affidavit**") and the Confidential Appendices to the Monitor's Second Report ("**Monitor Appendices**") until December 31, 2025.

2. On December 5, 2024, the Applicant filed a Notice of Intention to Make a Proposal ("**NOI**") under the *Bankruptcy and Insolvency Act*, RSC 1985, c B-3 ("**BIA**").

3. On January 10, 2025, an Initial Order pursuant to section 11 of the *Companies' Creditors Arrangement Act*, RSC 1985, c C-26, as amended (the "**CCAA**") was granted by the Honourable Justice M.J. Lema in respect of the Applicant, which continued the NOI proceedings into these CCAA proceedings, and which included a stay of proceedings to and including January 20, 2025. FTI Consulting Canada Inc. ("**FTI**") is the Monitor within the CCAA proceedings ("**Monitor**").

4. Also on January 10, 2025, the Honourable Justice M.J. Lema also granted an Order approving the SISP (with the Order approving the SISP being the "**Order – Approve SISP**") over the Applicant's Property.

Ernst & Young Orenda Corporate Finance Inc. (the "**Sales Agent**") administered the SISP as Sales Agent, with oversight from the Monitor.

5. On January 20, 2025, the Honourable Justice J.T. Nielson granted:

   a) an amended and restated initial order ("**ARIO**") which extended the stay of proceedings to June 16, 2025 and approved the KERP; and

   b) an order authorizing a process to return certain leased equipment to respective equipment lessors (the "**Lease Equipment Return Order**"), which process permitted the Applicant, subject to Monitor's approval, to return certain leased equipment which is unnecessary for current operations and which has little or no equity.

II. FACTS

6. The facts are set out in the Affidavit of Bryn Jones ("**Jones Affidavit #1**") sworn December 31, 2024, Affidavit of Bryn Jones sworn January 14, 2025 ("**Jones Affidavit #2**") and Affidavit of Bryn Jones sworn April 7, 2025 ("**Jones Affidavit #3**"). The salient facts will generally be referred to directly in argument as outlined below. Specific additional facts which are germane to the background of this matter, and updates on the activity of the Applicant since the last Court appearance on January 20, 2025 follow on a summary basis.

A. Activities of the Applicant since Initial Order[1]

7. The Applicant's primary operations consist of an ongoing bare rental agreement with Suncor pursuant to a Letter of Intent/ Purchase Order issued under the Applicant's existing multiple use agreement ("**MUA**") with Suncor (the "**Truck Rental Agreement**").

8. Since the Initial Order, the Truck Rental Agreement was expanded to include the bare rental of five or more additional Komatsu 930-4E's until the end of March 2025. That additional rental arrangement has concluded. However, the revenue was of great assistance to the Applicant during these proceedings.

9. In addition to the Truck Rental Agreement, the Applicant has in place a purchase order with Hudbay Minerals at its copper mountain mine in British Columbia to supply equipment operators to the site. That purchase order commenced at or around the date of the Initial Order and is for a term which expires on May 31, 2025 however there is work remaining which could result in an extension of the work into June.

[1] Jones Affidavit #3 at paras 13-16, 27, 55.

10. The cash flow from this work has eliminated the need for the Applicant to draw down further on its interim lending facility originally approved during the NOI proceedings and affirmed in the Initial Order and in the ARIO. The amount drawn under the interim lending facility was $3,000,000. The interim lending facility by its terms matures and expires on April 9, 2025. The principal amount plus accrued interest and the balance of the Interim Lender's fee, in the amount of $150,000, were paid in full from cash on hand on April 4, 2025.

11. As of April 4, 2025, the Applicant employed 92 full-time employees or subcontractors, of which 14 are located at its head office in Edmonton, Alberta, 40 on a labour supply project in British Columbia, and 38 field employees working in Fort McMurray or a field office location maintained there. If the Transaction is approved and the sale closes, there will be a significant reduction in the Applicant's staffing.

B. Lease Returns/ Disclaimers[2]

12. Under the terms and conditions of the Lease Equipment Return Order, the Applicant has taken steps to return assets which were secured to:

    a) Mitsubishi HC Capital Canada Leasing Inc.;
    b) Daimler Truck Financial;
    c) Jim Pattison Industries Ltd. ("**JPI**"); and
    d) Deutsche Leasing Canada Corp. ("**Deutsche**").

13. Pursuant to the Lease Equipment Return Order, the Monitor has provided each of the affected lessors with information respecting the costs payable by them in relation to their collateral, as a contribution towards the cost of these CCAA proceedings. The lessors have either paid those costs or are in the process of making arrangements to pay, prior to release of their equipment.

14. The Applicant is also in the process of initiating returns of certain equipment to Meridian OneCap Credit Corp., pursuant to the same Lease Equipment Return Order.

15. Except for payments to Komatsu International (Canada) Inc. ("**Komatsu**"), the Applicant has continued to make payments on leases for equipment which it continued to utilize during the SISP.

16. The payments to Komatsu were set out in the Applicant's cash flows and were forecast at $668,000 per month, and approximately $3.88 million over the forecast period. At the request of the Applicant's primary

[2] Jones Affidavit #3 at paras 17-26.

secured creditor (the “**Syndicate**”), and in consultation with the Monitor and Komatsu, it was determined that payments of that magnitude would cease during the SISP so payments were not made to Komatsu.

17. The Applicant leased a shop in Edmonton located at 5809 – 98 Street Edmonton, Alberta (“**Shop Lease**”).

18. The shop was no longer needed for the Applicant’s ongoing business operations and was not included as part of the Property to be addressed in the SISP.

19. As a result, on March 24, 2025, the Applicant sent a Notice to Disclaim or Resiliate to the landlord.

20. To date, no application has been filed to challenge the disclaimer of the Shop Lease and if no application is filed that will become effective as of April 23, 2025.

C. SISP[3]

21. The SISP was developed with input from the Applicant, Sales Agent and the Monitor, and the Syndicate. No party opposed the SISP and the Order – Approve SISP was granted on January 10, 2025.

22. The SISP was implemented by the Sales Agent in accordance with the Order- Approve SISP and has now concluded. Detailed results and analysis is provided in section IV(B)(i) of this Brief.

23. The SISP had certain deadlines for the marketing of the Property and for any interested parties to put forth offers, namely:

    a) Marketing Period Launch – January 15, 2025;

    b) Virtual Data Room Open – January 17, 2025;

    c) Phase I Bid Deadline – February 28, 2025; and

    d) Phase II Bid Deadline – March 28, 2025.

24. Assets were marketed on a world-wide basis with interest expressed, and due diligence undertaken, by parties from as far away as Australia.

[3] Order – Approve SISP and Jones Affidavit #3 at paras 29, 43.

25. The only party providing a deposit in accordance with the requirements of the SISP was the Purchaser, who made the *en bloc* offer for substantially all of the Property and executed an asset purchase agreement ("**APA**") in respect of same.

26. An analysis of the proposals has been undertaken by the Sales Agent in conjunction with the Monitor and has been reviewed with the Syndicate, the Applicant's primary secured creditor. An analysis was also provided to and reviewed with Komatsu, and discussions were held by the Sales Agent with each of Caterpillar Financial Services Limited ("**CAT**") and John Deere Canada ULC ("**John Deere**") .

27. While the recovery, if the Transaction is approved and closes, is not sufficient to retire all the Applicant's obligations, after a thorough canvas of a worldwide market, the Transaction represents the best value for the Applicant's Property in the circumstances at the present time. Continuing to operate the business on the revenue being generated at this time is neither in the longer-term interests of the enterprise nor will it generate sufficient income to make material payments to retire the debt if further sales efforts were undertaken.

III. ISSUES

28. In considering this Application before the Court, the Court must be satisfied that:

a) in consideration of section 36(3) of the CCAA, whether the sale of the Property to the Purchaser should be approved;

b) in consideration of section 11.3 of the CCAA, whether the Assumed Contracts ought to be assigned to the Purchaser;

c) with respect to the KERP adjustment, that the same is appropriate in the circumstances;

d) with respect to the Interim Distribution, whether the same should be authorized; and

e) with respect to the Sealing Order, whether the importance of protecting sensitive pricing and valuation information of the Property until after a sale is concluded outweigh the deleterious effects of restricting the accessibility of Court proceedings.

IV. ARGUMENT

A. The General Proposition

29. While historically the CCAA has prioritized "avoiding the social and economic losses resulting from liquidation of an insolvent company", the CCAA is fundamentally insolvency legislation.[4]

30. As fundamentally insolvency legislation, the CCAA has the simultaneous objectives of maximizing creditor recovery, preservation of going concern value where possible and preservation of jobs and communities affected by the firm's financial distress. In pursuit of those objectives, CCAA proceedings have evolved to permit outcomes that do not result in the emergence of the pre-filing debtor company in a restructured state.[5]

31. Liquidation is not necessarily inconsistent with the remedial objectives of the CCAA.[6]

32. Each case is looked at on its own merit. The relative weight which the different objectives of the CCAA take on in any case may vary based on the factual circumstances, the stage of proceedings and so forth.[7]

33. As has been previously noted by Courts in CCAA proceedings, "[t]here is, of course, no precise and invariable formula. This is not a 'cookie cutter' exercise… the matter must be decided on the basis of credible evidence and common sense, employing a principled, purposive and contextual approach."[8]

34. In the present circumstances, the relief sought is consistent with the objectives of the CCAA.

35. With these general propositions at the forefront, this Brief will now address the specific pieces of relief sought.

B. Transaction Ought to be Approved

i. <u>SISP was Reasonable and Fully Tested the Market</u>

36. The jurisdiction to approve the Transaction is set out in section 36 of the *CCAA* which states:

> 36(1) A debtor company in respect of which an order has been made under this Act may not sell or otherwise dispose of assets outside the ordinary course of business unless

---

[4] *Century Services Inc v Canada (Attorney General)*, 2010 SCC 60 [*Century Services*] at para 70 **[TAB 1]**.
[5] *9354-9186 Quebec Inc. and 9354-9178 Quebec Inc. v Callidus Capital Corporation*, 2020 SCC 10 [*Bluberi*] at para 42 **[TAB 2]**.
[6] *Bluberi,* at para 45 **[TAB 2]**.
[7] *Bluberi*, at para 46 **[TAB 2]**.
[8] *Lemare Holdings Ltd., Re*, 2012 BCSC 1591 at para 60 **[TAB 3]**.

> authorized to do so by a court. Despite any requirement for shareholder approval, including one under federal or provincial law, the court may authorize the sale or disposition even if shareholder approval was not obtained.
>
> (2) A company that applies to the court for an authorization is to give notice of the application to the secured creditors who are likely to be affected by the proposed sale or disposition.
>
> (3) In deciding whether to grant the authorization, the court is to consider, among other things,
>
> > (a) whether the process leading to the proposed sale or disposition was reasonable in the circumstances;
> >
> > (b) whether the monitor approved the process leading to the proposed sale or disposition;
> >
> > (c) whether the monitor filed with the court a report stating that in their opinion the sale or disposition would be more beneficial to the 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 or disposition on the 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.[9]

37. *Royal Bank of Canada v Soundair Corp.*[10] established the factors to consider when approving a sale in a Court supervised process:

    a) whether there has been sufficient effort made to obtain the best price and has not acted improvidently;

    b) the interests of the parties;

    c) the efficacy and integrity of the process by which offers were obtained; and

    d) whether there was unfairness in the working out of the process.[11]

38. In *Veris Gold Corp*., the Court recognized that "[a] more general test has been restated… namely to consider the transaction as a whole and decide 'whether or not the sale is appropriate, fair and reasonable'," which is sometimes referred to as the White Burch test.[12]

39. In *Re AbitibiBowater Inc*., the Court noted that it has jurisdiction to approve a sale of assets during CCAA proceedings, and observed that "[a]bsent some compelling, exceptional factor to the contrary, the Court

---

[9] *Companies' Creditors Arrangement Act*, RSC 1985, c C-26, s 36 **[TAB 4]**.
[10] *Royal Bank of Canada v Soundair Corp.*, 1991 CarswellOnt 205, 1991 CanLII 2727 [Soundair] **[TAB 5]**.
[11] *Soundair* at para 16 **[TAB 5]**; *Re Veris Gold Corp.,* 2015 BCSC 1204 at paras 24-25 [*Veris Gold Corp*] **[TAB 6]**.
[12] *Veris Gold Corp.* at para 23 **[TAB 6]**.

should accept an applicant's proposed sales process where it was recommended by the Monitor and supported by the stakeholders."[13]

40. The Applicant submits that the Transaction ought to be approved for the following reasons:

a) the SISP was developed with input from the Applicant, Sales Agent and the Monitor, and the Syndicate, with no party opposing the SISP;

b) marketing efforts were broad:

i) teaser and draft non-disclosure agreements ("**NDAs**") were sent to 2,391 individuals and 923 companies originally;

ii) all individuals, companies or brokers which the Applicant had previously been in contact with respecting potential asset sales were contacted;

iii) a press release was issued at the commencement of the SISP on January 15, 2025, with the information posted to both the website of the Applicant and the Monitor;

iv) a virtual data room ("**VDR**") was opened on January 17, 2025;

v) 58 NDAs were executed and those parties given access to the VDR;[14]

c) the SISP was phased: Phase I to seek interest and determine if bidders were qualified, and Phase II for those Phase I Qualified Bidders to proceed in the process;

d) the two-phase SISP enabled the Applicant to keep competitive tension in the SISP;[15]

e) 16 proposals were received in Phase I of the SISP, with those bidders who were qualified as Phase I Bidders pursuant to the SISP given an opportunity to conduct physical due diligence on the Applicant's Property, with several interested parties visiting the Suncor mining site where the majority of the Property is located;[16]

f) 9 proposals were received prior to the Phase II deadline:

i) one (1) unconditional Phase II proposal for substantially all of the Property (the APA);

ii) one (1) unconditional proposal for the acquisition of the Syncrude shop;

iii) three (3) conditional proposals for individual or smaller blocks of assets; and

iv) four (4) liquidation or auction proposals;[17]

[13] *Re AbitibiBowater Inc.,* 2009 QCCS 6460 at paras 36 and 59 **[TAB 7]**.
[14] Jones Affidavit #3 at paras 29-32, 34.
[15] Jones Affidavit #3 at para 33, 35.
[16] Jones Affidavit #3 at para 37-38.
[17] Jones Affidavit #3 at para 39.

g) only the Purchaser submitted a deposit in accordance with the terms of the SISP. Analysis of all Phase II proposals was conducted by the Sales Agent, in conjunction with the Monitor and has been reviewed with the Syndicate, the Applicant's primary secured creditor.[18]

41. Appraised values for the Property were previously provided within a Confidential Affidavit in this matter.[19] While the purchase price within the APA is lesser than said values, those values were based upon market assessment as of December 2023. Market conditions have changed significantly since then, including by the imposition and threat of further tariffs by the United States Government, Suncor's contracting strategy, cost implications of selling now versus holding the Property, and the expense of demobilizing the Property from the Suncor site.[20]

42. The SISP tested the market on a worldwide basis.[21] The market has spoken and the Transaction represents the greatest return for stakeholders at the present time.

43. With respect to the SISP as a whole:

a) the SISP was developed to be a process open to, and marketed upon, any interested buyers on a worldwide basis, and to permit the open market to determine the current market value of the Property;
b) the Sales Agent, with Monitor oversight, administered the SISP in a transparent manner in accordance with its Court-appointed duties; and
c) in the circumstances, there was a good faith and transparent SISP to solicit offers from any and all parties. Accordingly, the market has spoken and confirmed that the purchase price pursuant to the Transaction is the highest value a buyer is willing to pay for the Property at this time.

44. The Applicant submits that approving the Transaction is appropriate, fair and reasonable in the circumstances, including after consideration of the *Soundair* factors and all factors under sections 36(3) of the CCAA.

ii. <u>Leased Assets</u>

45. Of the Property proposed to be sold as part of the Transaction, approximately 30% of the Property is leased by the Applicant from various equipment lessors.

46. It is the opinion of the Applicant's counsel that two lessors have capital or true leases with the Applicant: John Deere and JPI. No assets of JPI are being sold as part of the Transaction. John Deere is being

[18] Jones Affidavit #3 at para 40.
[19] Confidential Affidavit of Bryn Jones sworn December 31, 2024, Exhibit "B".
[20] Jones Affidavit #3 at para 53.
[21] Jones Affidavit #3 at para 43.

consulted as to whether they are agreeable to their assets being sold as part of the Transaction. Current information is that it is expected that John Deere will allow its assets to be sold as part of the Transaction.[22]

47. The remainder of the leased assets are subject to financing leases[23] in the Applicant's opinion. The Applicant is of the view that the Order – Approve SISP and the nature of these financing leases permit the sale of those assets as part of the Transaction.

48. In any event, of the financing leases, lessors with interest in the vast majority of the leased assets proposed to be included in the Transaction are expected to be agreeable to their assets being included in the Transaction. Those lessors holding the vast majority of the leased assets proposed to be including in the Transaction have been consulted and the Applicant's current understanding is that said lessors will allow its assets to be sold to the Purchaser as part of the Transaction.[24]

49. Further, the APA includes provisions whereby if certain Property originally included in the APA does not form part of the ultimate Transaction, the purchase price is accordingly adjusted pursuant to the value attributed to the respective asset in the APA.

50. Overall, while at time of submission of this Brief the Applicant does not have explicit consent from all equipment lessors on the Transaction:

    a) it is actively communicating with all affected equipment lessors, and advising of the pending Transaction, proposed sale values and that they will be asked to contribute to the costs of these CCAA proceedings;

    b) as mentioned, lessors with the vast majority of the leased assets proposed to be included in the Transaction are expected to be agreeable to their assets being included in the Transaction; and

    c) in the event that not all equipment lessors consent to their assets being part of the Transaction and if the parties cannot otherwise reach a resolution prior to April 17, 2025, this Application can be used to determine the Applicant's ability to sell said leased assets, with reference to *Cow Harbour*, the Order – Approve SISP and Lease Equipment Return Order.

iii. Assumed Contracts should be Assigned to the Purchaser

51. The following are the four Assumed Contracts to which the Applicant is a party, and which form part of the Property subject to the Transaction:

---

[22] Jones Affidavit #3 at para 47.
[23] *Royal Bank of Canada v Cow Harbour Construction Ltd.*, 2012 ABQB 59 **[TAB 8]**.
[24] Jones Affidavit #3 at paras 41, 47-48.

a) the Syncrude Canada Ltd. ("**Syncrude**") shop lease on the Syncrude site;

b) the Truck Rental Agreement with Suncor which is effectively a purchase order under the Applicant's existing MUA with Suncor; and

c) a lease of land with the Government of Alberta - Forestry and Parks.[25]

52. The Applicant seeks the Assumed Contracts be assigned to the Purchaser as part of the Transaction.

53. Pursuant to section 11.3 of the CCAA, the Court has the power to assign contracts to which the debtor company is a party:

> Assignment of agreements
>
> 11.3 (1) On application by a debtor company and on notice to every party to an agreement and the monitor, the court may make an order assigning the rights and obligations of the company under the agreement to any person who is specified by the court and agrees to the assignment.
>
> Exceptions
>
> (2) Subsection (1) does not apply in respect of rights and obligations that are not assignable by reason of their nature or that arise under
>
> > (a) an agreement entered into on or after the day on which proceedings commence under this Act;
> >
> > (b) an eligible financial contract; or
> >
> > (c) a collective agreement.
>
> Factors to be considered
>
> (3) In deciding whether to make the order, the court is to consider, among other things,
>
> > (a) whether the monitor approved the proposed assignment;
> >
> > (b) whether the person to whom the rights and obligations are to be assigned would be able to perform the obligations; and
> >
> > (c) whether it would be appropriate to assign the rights and obligations to that person.
>
> Restriction
>
> (4) The court may not make the order unless it is satisfied that all monetary defaults in relation to the agreement — other than those arising by reason only of the company's insolvency, the commencement of proceedings under this Act or the company's failure to perform a non-monetary obligation — will be remedied on or before the day fixed by the court.
>
> ….

[25] Jones Affidavit #3 at para 50.

54. Section 11.3 of the CCAA gives the Court jurisdiction and the discretion to make an order assigning the rights and obligations of the debtor company.[26]

55. Section 84.1 of the BIA[27] is analogous to section 11.3 of the CCAA, other than the CCAA requiring the debtor (rather than the trustee in bankruptcy) to bring the application and that the Court is to also consider whether the Monitor approves of the proposed assignment.

56. Harmonization of Canada's insolvency and restructuring schemes has been a priority. The Supreme Court of Canada's comments in *Century Services* provide insight into the harmonization of the CCAA and BIA when stating that "with parallel CCAA and BIA restructuring schemes now an accepted feature of the insolvency law landscape, the contemporary thrust of legislative reform has been towards harmonizing aspects of insolvency law common to the two statutory schemes…"[28]

57. With the Supreme Court of Canada outlining the harmony between the BIA and CCAA, and the materially similar wording of sections 84.1 of the BIA and 11.3 of the CCAA, the principles of cases interpreting either section are instructive.

58. In consideration of section 84.1 of the BIA, the Alberta Court of Appeal in *Ford Motor Company of Canada, Limited v Welcome Ford Sales Ltd* noted the basis of the section is to preserve the value of the estate as a whole, even if some contractual rights of some creditors are compromised:

> [30] The effect of s. 84.1 of the BIA is to override the common law unilateral right of the innocent party to the contract to accept the repudiation and end the contract. It has been designed to preserve the value of the estate as a whole, even if the contractual rights of some creditors, such as Ford in this case, are compromised. Therefore, even if Ford otherwise had the right to terminate the dealership agreement for breach of condition, and its assignment clause was not one which survived the termination, s. 84.1 nonetheless allows the trustee to apply to the Court for permission to assign the contract so long as the provisions of the statute are met.[29]

[26] *BBB Canada Inc.*, 2023 ONSC 2308 at para 18 **[TAB 9]**.
[27] *Bankruptcy and Insolvency Act*, RSC 1985, c B-3, s 84.1 **[TAB 10]**.
[28] *Century Services* at para 24 **[TAB 1]**.
[29] *Ford Motor Company of Canada, Limited v Welcome Ford Sales Ltd.*, 2011 ABCA 158 [*Welcome Ford*] at para 30 **[TAB 11]**.

59. Further, the Alberta Court of Appeal noted that the circumstances in which contracts are not assignable are narrow:

> [52] Parties to a contract cannot insulate it from the effect of s. 84.1 simply by including a clause describing it as creating "personal" obligations where the contract is, in fact, a commercial one which could be performed by many others than the contracting parties.
>
> [53] Ford correctly pointed out that s. 84.1(3) does not speak of a personal contract as being the only type of contract which contains rights and obligations that are not assignable by their nature. It argued that the above terms of the dealership agreement evidence that it is not assignable by reason of its nature even if it is not a personal contract.
>
> [54] However, those express provisions – including those which describe it as personal in nature as well as Ford's reservation of the right to execute dealership agreements with those specifically selected and approved by it – are not sufficient to attract the application of s. 84.1(3) if other circumstances suggest the contrary. Otherwise, s. 84.1(4) would have no meaning, if a simple contractual provision to the effect that it was not "by reason of its nature" capable of unilateral assignment would be enough to make that so.[30]

60. Courts have approved assignments under section 11.3 of the CCAA even when the proposed purchaser of the contract was newly incorporated and highly leveraged:

> [30] It seems to me that a fundamental condition precedent to requiring a contract counterpart to be locked into an involuntary assignment post-insolvency is that the court sanctioning the assignment is able to conclude that the assignee will, in the words of s. 11.3(3)(b) of the CCAA, "be able to perform the obligations". This does not imply iron-clad guarantees. It does not give license to the counterparty to demand the receipt of financial covenants or assurances that it did not previously enjoy under the contract it originally negotiated with the debtor.
>
> [31] A proposed purchaser starting life with close to 100% leverage gives this judge a considerable degree of heartburn when it comes to answering the question of whether the assignee is a person who will be able to perform the obligations. That concern is amplified when one adds the prospect of landowners being made liable for environmental remediation caused by lessees and others on their land.[31]

61. Parliament made a policy decision that a Court ought to have the discretion to authorize a trustee to assign (sell) the rights and obligations of a bankrupt under such an agreement notwithstanding objections of the counter-party.[32] The analogous section under section 11.3 of the CCAA provides the same authority.

62. Canvassing the consent of the contracting party is not a prerequisite to the application for approval of an assignment of an agreement.[33]

---

[30] *Welcome Ford* at paras 52-54 **[TAB 11]**.
[31] *Dundee Oil and Gas Limited (Re)*, 2018 ONSC 3678 at paras 30-31 **[TAB 12]**.
[32] *Welcome Ford* at para 39 **[TAB 11]**.
[33] *Welcome Ford* at para 66 **[TAB 11]**.

63. None of the exceptions within section 11.3(2) are applicable to the Assumed Contracts.

64. The factors to be considered under section 11.3(3) all favour assignment of the Assumed Contracts as:

a) the Monitor is supportive of the assignment of the Assumed Contracts;

b) the Purchaser is willing and able to perform the obligations of the Assumed Contracts and to the Applicant's knowledge, has an existing MUA with Suncor and is therefore an approved supplier to Suncor[34];

c) the Assumed Contracts are not personal in nature[35], and rather are commercial contracts that can be performed by others with similar experience in the industry[36];

d) the Assumed Contracts are an integral part of the Transaction[37] and to the extent they are not included in the Transaction, the purchase price is reduced pursuant to the APA, reducing value to stakeholders;

e) in the circumstances where the Applicant is in the process of selling its Property and winding down most operations, it is appropriate the Assumed Contracts be assigned to a party who is able to perform the obligations thereunder, and willing to accept the assignment of the Assumed Contracts.

65. There are no monetary defaults under the Assumed Contracts.[38]

66. The factors for the Court to consider in assigning the Assumed Contracts all favour assignment and therefore, it is submitted that this Court should exercise its discretion under section 11.3 of the CCAA and confirm the assignment to the Purchaser of the Assumed Contracts.

C. The Key Employee Retention Plan Adjustment is Appropriate

67. The Applicant seeks an Order adjusting the KERP. Two employees who would have been entitled to payments under the KERP left their employment with the Applicant on their own accord. Those potential payments under the KERP totalled $30,000.[39] The Applicant proposes that said amount be paid to Daniel Klemke, the President and CEO of the Applicant, who played an integral role during the SISP.

---

[34] Jones Affidavit #3 at para 51(b).
[35] *Welcome Ford* at para 55 **[TAB 11]** citing *Black Hawk Mining Inc. v Manitoba (Provincial Assessor)*, 2002 MBCA 51: "Agreements are said to be personal in this sense when they are based on confidences, or considerations applicable to special personal characteristics, and so cannot be usefully performed to or by another."
[36] *Welcome Ford* at para 50 **[TAB 11]**.
[37] Jones Affidavit #3 at para 51(c).
[38] Jones Affidavit #3 at para 51(a).
[39] Jones Affidavit #3 at paras 60-61.

68. As part of the ARIO on January 20, 2025, the KERP was approved. The complete KERP is subject to a Sealing Order of the Court and will be provided to the Court for consideration of this adjustment.

69. Courts have the discretion under section 11 of the CCAA to approve a KERP[40] and similarly Courts can use that discretion and amend a KERP if reasonable in the circumstances.[41]

70. Two of the employees that would be entitled to phase one or phase two payments under the KERP have ceased to be employed by the Applicant of their own accord. The total amount that would otherwise be payable to those employees is $30,000.

71. Daniel Klemke, the President and CEO of the Applicant is a beneficiary of the KERP but would not be receiving any payment unless and until a Plan of Arrangement is made to creditors.

72. Mr. Klemke has played an integral role in the SISP. In the circumstances of this matter, while the Applicant has not ruled out anything on a go forward basis, and therefore has not ruled out the prospect of a Plan of Arrangement, the prospects for a Plan of Arrangement being made are remote.[42]

73. The Applicant proposes that funds which might otherwise be directed to be paid to the two individuals who have now departed be paid to Mr. Klemke at the same times and on the same basis as those for the departed employees. Doing so will not impact the overall KERP, nor will payments under the KERP be greater than initially approved by this Court, and in considering the integral role of Mr. Klemke in the SISP, the KERP adjustment is reasonable and appropriate in the circumstances.

D. WEPPA

74. As part of the ARIO, the Applicant sought, and this Court granted, a declaration under the WEPPA that it, and its collective former employees, meet the criteria prescribed by section 3.2 of the WEPPA Regulation and are individuals to whom the WEPPA applies as of the date of the ARIO.[43]

75. If the Transaction is approved and the sale closes, there will be a significant further reduction in the Applicant's staffing.[44]

---

[40] *U.S. Steel Canada Inc. (Re),* 2014 ONSC 6145 *[US Steel]* at para 27 **[TAB 13]**.
[41] *Nortel Networks Corporation (Re)*, 2010 ONSC 1438 at para 28 **[TAB 14]**.
[42] Jones Affidavit #3 at para 63.
[43] ARIO, para 46.
[44] Jones Affidavit #3 at para 55.

76. Section 5(5) of WEPPA provides:

> (5) On application by any person, a court may, in proceedings under Division I of Part III of the *Bankruptcy and Insolvency Act* or under the *Companies' Creditors Arrangement Act*, determine that the former employer meets the criteria prescribed by regulation.[45]

77. While the WEPPA declaration in the ARIO remains unchanged, to the extent necessary for any clarity, the Applicant seeks a declaration that the WEPPA continues to apply to all non-union employees terminated since the ARIO, or who may be terminated after the Transaction closes, as those employees meet the criteria under WEPPA and the WEPPA Regulation.

E. Interim Distribution

78. It is common to proceed with interim distributions in insolvency proceedings.[46] In determining whether to authorize an interim distribution, courts may consider the following factors:

    a) whether the security is valid and enforceable;

    b) whether the amounts owed to the creditors would exceed the interim distribution;

    c) whether the interim distribution would generate interest savings; and

    d) whether there would be sufficient remaining liquidity after the interim distribution is made.[47]

79. The Monitor and its counsel are in the process of finalizing their review of the security held by the Syndicate and the various lessors, and it is expected to have that review completed before the date scheduled for this Application.

80. If the Transaction closes, net sale proceeds in excess of $100,000,000 will be received. Neither the Applicant, nor the Monitor, needs to hold that entire amount. The Applicant proposes, and submits that it is reasonable in the circumstances, for the Monitor to distribute up to 50% of the net sale proceeds from the Transaction to those respective creditors whose collateral is sold as part of the Transaction.

81. Cost allocations amongst various Property and creditors can be completed prior to final distributions. Distributing 50% of the net sale proceeds will pay down a portion of the indebtedness owing by the Applicant and result in interest savings.

---

[45] *Wage Earner Protection Program Act*, SC 2005, c 47, s 1, s 5(5) **[TAB 15]**.
[46] *Re AbitibiBowater Inc*, 2009 QCCS 6461 [*AbitibiBowater*] at para 71 **[TAB 16]**.
[47] *AbitibiBowater* at para 75 **[TAB 16]**.

F. Sealing Order

82. On an application to temporarily seal a court file, or a portion of it, this Honourable Court has broad discretion and may make a direction on any matter that the circumstances require, and it may grant the Order notwithstanding the provisions of Division 4 of Part 6 of the *Alberta Rules of Court*.[48]

83. Temporary sealing orders should be granted when:

a) an Order is needed to prevent serious risk to an important interest because reasonable alternative measures will not prevent the risk; and

b) the salutary effects of the Order outweigh its deleterious effects, including the effects on the right to free expression, which includes public interest in open and accessible court proceedings.[49]

84. More recently, the Supreme Court of Canada in *Sherman Estate v Donovan*, restated the test upon which an applicant must satisfy in asking a court to exercise discretion in a way that limits the open court presumption. An applicant must demonstrate (a) court openness poses a serious risk to an important public interest, (b) the order sought is necessary to prevent this serious risk to the identified interest because reasonably alternative measures will not prevent this risk, and (c) as a matter of proportionality, the benefits of the order outweigh its negative effects.[50]

85. The Applicant seeks the Sealing Order with respect to the Fifth Confidential Affidavit until December 31, 2025 (or further Order of this Court) and the Monitor Appendices, which contains detailed pricing and valuation information regarding the Property, and the Assumed Contracts.

86. The information within the Fifth Confidential Affidavit and Monitor Appendices is sensitive as it contains detailed pricing and valuation information regarding the Property and the Assumed Contracts. Fully disclosing that information on the public record prior to a transaction for the sale of the Property being completed could adversely affect future marketing and sale of the Property, if the Transaction for which approval is currently sought does not close.

87. Sealing the Fifth Confidential Affidavit and Monitor Appendices is the least restrictive method available to prevent the dissemination of the confidential information. The purpose of the sealing order, being to

[48] *Alberta Rules of Court*, Alta Reg 124-2010, Division 4 of Part 6.
[49] *Sierra Club of Canada v Canada (Minister of Finance)*, 2002 SCC 41 at para 45 **[TAB 17]**.
[50] *Sherman Estate v Donovan*, 2021 SCC 25 at para 38 **[TAB 18]**.

protect sensitive valuation information, far outweigh the deleterious effects of restricting the accessibility of Court proceedings. It is also a temporary measure.

88. The Applicant submits that the Sealing Order is appropriate in the circumstances and ought to be granted.

V. CONCLUSIONS AND RELIEF SOUGHT

89. The relief sought by the Applicant is just and appropriate, and consistent with the objectives of the CCAA:

a) The SISP was conducted by the Sales Agent, with Monitor oversight, in accordance with the Order – Approve SISP, the market for the Property was fully tested and approving the Transaction is appropriate and reasonable after consideration of the *Soundair* factors and all factors under sections 36(3) of the CCAA;

b) assignment of the Assumed Contracts is appropriate and reasonable, the Purchaser is capable of performing the Assumed Contracts and the Court has the authority under section 11.3 of CCAA to order the assignment;

c) the KERP adjustment does not alter the total payable under the previously approved KERP, the WEPPA declaration is a restatement of the WEPPA declaration this Court granted within the ARIO with the confirmation that said declaration continues to apply to future employees, and an Interim Distribution of 50% of net sale proceeds of the Transaction is reasonable in the circumstances; and

d) the Sealing Order is a temporary remedy to seal currently commercially sensitive property valuation information.

90. In all the circumstances this Application ought to be allowed.

DATED this 7th day of April, 2025.

DUNCAN CRAIG LLP
Per:

____
Darren R. Bieganek, KC/ Zachary Soprovich
Counsel for the Applicant, KMC Mining Corporation

TABLE OF AUTHORITIES

1. *Century Services Inc v Canada (Attorney General),* 2010 SCC 60
2. *9354-9186 Quebec Inc. and 9354-9178 Quebec Inc. v Callidus Capital Corporation*, 2020 SCC 10
3. *Lemare Holdings Ltd., Re*, 2012 BCSC 1591
4. *Companies' Creditors Arrangement Act*, RSC 1985, c C-26, s 11, 11.3, 36
5. *Royal Bank of Canada v Soundair Corp.,* 1991 CarswellOnt 205, 1991 CanLII 2727
6. *Re Veris Gold Corp.*, 2015 BCSC 1204
7. *Re AbitibiBowater Inc.*, 2009 QCCS 6460
8. *Royal Bank of Canada v. Cow Harbour Construction Ltd.,* 2012 ABQB 59
9. *BBB Canada Inc.*, 2023 ONSC 2308
10. *Bankruptcy and Insolvency Act*, RSC 1985, c B-3, s 84.1
11. *Ford Motor Company of Canada, Limited v Welcome Ford Sales Ltd.*, 2011 ABCA 158
12. *Dundee Oil and Gas Limited (Re)*, 2018 ONSC 3678
13. *U.S. Steel Canada Inc. (Re)*, 2014 ONSC 6145
14. *Nortel Networks Corporation (Re)*, 2010 ONSC 1438
15. *Wage Earner Protection Program Act*, SC 2005, c 47, s 1, s 2, 5
16. *Re AbitibiBowater Inc*, 2009 QCCS 6461
17. *Sierra Club of Canada v Canada (Minister of Finance)*, 2002 SCC 41
18. *Sherman Estate v Donovan*, 2021 SCC 25

Century Services Inc. v. Canada (Attorney General), [2010] 3 S.C.R. 379

Supreme Court Reports

Supreme Court of Canada

Present: McLachlin C.J. and Binnie, LeBel, Deschamps, Fish, Abella, Charron, Rothstein and Cromwell JJ.

Heard: May 11, 2010;

Judgment: December 16, 2010.

File No.: 33239.

[2010] 3 S.C.R. 379 | [2010] 3 R.C.S. 379 | [2010] S.C.J. No. 60 | [2010] A.C.S. no 60 | 2010 SCC 60 | 2010 CarswellBC 3419 | 72 C.B.R. (5th) 170 | 12 B.C.L.R. (5th) 1 | 296 B.C.A.C. 1 | 326 D.L.R. (4th) 577 | 409 N.R. 201 | [2011] 2 W.W.R. 383

Century Services Inc. Appellant; v. Attorney General of Canada on behalf of Her Majesty The Queen in Right of Canada Respondent.

(136 paras.)

Counsel

Mary I. A. Buttery, *Owen J. James* and *Matthew J. G. Curtis*, for the appellant.

Gordon Bourgard, *David Jacyk* and *Michael J. Lema*, for the respondent.

The judgment of McLachlin C.J. and Binnie, LeBel, Deschamps, Charron, Rothstein and Cromwell JJ. was delivered by

DESCHAMPS J.

1 For the first time this Court is called upon to directly interpret the provisions of the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36 ("*CCAA*"). In that respect, two questions are raised. The first requires reconciliation of provisions of the *CCAA* and the *Excise Tax Act*, R.S.C. 1985, c. E-15 ("*ETA*"), which lower courts have held to be in conflict with one another. The second concerns the scope of a court's discretion when supervising reorganization. The relevant statutory provisions are reproduced in the Appendix. On the first question, having considered the evolution of Crown priorities in the context of insolvency and the wording of the various statutes creating Crown priorities, I conclude that it is the *CCAA* and not the *ETA* that provides the rule. On the second question, I conclude that the broad discretionary jurisdiction conferred on the supervising judge must be interpreted having regard to the remedial nature of the *CCAA* and insolvency legislation generally. Consequently, the court had the discretion to partially lift a stay of proceedings to allow the debtor to make an assignment under the *Bankruptcy and Insolvency [page389] Act*, R.S.C. 1985, c. B-3 ("*BIA*"). I would allow the appeal.

1. Facts and Decisions of the Courts Below

2 Ted LeRoy Trucking Ltd. ("LeRoy Trucking") commenced proceedings under the *CCAA* in the Supreme Court of British Columbia on December 13, 2007, obtaining a stay of proceedings with a view to reorganizing its financial affairs. LeRoy Trucking sold certain redundant assets as authorized by the order.

3 Amongst the debts owed by LeRoy Trucking was an amount for Goods and Services Tax ("GST") collected but unremitted to the Crown. The *ETA* creates a deemed trust in favour of the Crown for amounts collected in respect of GST. The deemed trust extends to any property or proceeds held by the person collecting GST and any property of that person held by a secured creditor, requiring that property to be paid to the Crown in priority to all security interests. The *ETA* provides that the deemed trust operates despite any other enactment of Canada except the *BIA*. However, the *CCAA* also provides that subject to certain exceptions, none of which mentions GST, deemed trusts in favour of the Crown do not operate under the *CCAA*. Accordingly, under the *CCAA* the Crown ranks as an unsecured creditor in respect of GST. Nonetheless, at the time LeRoy Trucking commenced *CCAA* proceedings the leading line of jurisprudence held that the *ETA* took precedence over the *CCAA* such that the Crown enjoyed priority for GST claims under the *CCAA*, even though it would have lost that same priority under the *BIA*. The *CCAA* underwent substantial amendments in 2005 in which some of the provisions at issue in this appeal were renumbered and reformulated (S.C. 2005, c. 47). However, these amendments only came into force on September 18, 2009. I will refer to the amended provisions only where relevant.

[page390]

4 On April 29, 2008, Brenner C.J.S.C., in the context of the *CCAA* proceedings, approved a payment not exceeding $5 million, the proceeds of redundant asset sales, to Century Services, the debtor's major secured creditor. LeRoy Trucking proposed to hold back an amount equal to the GST monies collected but unremitted to the Crown and place it in the Monitor's trust account until the outcome of the reorganization was known. In order to maintain the *status quo* while the success of the reorganization was uncertain, Brenner C.J.S.C. agreed to the proposal and ordered that an amount of $305,202.30 be held by the Monitor in its trust account.

5 On September 3, 2008, having concluded that reorganization was not possible, LeRoy Trucking sought leave to make an assignment in bankruptcy under the *BIA*. The Crown sought an order that the GST monies held by the Monitor be paid to the Receiver General of Canada. Brenner C.J.S.C. dismissed the latter application. Reasoning that the purpose of segregating the funds with the Monitor was "to facilitate an ultimate payment of the GST monies which were owed pre-filing, but only if a viable plan emerged", the failure of such a reorganization, followed by an assignment in bankruptcy, meant the Crown would lose priority under the *BIA* (2008 BCSC 1805, [2008] G.S.T.C. 221).

6 The Crown's appeal was allowed by the British Columbia Court of Appeal (2009 BCCA 205, 270 B.C.A.C. 167). Tysoe J.A. for a unanimous court found two independent bases for allowing the Crown's appeal.

7 First, the court's authority under s. 11 of the *CCAA* was held not to extend to staying the Crown's application for immediate payment of the GST funds subject to the deemed trust after it was clear that reorganization efforts had failed and [page391] that bankruptcy was inevitable. As restructuring was no longer a possibility, staying the Crown's claim to the GST funds no longer served a purpose under the *CCAA* and the court was bound under the priority scheme provided by the *ETA* to allow payment to the Crown. In so holding, Tysoe J.A. adopted the reasoning in *Ottawa Senators Hockey Club Corp. (Re)* (2005), 73 O.R. (3d) 737 (C.A.), which found that the *ETA* deemed trust for GST established Crown priority over secured creditors under the *CCAA*.

8 Second, Tysoe J.A. concluded that by ordering the GST funds segregated in the Monitor's trust account on April 29, 2008, the judge had created an express trust in favour of the Crown from which the monies in question could not be diverted for any other purposes. The Court of Appeal therefore ordered that the money held by the Monitor in trust be paid to the Receiver General.

2. <u>Issues</u>

9 This appeal raises three broad issues which are addressed in turn:

(1) Did s. 222(3) of the *ETA* displace s. 18.3(1) of the *CCAA* and give priority to the Crown's *ETA* deemed trust during *CCAA* proceedings as held in *Ottawa Senators*?

(2) Did the court exceed its *CCAA* authority by lifting the stay to allow the debtor to make an assignment in bankruptcy?

21 In retrospect, this conclusion by the House of Commons committee was out of step with reality. It overlooked the renewed vitality the *CCAA* enjoyed in contemporary practice and the advantage that a [page397] flexible judicially supervised reorganization process presented in the face of increasingly complex reorganizations, when compared to the stricter rules-based scheme contained in the *BIA*. The "flexibility of the *CCAA* [was seen as] a great benefit, allowing for creative and effective decisions" (Industry Canada, Marketplace Framework Policy Branch, *Report on the Operation and Administration of the Bankruptcy and Insolvency Act and the Companies' Creditors Arrangement Act* (2002), at p. 41). Over the past three decades, resurrection of the *CCAA* has thus been the mainspring of a process through which, one author concludes, "the legal setting for Canadian insolvency restructuring has evolved from a rather blunt instrument to one of the most sophisticated systems in the developed world" (R. B. Jones, "The Evolution of Canadian Restructuring: Challenges for the Rule of Law", in J. P. Sarra, ed., *Annual Review of Insolvency Law 2005* (2006), 481, at p. 481).

22 While insolvency proceedings may be governed by different statutory schemes, they share some commonalities. The most prominent of these is the single proceeding model. The nature and purpose of the single proceeding model are described by Professor Wood in *Bankruptcy and Insolvency Law*:

> They all provide a collective proceeding that supersedes the usual civil process available to creditors to enforce their claims. The creditors' remedies are collectivized in order to prevent the free-for-all that would otherwise prevail if creditors were permitted to exercise their remedies. In the absence of a collective process, each creditor is armed with the knowledge that if they do not strike hard and swift to seize the debtor's assets, they will be beat out by other creditors. [pp. 2-3]

The single proceeding model avoids the inefficiency and chaos that would attend insolvency if each creditor initiated proceedings to recover its debt. Grouping all possible actions against the debtor into a single proceeding controlled in a single forum facilitates negotiation with creditors because it places them all on an equal footing, [page398] rather than exposing them to the risk that a more aggressive creditor will realize its claims against the debtor's limited assets while the other creditors attempt a compromise. With a view to achieving that purpose, both the *CCAA* and the *BIA* allow a court to order all actions against a debtor to be stayed while a compromise is sought.

23 Another point of convergence of the *CCAA* and the *BIA* relates to priorities. Because the *CCAA* is silent about what happens if reorganization fails, the *BIA* scheme of liquidation and distribution necessarily supplies the backdrop for what will happen if a *CCAA* reorganization is ultimately unsuccessful. In addition, one of the important features of legislative reform of both statutes since the enactment of the *BIA* in 1992 has been a cutback in Crown priorities (S.C. 1992, c. 27, s. 39; S.C. 1997, c. 12, ss. 73 and 125; S.C. 2000, c. 30, s. 148; S.C. 2005, c. 47, ss. 69 and 131; S.C. 2009, c. 33, s. 25; see also *Quebec (Revenue) v. Caisse populaire Desjardins de Montmagny*, 2009 SCC 49, [2009] 3 S.C.R. 286; *Deputy Minister of Revenue v. Rainville*, [1980] 1 S.C.R. 35; *Proposed Bankruptcy Act Amendments: Report of the Advisory Committee on Bankruptcy and Insolvency*).

24 With parallel *CCAA* and *BIA* restructuring schemes now an accepted feature of the insolvency law landscape, the contemporary thrust of legislative reform has been towards harmonizing aspects of insolvency law common to the two statutory schemes to the extent possible and encouraging reorganization over liquidation (see *An Act to establish the Wage Earner Protection Program Act, to amend the Bankruptcy and Insolvency Act and the Companies' Creditors Arrangement Act and to make consequential amendments to other Acts*, S.C. 2005, c. 47; *Gauntlet Energy Corp., Re*, 2003 ABQB 894, 30 Alta. L.R. (4th) 192, at para. 19).

25 Mindful of the historical background of the *CCAA* and *BIA*, I now turn to the first question at issue.

[page399]

3.2 *GST Deemed Trust Under the CCAA*

26 The Court of Appeal proceeded on the basis that the *ETA* precluded the court from staying the Crown's enforcement of the GST deemed trust when partially lifting the stay to allow the debtor to enter bankruptcy. In so

68 In this regard, though not strictly applicable to the case at bar, I note that Parliament has in recent amendments changed the wording contained in s. 11(1), making explicit the discretionary authority of the court under the *CCAA*. Thus, in s. 11 of the *CCAA* as currently enacted, a court may, "subject to the restrictions set out in this Act, ... make any order that it considers appropriate in the circumstances" (S.C. 2005, c. 47, s. 128). Parliament appears to have endorsed the broad reading of *CCAA* authority developed by the jurisprudence.

69 The *CCAA* also explicitly provides for certain orders. Both an order made on an initial application and an order on subsequent applications may stay, restrain, or prohibit existing or new proceedings against the debtor. The burden is on the applicant to satisfy the court that the order is appropriate in the circumstances and that the applicant has been acting in good faith and with due diligence (*CCAA*, ss. 11(3), (4) and (6)).

70 The general language of the *CCAA* should not be read as being restricted by the availability of more specific orders. However, the requirements of appropriateness, good faith, and due diligence are baseline considerations that a court should always bear in mind when exercising *CCAA* authority. Appropriateness under the *CCAA* is assessed by inquiring whether the order sought advances the policy objectives underlying the *CCAA*. The question is whether the order will usefully further efforts to achieve the remedial purpose of the *CCAA* -- avoiding the social and economic losses resulting from liquidation of an insolvent company. I would add that appropriateness extends not only to the purpose of the order, but also to the means it employs. Courts should be mindful that chances for successful reorganizations are enhanced where participants achieve common ground and all [page417] stakeholders are treated as advantageously and fairly as the circumstances permit.

71 It is well established that efforts to reorganize under the *CCAA* can be terminated and the stay of proceedings against the debtor lifted if the reorganization is "doomed to failure" (see *Chef Ready*, at p. 88; *Philip's Manufacturing Ltd., Re* (1992), 9 C.B.R. (3d) 25 (B.C.C.A.), at paras. 6-7). However, when an order is sought that does realistically advance the *CCAA*'s purposes, the ability to make it is within the discretion of a *CCAA* court.

72 The preceding discussion assists in determining whether the court had authority under the *CCAA* to continue the stay of proceedings against the Crown once it was apparent that reorganization would fail and bankruptcy was the inevitable next step.

73 In the Court of Appeal, Tysoe J.A. held that no authority existed under the *CCAA* to continue staying the Crown's enforcement of the GST deemed trust once efforts at reorganization had come to an end. The appellant submits that in so holding, Tysoe J.A. failed to consider the underlying purpose of the *CCAA* and give the statute an appropriately purposive and liberal interpretation under which the order was permissible. The Crown submits that Tysoe J.A. correctly held that the mandatory language of the *ETA* gave the court no option but to permit enforcement of the GST deemed trust when lifting the *CCAA* stay to permit the debtor to make an assignment under the *BIA*. Whether the *ETA* has a mandatory effect in the context of a *CCAA* proceeding has already been discussed. I will now address the question of whether the order was authorized by the *CCAA*.

[page418]

74 It is beyond dispute that the *CCAA* imposes no explicit temporal limitations upon proceedings commenced under the Act that would prohibit ordering a continuation of the stay of the Crown's GST claims while lifting the general stay of proceedings temporarily to allow the debtor to make an assignment in bankruptcy.

75 The question remains whether the order advanced the underlying purpose of the *CCAA*. The Court of Appeal held that it did not because the reorganization efforts had come to an end and the *CCAA* was accordingly spent. I disagree.

76 There is no doubt that had reorganization been commenced under the *BIA* instead of the *CCAA*, the Crown's deemed trust priority for the GST funds would have been lost. Similarly, the Crown does not dispute that under the scheme of distribution in bankruptcy under the *BIA* the deemed trust for GST ceases to have effect. Thus, after

9354-9186 Québec inc. v. Callidus Capital Corp., [2020] 1 S.C.R. 522

Supreme Court Reports

Supreme Court of Canada

Present: Wagner C.J. and Abella, Moldaver, Karakatsanis, Côté, Rowe and Kasirer JJ.

Heard: January 23, 2020;

Judgment: January 23, 2020.

Reasons delivered: May 8, 2020.

File No.: 38594.

[2020] 1 S.C.R. 522 | [2020] 1 R.C.S. 522 | [2020] S.C.J. No. 100 | [2020] A.C.S. no 100 | 2020 SCC 10

9354-9186 Québec inc. and 9354-9178 Québec inc. Appellants; v. Callidus Capital Corporation, International Game Technology, Deloitte LLP, Luc Carignan François Vigneault, Philippe Millette, Francis Proulx and François Pelletier Respondents, and Ernst & Young Inc. IMF Bentham Limited (now known as Omni Bridgeway Limited) Bentham IMF Capital Limited (now known as Omni Bridgeway Capital (Canada) Limited), Insolvency Institute of Canada and Canadian Association of Insolvency and Restructuring Professionals Interveners And IMF Bentham Limited (now known as Omni Bridgeway Limited) and Bentham IMF Capital Limited (now known as Omni Bridgeway Capital (Canada) Limited) Appellants; v. Callidus Capital Corporation, International Game Technology, Deloitte LLP, Luc Carignan, François Vigneault, Philippe Millette, Francis Proulx and François Pelletier Respondents, and Ernst & Young Inc. 9354-9186 Québec inc. 9354-9178 Québec inc. Insolvency Institute of Canada and Canadian Association of Insolvency and Restructuring Professionals Interveners

(117 paras.)

Appeal From:

ON APPEAL FROM THE COURT OF APPEAL FOR QUEBEC

Bankruptcy and insolvency ? Discretionary authority of supervising judge in proceedings under Companies' Creditors Arrangement Act ? Appellate review of decisions of supervising judge ? Whether supervising judge has discretion to bar creditor from voting on plan of arrangement where creditor is acting for improper purpose ? Whether supervising judge can approve third party litigation funding as interim financing ? Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36, ss. 11, 11.2.

The debtor companies filed a petition for the issuance of an initial order under the *Companies' Creditors Arrangement Act* ("*CCAA*") in November 2015. The petition succeeded, and the initial order was issued by a supervising judge, who became responsible for overseeing the proceedings. Since then, substantially all of the assets of the debtor companies have been liquidated, with the notable exception of retained claims for damages against the companies' only secured creditor. In September 2017, the secured creditor proposed a plan of arrangement, which later failed to receive sufficient creditor support. In February 2018, the secured creditor proposed another, virtually identical, plan of arrangement. It also sought the supervising judge's permission to vote on this new plan in the same class as the debtor companies' unsecured creditors, on the basis that its security was worth nil. Around the [page523] same time, the debtor companies sought interim financing in the form of a proposed third party litigation funding agreement, which would permit them to pursue litigation of the retained claims. They also sought the approval of a related super-priority litigation financing charge.

The supervising judge determined that the secured creditor should not be permitted to vote on the new plan because it was acting with an improper purpose. As a result, the new plan had no reasonable prospect of success and was not put to a creditors' vote. The supervising judge allowed the debtor companies' application, authorizing them to enter into a third party litigation funding agreement. On appeal by the secured creditor and certain of the unsecured creditors, the Court of Appeal set aside the supervising judge's order, holding that he had erred in reaching the foregoing conclusions.

Held: The appeal should be allowed and the supervising judge's order reinstated.

The supervising judge made no error in barring the secured creditor from voting or in authorizing the third party litigating funding agreement. A supervising judge has the discretion to bar a creditor from voting on a plan of arrangement where they determine that the creditor is acting for an improper purpose. A supervising judge can also approve third party litigation funding as interim financing, pursuant to s. 11.2 of the *CCAA*. The Court of Appeal was not justified in interfering with the supervising judge's discretionary decisions in this regard, having failed to treat them with the appropriate degree of deference.

The *CCAA* is one of three principal insolvency statutes in Canada. It pursues an array of overarching remedial objectives that reflect the wide ranging and potentially catastrophic impacts insolvency can have. These objectives include: providing for timely, efficient and impartial resolution of a debtor's insolvency; preserving and maximizing the value of a debtor's assets; ensuring fair and equitable treatment of the claims against a debtor; protecting the public interest; and, in the context of a commercial insolvency, balancing the costs and benefits of restructuring or liquidating the company. The architecture of the *CCAA* leaves the case-specific assessment and balancing of these objectives to the supervising judge.

[page524]

From beginning to end, each proceeding under the *CCAA* is overseen by a single supervising judge, who has broad discretion to make a variety of orders that respond to the circumstances of each case. The anchor of this discretionary authority is s. 11 of the *CCAA*, with empowers a judge to make any order that they consider appropriate in the circumstances. This discretionary authority is broad, but not boundless. It must be exercised in furtherance of the remedial objectives of the *CCAA* and with three baseline considerations in mind: (1) that the order sought is appropriate in the circumstances, and (2) that the applicant has been acting in good faith and (3) with due diligence. The due diligence consideration discourages parties from sitting on their rights and ensures that creditors do not strategically manoeuvre or position themselves to gain an advantage. A high degree of deference is owed to discretionary decisions made by judges supervising *CCAA* proceedings and, as such, appellate intervention will only be justified if the supervising judge erred in principle or exercised their discretion unreasonably.

A creditor can generally vote on a plan of arrangement or compromise that affects its rights, subject to any specific provisions of the *CCAA* that may restrict its voting rights, or a proper exercise of discretion by the supervising judge to constrain or bar the creditor's right to vote. Given that the *CCAA* regime contemplates creditor participation in decision-making as an integral facet of the workout regime, the discretion to bar a creditor from voting should only be exercised where the circumstances demand such an outcome. Where a creditor is seeking to exercise its voting rights in a manner that frustrates, undermines, or runs counter to the remedial objectives of the *CCAA* ? that is, acting for an improper purpose ? s. 11 of the *CCAA* supplies the supervising judge with the discretion to bar that creditor from voting. This discretion parallels the similar discretion that exists under the *Bankruptcy and Insolvency Act* and advances the basic fairness that permeates Canadian insolvency law and practice. Whether this discretion ought to be exercised in a particular case is a circumstance-specific inquiry that the supervising judge is best-positioned to undertake.

In the instant case, the supervising judge's decision to bar the secured creditor from voting on the new plan discloses no error justifying appellate intervention. When he made this decision, the supervising judge was intimately [page525] familiar with these proceedings, having presided over them for over 2 years, received 15 reports from the monitor, and issued approximately 25 orders. He considered the whole of the circumstances and concluded that the secured creditor's vote would serve an improper purpose. He was aware that the secured creditor had chosen not to value any of its claim as unsecured prior to the vote on the first plan and did not attempt to vote on that plan, which ultimately failed to receive the other creditors' approval. Between the failure of the first plan and the proposal of the (essentially identical) new plan, none of the factual circumstances relating to the debtor companies' financial or business affairs had materially changed. However, the secured creditor sought to value the entirety of its security at nil and, on that basis, sought leave to vote on the new plan as an unsecured creditor. If the secured creditor were permitted to vote in this way, the new plan would certainly have met the double majority threshold for approval under s. 6(1) of the *CCAA*. The inescapable inference was that the secured creditor was attempting to strategically value its security to acquire control over the outcome of the vote and thereby circumvent the creditor democracy the *CCAA* protects. The secured creditor's course of action was also plainly contrary to the expectation that parties act with due diligence in an insolvency proceeding, which includes acting with due diligence in valuing their claims and security. The secured creditor was therefore properly barred from voting on the new plan.

Whether third party litigation funding should be approved as interim financing is a case-specific inquiry that should have regard to the text of s. 11.2 of the *CCAA* and the remedial objectives of the *CCAA* more generally. Interim financing is a flexible tool that may take on a range of forms. This is apparent from the wording of s. 11.2(1), which is broad and does not mandate any standard form or terms. At its core, interim financing enables the preservation and realization of the value of a debtor's assets. In some circumstances, like the instant case, litigation funding furthers this basic purpose. Third party litigation funding agreements may therefore be approved as interim financing in *CCAA* proceedings when the supervising judge determines that doing so would be fair and appropriate, having regard to all the circumstances and the objectives of the Act. This requires consideration of the specific factors set out in s. 11.2(4) of the *CCAA*. These factors need not be mechanically applied or individually reviewed by the supervising judge, as not all of them will be significant in every case, nor are they exhaustive. [page526] Additionally, in order for a third party litigation funding agreement to be approved as interim financing, the agreement must not contain terms that effectively convert it into a plan of arrangement.

In the instant case, there is no basis upon which to interfere with the supervising judge's exercise of his discretion to approve the litigation funding agreement as interim financing. A review of the supervising judge's reasons as a whole, combined with a recognition of his manifest experience with the debtor companies' *CCAA* proceedings, leads to the conclusion that the factors listed in s. 11.2(4) concern matters that could not have escaped his attention and due consideration. It is apparent that he was focussed on the fairness at stake to all parties, the specific objectives of the *CCAA*, and the particular circumstances of this case when he approved the litigation funding agreement as interim financing. Further, the litigation funding agreement is not a plan of arrangement because it does not propose any compromise of the creditors' rights. The fact that the creditors may walk away with more or less money at the end of the day does not change the nature or existence of their rights to access the funds generated from the debtor companies' assets, nor can it be said to compromise those rights. Finally, the litigation financing charge does not convert the litigation funding agreement into a plan of arrangement. Holding otherwise would effectively extinguish the supervising judge's authority to approve these charges without a creditors' vote, which is expressly provided for in s. 11.2 of the *CCAA*.

Case Summary

Cases Cited

By Wagner C.J. and Moldaver J.

Applied: *Century Services Inc. v. Canada (Attorney General)*, 2010 SCC 60, [2010] 3 S.C.R. 379; **considered:** *Re Crystallex*, 2012 ONCA 404, 293 O.A.C. 102; *Laserworks Computer Services Inc. (Bankruptcy), Re*, 1998 NSCA 42, 165 N.S.R. (2d) 296; **referred to:** *Bayens v. Kinross Gold Corporation*, 2013 ONSC 4974, 117 O.R. (3d) 150; *Hayes v. The City of Saint John*, 2016 NBQB 125; *Schenk v. Valeant Pharmaceuticals International Inc.*, 2015 ONSC 3215, 74 C.P.C. (7th) 332; *Re Blackburn*, 2011 BCSC 1671, 27 B.C.L.R. (5th) 199; *Sun Indalex Finance, LLC v. United Steelworkers*, 2013 SCC 6, [2013] 1 S.C.R. 271; *Ernst & Young Inc. v. Essar Global Fund Ltd.*, 2017 ONCA 1014, 139 O.R. (3d) 1; [page527] *Third Eye Capital Corporation v. Ressources Dianor Inc./Dianor*

(1) The Evolving Nature of *CCAA* Proceedings

[12]

39 The *CCAA* is one of three principal insolvency statutes in Canada. The others are the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3 ("*BIA*"), which covers insolvencies of both individuals and companies, and the *Winding-up and Restructuring Act*, R.S.C. 1985, c. W-11 ("*WURA*"), which covers insolvencies of financial institutions and certain other corporations, such as insurance companies (*WURA*, s. 6(1)). While both the *CCAA* and the *BIA* enable reorganizations of insolvent companies, access to the *CCAA* is restricted to debtor companies facing total claims in excess of $5 million (*CCAA*, s. 3(1)).

40 Together, Canada's insolvency statutes pursue an array of overarching remedial objectives that reflect the wide ranging and potentially "catastrophic" impacts insolvency can have (*Sun Indalex Finance, LLC v. United Steelworkers*, 2013 SCC 6, [2013] 1 S.C.R. 271, at para. 1). These objectives include: providing for timely, efficient and impartial resolution of a debtor's insolvency; preserving and maximizing the value of a debtor's assets; ensuring fair and equitable treatment of the claims against a debtor; protecting the public interest; and, in the context of a commercial insolvency, balancing the costs and benefits of restructuring or liquidating the company (J. P. Sarra, "The Oscillating Pendulum: Canada's Sesquicentennial and Finding the Equilibrium for Insolvency Law", in J. P. Sarra and B. Romaine, eds., *Annual Review of Insolvency Law 2016* (2017), 9, at pp. 9-10; J. P. Sarra, *Rescue! The Companies' Creditors Arrangement Act* (2nd ed. 2013), at pp. 4-5 and 14; Standing Senate Committee on Banking, Trade and Commerce, *Debtors and Creditors Sharing the Burden: A Review of the Bankruptcy and Insolvency Act and the Companies' Creditors Arrangement Act* (2003), at pp. 9-10; R. J. Wood, *Bankruptcy and Insolvency Law* (2nd ed. 2015), at pp. 4-5).

[page542]

41 Among these objectives, the *CCAA* generally prioritizes "avoiding the social and economic losses resulting from liquidation of an insolvent company" (*Century Services*, at para. 70). As a result, the typical *CCAA* case has historically involved an attempt to facilitate the reorganization and survival of the pre-filing debtor company in an operational state - that is, as a going concern. Where such a reorganization was not possible, the alternative course of action was seen as a liquidation through either a receivership or under the *BIA* regime. This is precisely the outcome that was sought in *Century Services* (see para. 14).

42 That said, the *CCAA* is fundamentally insolvency legislation, and thus it also "has the simultaneous objectives of maximizing creditor recovery, preservation of going-concern value where possible, preservation of jobs and communities affected by the firm's financial distress ... and enhancement of the credit system generally" (Sarra, *Rescue! The Companies' Creditors Arrangement Act*, at p. 14; see also *Ernst & Young Inc. v. Essar Global Fund Ltd.*, 2017 ONCA 1014, 139 O.R. (3d) 1 ("*Essar*"), at para. 103). In pursuit of those objectives, *CCAA* proceedings have evolved to permit outcomes that do not result in the emergence of the pre-filing debtor company in a restructured state, but rather involve some form of liquidation of the debtor's assets under the auspices of the Act itself (Sarra, "The Oscillating Pendulum: Canada's Sesquicentennial and Finding the Equilibrium for Insolvency Law", at pp. 19-21). Such scenarios are referred to as "liquidating CCAAs", and they are now commonplace in the *CCAA* landscape (see *Third Eye Capital Corporation v. Ressources Dianor Inc./Dianor Resources Inc.*, 2019 ONCA 508, 435 D.L.R. (4th) 416, at para. 70).

[page543]

43 Liquidating CCAAs take diverse forms and may involve, among other things: the sale of the debtor company as a going concern; an "en bloc" sale of assets that are capable of being operationalized by a buyer; a partial liquidation or downsizing of business operations; or a piecemeal sale of assets (B. Kaplan, "Liquidating CCAAs: Discretion Gone Awry?", in J. P. Sarra, ed., *Annual Review of Insolvency Law* (2008), 79, at pp. 87-89). The ultimate commercial outcomes facilitated by liquidating CCAAs are similarly diverse. Some may result in the continued operation of the business of the debtor under a different going concern entity (e.g., the liquidations in *Indalex* and *Re Canadian Red Cross Society* (1998), 5 C.B.R. (4th) 299 (Ont. C.J. (Gen. Div.)), while others may result in a sale of assets and inventory with no such entity emerging (e.g., the proceedings in *Re Target Canada Co.*, 2015 ONSC 303, 22 C.B.R. (6th) 323, at paras. 7 and 31). Others still, like the case at bar, may involve a going concern sale of most of the assets of the debtor, leaving residual assets to be dealt with by the debtor and its stakeholders.

44 *CCAA* courts first began approving these forms of liquidation pursuant to the broad discretion conferred by the Act. The emergence of this practice was not without criticism, largely on the basis that it appeared to be inconsistent with the *CCAA* being a "restructuring statute" (see, e.g., *Uti Energy Corp. v. Fracmaster Ltd.*, 1999 ABCA 178, 244 A.R. 93, at paras. 15-16, aff'g 1999 ABQB 379, 11 C.B.R. (4th) 204, at paras. 40-43; A. Nocilla, "The History of the Companies' Creditors Arrangement Act and the Future of Re-Structuring Law in Canada" (2014), 56 *Can. Bus. L.J.* 73, at pp. 88-92).

45 However, since s. 36 of the *CCAA* came into force in 2009, courts have been using it to effect liquidating CCAAs. Section 36 empowers courts to authorize the sale or disposition of a debtor [page544] company's assets outside the ordinary course of business.[3] Significantly, when the Standing Senate Committee on Banking, Trade and Commerce recommended the adoption of s. 36, it observed that liquidation is not necessarily inconsistent with the remedial objectives of the *CCAA*, and that it may be a means to "raise capital [to facilitate a restructuring], eliminate further loss for creditors or focus on the solvent operations of the business" (p. 147). Other commentators have observed that liquidation can be a "vehicle to restructure a business" by allowing the business to survive, albeit under a different corporate form or ownership (Sarra, *Rescue! The Companies' Creditors Arrangement Act*, at p. 169; see also K. P. McElcheran, *Commercial Insolvency in Canada* (4th ed. 2019), at p. 311). Indeed, in *Indalex*, the company sold its assets under the *CCAA* in order to preserve the jobs of its employees, despite being unable to survive as their employer (see para. 51).

46 Ultimately, the relative weight that the different objectives of the *CCAA* take on in a particular case may vary based on the factual circumstances, the stage of the proceedings, or the proposed solutions that are presented to the court for approval. Here, a parallel may be drawn with the *BIA* context. In *Orphan Well Association v. Grant Thornton Ltd.*, 2019 SCC 5, [2019] 1 S.C.R. 150, at para. 67, this Court explained that, as a general matter, the *BIA* serves two purposes: (1) the bankrupt's financial rehabilitation and (2) the equitable distribution of the bankrupt's assets among creditors. However, [page545] in circumstances where a debtor corporation will never emerge from bankruptcy, only the latter purpose is relevant (see para. 67). Similarly, under the *CCAA*, when a reorganization of the pre-filing debtor company is not a possibility, a liquidation that preserves going-concern value and the ongoing business operations of the pre-filing company may become the predominant remedial focus. Moreover, where a reorganization or liquidation is complete and the court is dealing with residual assets, the objective of maximizing creditor recovery from those assets may take centre stage. As we will explain, the architecture of the *CCAA* leaves the case-specific assessment and balancing of these remedial objectives to the supervising judge.

(2) The Role of a Supervising Judge in *CCAA* Proceedings

[13]

47 One of the principal means through which the *CCAA* achieves its objectives is by carving out a unique supervisory role for judges (see Sarra, *Rescue! The Companies' Creditors Arrangement Act*, at pp. 18-19). From beginning to end, each *CCAA* proceeding is overseen by a single supervising judge. The supervising judge acquires extensive knowledge and insight into the stakeholder dynamics and the business realities of the proceedings from their ongoing dealings with the parties.

48 The *CCAA* capitalizes on this positional advantage by supplying supervising judges with broad discretion to make a variety of orders that respond to the circumstances of each case and "meet contemporary business and social needs" (*Century Services*, at para. 58) in "real-time" (para. 58, citing R. B. Jones, "The Evolution of Canadian Restructuring: Challenges for the Rule of Law", in J. P. Sarra, ed., *Annual Review of Insolvency Law 2005* (2006), 481, at p. 484). The anchor of this discretionary authority is s. 11, which empowers a judge "to make any order that [the judge] considers appropriate in the circumstances". This section has been described as "the engine" driving the statutory scheme [page546] (*Stelco Inc. (Re)* (2005), 253 D.L.R. (4th) 109 (Ont. C.A.), at para. 36).

49 The discretionary authority conferred by the *CCAA*, while broad in nature, is not boundless. This authority must be exercised in furtherance of the remedial objectives of the *CCAA*, which we have explained above (see *Century Services*, at para. 59). Additionally, the court must keep in mind three "baseline considerations" (at para. 70), which the applicant bears the burden of demonstrating: (1) that the order sought is appropriate in the circumstances, and (2) that the applicant has been acting in good faith and (3) with due diligence (para. 69).

50 The first two considerations of appropriateness and good faith are widely understood in the *CCAA* context. Appropriateness "is assessed by inquiring whether the order sought advances the policy objectives underlying the *CCAA*" (para. 70). Further, the well-established requirement that parties must act in good faith in insolvency proceedings has recently been made express in s. 18.6 of the *CCAA*, which provides:

> **Good faith**
>
> **18.6 (1)** Any interested person in any proceedings under this Act shall act in good faith with respect to those proceedings.
>
> **Good faith - powers of court**
>
> **(2)** If the court is satisfied that an interested person fails to act in good faith, on application by an interested person, the court may make any order that it considers appropriate in the circumstances.

(See also *BIA*, s. 4.2; *Budget Implementation Act*, *2019, No. 1*, S.C. 2019, c. 29, ss. 133 and 140.)

51 The third consideration of due diligence requires some elaboration. Consistent with the *CCAA* regime generally, the due diligence consideration discourages parties from sitting on their rights and ensures that creditors do not strategically manoeuver or [page547] position themselves to gain an advantage (*Lehndorff General Partner Ltd., Re* (1993), 17 C.B.R. (3d) 24 (Ont. C.J. (Gen. Div.)), at p. 31). The procedures set out in the *CCAA* rely on negotiations and compromise between the debtor and its stakeholders, as overseen by the supervising judge and the monitor. This necessarily requires that, to the extent possible, those involved in the proceedings be on equal footing and have a clear understanding of their respective rights (see McElcheran, at p. 262). A party's failure to participate in *CCAA* proceedings in a diligent and timely fashion can undermine these procedures and, more generally, the effective functioning of the *CCAA* regime (see, e.g., *North American Tungsten Corp. v. Global Tungsten and Powders Corp.*, 2015 BCCA 390, 377 B.C.A.C. 6, at paras. 21-23; *Re BA Energy Inc.*, 2010 ABQB 507, 70 C.B.R. (5th) 24; *HSBC Bank Canada v. Bear Mountain Master Partnership*, 2010 BCSC 1563, 72 C.B.R. (5th) 276, at para. 11; *Caterpillar Financial Services Ltd. v. 360networks Corp.*, 2007 BCCA 14, 279 D.L.R. (4th) 701, at paras. 51-52, in which the courts seized on a party's failure to act diligently).

52 We pause to note that supervising judges are assisted in their oversight role by a court appointed monitor whose qualifications and duties are set out in the *CCAA* (see ss. 11.7, 11.8 and 23 to 25). The monitor is an independent and impartial expert, acting as "the eyes and the ears of the court" throughout the proceedings (*Essar*, at para. 109). The core of the monitor's role includes providing an advisory opinion to the court as to the fairness of any proposed plan of arrangement and on orders sought by parties, including the sale of assets and requests for interim financing (see *CCAA*, s. 23(1)(d) and (i); Sarra, *Rescue! The Companies' Creditors Arrangement Act*, at pp. 566 and 569).

[page548]

Lemare Holdings Ltd. (Re), [2012] B.C.J. No. 2218

British Columbia Judgments

British Columbia Supreme Court

Vancouver, British Columbia

J.C. Grauer J.

Heard: October 16, 18 and 19, 2012.

Judgment: October 26, 2012.

Docket: S124409

Registry: Vancouver

[2012] B.C.J. No. 2218 | 2012 BCSC 1591 | 96 C.B.R. (5th) 35 | 223 A.C.W.S. (3d) 307 | 2012 CarswellBC 3294

IN THE MATTER OF the Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36, As Amended AND IN THE MATTER OF the Business Corporations Act, S.B.C. 2002, c. 57, As Amended AND IN THE MATTER OF a Plan of Compromise or Arrangement of Lemare Holdings Ltd., Lemare Lake Logging Ltd., Lone Tree Logging Ltd., C.&E. Roadbuilders Ltd., Coast Dryland Services Ltd., Dominion Log Sort Ltd., and Central Coast Industries Ltd., Petitioners

(94 paras.)

Case Summary

Bankruptcy and insolvency law — Companies' Creditors Arrangement Act (CCAA) matters — Application of Act — Debtor company — Compromises and arrangements — Claims — Where Crown affected — Application by Province to set aside Initial Order dismissed; application by petitioners for order excluding evidence tendered by Province in its application and for further stay and claims process order allowed in part — Court rejected Province's assertion petitioners were not insolvent when Initial Order granted — Amount of assessed stumpage and penalties claimed by Province against petitioners constituted a contingent claim — Reasonably foreseeable expectation of looming liquidity crisis existed at time of Initial Order — Provision made in claims process order to facilitate Province's claim in manner that preserved its ability to take advantage of Forest Act provisions.

Bankruptcy and insolvency law — Proceedings — Practice and procedure — Courts — Jurisdiction — CCAA matters — Evidence — Affidavits — Stays — Application by Province to set aside Initial Order dismissed; application by petitioners for order excluding evidence tendered by Province in its application and for further stay and claims process order allowed in part — Court rejected Province's assertion petitioners were not insolvent when Initial Order granted — Reasonably foreseeable expectation of a looming liquidity crisis existed at time of Initial Order — Excerpts of Province's affidavit that referred to information unlawfully seized from petitioners redacted — Petitioners' stay extended and claims process order accepted with minor modifications.

Application by the Province to set aside an Initial Order that had been granted pursuant to the Companies' Creditors Arrangement Act ("CCAA"); application by the petitioners for an order excluding certain evidence tendered by the Province in its application, for a further stay and for a claims process order ("CPO"). The petitioners were a group of companies that constituted an integrated forestry business. For a considerable time, the petitioners had been at loggerheads with the Province over stumpage that the Province claimed the petitioners owed. In May and June 2012, the petitioners received letters from the Province, supported by extensive documentation, which proposed to

56 Although courts have generally had regard to the BIA definition of "insolvent person" when dealing with insolvency under the CCAA, the modern trend is to take into account the different objectives of the CCAA. These address the interests of a broader group of stakeholders, and include a more comprehensive process to preserve the debtor company as a going concern.

57 Thus in *Century Services Inc. v. Canada (Attorney General)*, 2010 SCC 60, [2010] 3 S.C.R. 379 at para. 21, the Supreme Court of Canada described the CCAA regime as a flexible, judicially supervised reorganization process that allows for creative and effective decisions. It noted that with reorganizations becoming increasingly complex:

> [61] *... CCAA* courts have been called upon to innovate accordingly in exercising their jurisdiction beyond merely staying proceedings against the debtor to allow breathing room for reorganization. They have been asked to sanction measures for which there is no explicit authority in the *CCAA.*
>
> ...
>
> [70] ... Appropriateness under the *CCAA* is assessed by inquiring whether the order sought advances the policy objectives underlying the *CCAA*. The question is whether the order will usefully further efforts to achieve the remedial purpose of the *CCAA* -- avoiding the social and economic losses resulting from liquidation of an insolvent company.

58 In *Re Stelco Inc.* (2004), 48 C.B.R. (4th) 299 (Ont. Sup. Ct. J.); leave to appeal refused: [2004] O.J. No. 1903, 2004 CarswellOnt 2936 (C.A.), the Court dealt with a submission, like the Province's here, that the Initial Order should be reversed on the ground that Stelco was not a "debtor company" because it was not "insolvent" as defined by the BIA.

59 Mr. Justice Farley, whose views in this area do not bind me but are entitled to the highest respect, made the following observations, which I have taken the liberty of paraphrasing:

* *On timing*: the usual problem is leaving the application for an Initial Order too late. CCAA should be implemented at a stage prior to the company's death spiral. Thus objections in the reported cases have been based not on an absence of insolvency, but on the proposed plan being doomed to failure as coming too late. [Paras. 13-15]

* *On stakeholders*: these include not only the company and its creditors, but also its employees and their interest in a viable enterprise. Thus there is an emphasis on operational restructuring so that the emerging company will have the benefit of a long-term viable fix, to the advantage of all stakeholders. [Paras. 17-20]

* *On the test for insolvency*: given the time and steps involved in a reorganization, the condition of insolvency perforce requires an expanded meaning under the CCAA. What the debtor must do is meet the onus of demonstrating with credible evidence on a common sense basis that it is insolvent within the meaning required by the CCAA in the context and within the purpose of that legislation. The BIA definition of insolvent person is acceptable with the caveat that under the first branch (unable to meet obligations as they generally become due), 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. Considering the notion of 'insolvent' contextually and purposively, the question is whether, at the time of filing, there is a reasonably foreseeable 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 stay and ancillary protection and procedure by Court authorization pursuant to a CCAA order. [Paras. 26 and 40]

60 There is, of course, no precise and invariable formula. This is not a "cookie cutter" exercise. As Farley J. pointed out, the matter must be decided on the basis of credible evidence and common sense, employing a principled, purposive and contextual approach.

Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36, s. 11

Canada Statutes

R.S.C. 1985, c. C-36, s. 11 | L.R.C. 1985, ch. C-36, art. 11

Canada Statutes > Companies' Creditors Arrangement Act [ss. 1-63] > PART II JURISDICTION OF COURTS [ss. 9-18.6]

Notice

Current Version: Effective 18-09-2009

SECTION 11.

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.

Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36, s. 11.3

Canada Statutes

R.S.C. 1985, c. C-36, s. 11.3 | L.R.C. 1985, ch. C-36, art. 11.3

Notice

Current Version: Effective 18-09-2009

SECTION 11.3

Assignment of agreements

11.3 (1) On application by a debtor company and on notice to every party to an agreement and the monitor, the court may make an order assigning the rights and obligations of the company under the agreement to any person who is specified by the court and agrees to the assignment.

Exceptions

(2) Subsection (1) does not apply in respect of rights and obligations that are not assignable by reason of their nature or that arise under

(a) an agreement entered into on or after the day on which proceedings commence under this Act;

(b) an eligible financial contract; or

(c) a collective agreement.

Factors to be considered

(3) In deciding whether to make the order, the court is to consider, among other things,

(a) under an eligible financial contract;

(b) whether the person to whom the rights and obligations are to be assigned would be able to perform the obligations; and

(c) whether it would be appropriate to assign the rights and obligations to that person.

Restriction

(4) The court may not make the order unless it is satisfied that all monetary defaults in relation to the agreement - other than those arising by reason only of the company's insolvency, the commencement of proceedings under this Act or the company's failure to perform a non-monetary obligation - will be remedied on or before the day fixed by the court.

Copy of order

(5) The applicant is to send a copy of the order to every party to the agreement.

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

Canada Statutes

R.S.C. 1985, c. C-36, s. 36 | L.R.C. 1985, ch. C-36, art. 36

Canada Statutes > Companies' Creditors Arrangement Act [ss. 1-63] > PART III GENERAL [ss. 19-43] > Obligations and Prohibitions [ss. 35-36]

Notice

Current Version: Effective 01-11-2019

SECTION 36.

Restriction on disposition of business assets

36. (1) A debtor company in respect of which an order has been made under this Act may not sell or otherwise dispose of assets outside the ordinary course of business unless authorized to do so by a court. Despite any requirement for shareholder approval, including one under federal or provincial law, the court may authorize the sale or disposition even if shareholder approval was not obtained.

Notice to creditors

(2) A company that applies to the court for an authorization is to give notice of the application to the secured creditors who are likely to be affected by the proposed sale or disposition.

Factors to be considered

(3) In deciding whether to grant the authorization, the court is to consider, among other things,

(a) whether the process leading to the proposed sale or disposition was reasonable in the circumstances;

(b) whether the monitor approved the process leading to the proposed sale or disposition;

(c) whether the monitor filed with the court a report stating that in their opinion the sale or disposition would be more beneficial to the 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 or disposition on the 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.

Additional factors - related persons

(4) If the proposed sale or disposition is to a person who is related to the company, the court may, after considering the factors referred to in subsection (3), grant the authorization only if it is satisfied that

(a) good faith efforts were made to sell or otherwise dispose of the assets to persons who are not related to the company; and

(b) the consideration to be received is superior to the consideration that would be received under any other offer made in accordance with the process leading to the proposed sale or disposition.

Related persons

(5) For the purpose of subsection (4), a person who is related to the company includes

(a) a director or officer of the company;

(b) a person who has or has had, directly or indirectly, control in fact of the company; and

(c) a person who is related to a person described in paragraph (a) or (b).

Assets may be disposed of free and clear

(6) The court may authorize a sale or disposition free and clear of any security, charge or other restriction and, if it does, it shall also order that other assets of the company or the proceeds of the sale or disposition be subject to a security, charge or other restriction in favour of the creditor whose security, charge or other restriction is to be affected by the order.

Restriction - employers

(7) The court may grant the authorization only if the court is satisfied that the company can and will make the payments that would have been required under paragraphs 6(5)(a) and (6)(a) if the court had sanctioned the compromise or arrangement.

Restriction - intellectual property

(8) If, on the day on which an order is made under this Act in respect of the company, the company is a party to an agreement that grants to another party a right to use intellectual property that is included in a sale or disposition authorized under subsection (6), that sale or disposition does not affect that other party's right to use the intellectual property - including the other party's right to enforce an exclusive use - during the term of the agreement, including any period for which the other party extends the agreement as of right, as long as the other party continues to perform its obligations under the agreement in relation to the use of the intellectual property.

1991 CarswellOnt 205
Ontario Court of Appeal

Royal Bank v. Soundair Corp.

1991 CarswellOnt 205, [1991] O.J. No. 1137, 27 A.C.W.S. (3d) 1178,
46 O.A.C. 321, 4 O.R. (3d) 1, 7 C.B.R. (3d) 1, 83 D.L.R. (4th) 76

ROYAL BANK OF CANADA (plaintiff/respondent) v. SOUNDAIR CORPORATION (respondent), CANADIAN PENSION CAPITAL LIMITED (appellant) and CANADIAN INSURERS' CAPITAL CORPORATION (appellant)

Goodman, McKinlay and Galligan JJ.A.

Heard: June 11, 12, 13 and 14, 1991
Judgment: July 3, 1991
Docket: Doc. CA 318/91

Counsel: *J. B. Berkow* and *S. H. Goldman* , for appellants Canadian Pension Capital Limited and Canadian Insurers' Capital Corporation.
J. T. Morin, Q.C. , for Air Canada.
L.A.J. Barnes and *L.E. Ritchie* , for plaintiff/respondent Royal Bank of Canada.
S.F. Dunphy and *G.K. Ketcheson* , for Ernst & Young Inc., receiver of respondent Soundair Corporation.
W.G. Horton , for Ontario Express Limited.
N.J. Spies , for Frontier Air Limited.

Subject: Corporate and Commercial; Insolvency
Headnote
Receivers --- Conduct and liability of receiver — General conduct of receiver
Court considering its position when approving sale recommended by receiver.
S Corp., which engaged in the air transport business, had a division known as AT. When S Corp. experienced financial difficulties, one of the secured creditors, who had an interest in the assets of AT, brought a motion for the appointment of a receiver. The receiver was ordered to operate AT and to sell it as a going concern. The receiver had two offers. It accepted the offer made by OEL and rejected an offer by 922 which contained an unacceptable condition. Subsequently, 922 obtained an order allowing it to make a second offer removing the condition. The secured creditors supported acceptance of the 922 offer. The court approved the sale to OEL and dismissed the motion to approve the 922 offer. An appeal was brought from this order.
Held:
The appeal was dismissed.
Per Galligan J.A.: When a court appoints a receiver to use its commercial expertise to sell an airline, it is inescapable that it intends to rely upon the receiver's expertise and not upon its own. The court should be reluctant to second-guess, with the benefit of hindsight, the considered business decisions made by its receiver.
The conduct of the receiver should be reviewed in the light of the specific mandate given to him by the court. The order appointing the receiver did not say how the receiver was to negotiate the sale. The order obviously intended, because of the unusual nature of the asset being sold, to leave the method of sale substantially to the discretion of the receiver.
To determine whether a receiver has acted providently, the conduct of the receiver should be examined in light of the information the receiver had when it agreed to accept an offer. On the date the receiver accepted the OEL offer, it had only two offers: that of OEL, which was acceptable, and that of 922, which contained an unacceptable condition. The decision made was a sound one in the circumstances. The receiver made a sufficient effort to obtain the best price, and did not act improvidently.

The court must exercise extreme caution before it interferes with the process adopted by a receiver to sell an unusual asset. It is important that prospective purchasers know that, if they are acting in good faith, bargain seriously with a receiver and enter into an agreement with it, a court will not lightly interfere with the commercial judgment of the receiver to sell the assets to them.
Per McKinlay J.A. (concurring in the result): It is most important that the integrity of procedures followed by court-appointed receivers be protected in the interests of both commercial morality and the future confidence of business persons in their dealings with receivers. In all cases, the court should carefully scrutinize the procedure followed by the receiver. While the procedure carried out by the receiver in this case was appropriate, given the unfolding of events and the unique nature of the asset involved, it may not be a procedure that is likely to be appropriate in many receivership sales.
Per Goodman J.A. (dissenting): It was imprudent and unfair on the part of the receiver to ignore an offer from an interested party which offered approximately triple the cash down payment without giving a chance to the offeror to remove the conditions or other terms which made the offer unacceptable to the receiver. The offer accepted by the receiver was improvident and unfair insofar as two creditors were concerned.

Appeal from order approving sale of assets by receiver.

Galligan J.A. **:**

1 This is an appeal from the order of Rosenberg J. made on May 1, 1991. By that order, he approved the sale of Air Toronto to Ontario Express Limited and Frontier Air Limited, and he dismissed a motion to approve an offer to purchase Air Toronto by 922246 Ontario Limited.

2 It is necessary at the outset to give some background to the dispute. Soundair Corporation ("Soundair") is a corporation engaged in the air transport business. It has three divisions. One of them is Air Toronto. Air Toronto operates a scheduled airline from Toronto to a number of mid-sized cities in the United States of America. Its routes serve as feeders to several of Air Canada's routes. Pursuant to a connector agreement, Air Canada provides some services to Air Toronto and benefits from the feeder traffic provided by it. The operational relationship between Air Canada and Air Toronto is a close one.

3 In the latter part of 1989 and the early part of 1990, Soundair was in financial difficulty. Soundair has two secured creditors who have an interest in the assets of Air Toronto. The Royal Bank of Canada (the "Royal Bank") is owed at least $65 million dollars. The appellants Canadian Pension Capital Limited and Canadian Insurers' Capital Corporation (collectively called "CCFL") are owed approximately $9,500,000. Those creditors will have a deficiency expected to be in excess of $50 million on the winding up of Soundair.

4 On April 26, 1990, upon the motion of the Royal Bank, O'Brien J. appointed Ernst & Young Inc. (the "receiver") as receiver of all of the assets, property and undertakings of Soundair. The order required the receiver to operate Air Toronto and sell it as a going concern. Because of the close relationship between Air Toronto and Air Canada, it was contemplated that the receiver would obtain the assistance of Air Canada to operate Air Toronto. The order authorized the receiver:

> (b) to enter into contractual arrangements with Air Canada to retain a manager or operator, including Air Canada, to manage and operate Air Toronto under the supervision of Ernst & Young Inc. until the completion of the sale of Air Toronto to Air Canada or other person.

Also because of the close relationship, it was expected that Air Canada would purchase Air Toronto. To that end, the order of O'Brien J. authorized the Receiver:

> (c) to negotiate and do all things necessary or desirable to complete a sale of Air Toronto to Air Canada and, if a sale to Air Canada cannot be completed, to negotiate and sell Air Toronto to another person, subject to terms and conditions approved by this Court.

5 Over a period of several weeks following that order, negotiations directed towards the sale of Air Toronto took place between the receiver and Air Canada. Air Canada had an agreement with the receiver that it would have exclusive negotiating rights during that period. I do not think it is necessary to review those negotiations, but I note that Air Canada had complete

access to all of the operations of Air Toronto and conducted due diligence examinations. It became thoroughly acquainted with every aspect of Air Toronto's operations.

6 Those negotiations came to an end when an offer made by Air Canada on June 19, 1990, was considered unsatisfactory by the receiver. The offer was not accepted and lapsed. Having regard to the tenor of Air Canada's negotiating stance and a letter sent by its solicitors on July 20, 1990, I think that the receiver was eminently reasonable when it decided that there was no realistic possibility of selling Air Toronto to Air Canada.

7 The receiver then looked elsewhere. Air Toronto's feeder business is very attractive, but it only has value to a national airline. The receiver concluded reasonably, therefore, that it was commercially necessary for one of Canada's two national airlines to be involved in any sale of Air Toronto. Realistically, there were only two possible purchasers, whether direct or indirect. They were Air Canada and Canadian Airlines International.

8 It was well known in the air transport industry that Air Toronto was for sale. During the months following the collapse of the negotiations with Air Canada, the receiver tried unsuccessfully to find viable purchasers. In late 1990, the receiver turned to Canadian Airlines International, the only realistic alternative. Negotiations began between them. Those negotiations led to a letter of intent dated February 11, 1990. On March 6, 1991, the receiver received an offer from Ontario Express Limited and Frontier Airlines Limited, who are subsidiaries of Canadian Airlines International. This offer is called the OEL offer.

9 In the meantime, Air Canada and CCFL were having discussions about making an offer for the purchase of Air Toronto. They formed 922246 Ontario Limited ("922") for the purpose of purchasing Air Toronto. On March 1, 1991, CCFL wrote to the receiver saying that it proposed to make an offer. On March 7, 1991, Air Canada and CCFL presented an offer to the receiver in the name of 922. For convenience, its offers are called the "922 offers."

10 The first 922 offer contained a condition which was unacceptable to the receiver. I will refer to that condition in more detail later. The receiver declined the 922 offer and on March 8, 1991, accepted the OEL offer. Subsequently, 922 obtained an order allowing it to make a second offer. It then submitted an offer which was virtually identical to that of March 7, 1991, except that the unacceptable condition had been removed.

11 The proceedings before Rosenberg J. then followed. He approved the sale to OEL and dismissed a motion for the acceptance of the 922 offer. Before Rosenberg J., and in this court, both CCFL and the Royal Bank supported the acceptance of the second 922 offer.

12 There are only two issues which must be resolved in this appeal. They are:

(1) Did the receiver act properly when it entered into an agreement to sell Air Toronto to OEL?

(2) What effect does the support of the 922 offer by the secured creditors have on the result?

13 I will deal with the two issues separately.

1. Did the Receiver Act Properly in Agreeing to Sell to OEL?

14 Before dealing with that issue, there are three general observations which I think I should make. The first is that the sale of an airline as a going concern is a very complex process. The best method of selling an airline at the best price is something far removed from the expertise of a court. When a court appoints a receiver to use its commercial expertise to sell an airline, it is inescapable that it intends to rely upon the receiver's expertise and not upon its own. Therefore, the court must place a great deal of confidence in the actions taken and in the opinions formed by the receiver. It should also assume that the receiver is acting properly unless the contrary is clearly shown. The second observation is that the court should be reluctant to second-guess, with the benefit of hindsight, the considered business decisions made by its receiver. The third observation which I wish to make is that the conduct of the receiver should be reviewed in the light of the specific mandate given to him by the court.

15 The order of O'Brien J. provided that if the receiver could not complete the sale to Air Canada that it was "to negotiate and sell Air Toronto to another person." The court did not say how the receiver was to negotiate the sale. It did not say it was to call for bids or conduct an auction. It told the receiver to negotiate and sell. It obviously intended, because of the unusual nature of the asset being sold, to leave the method of sale substantially in the discretion of the receiver. I think, therefore, that the court should not review minutely the process of the sale when, broadly speaking, it appears to the court to be a just process.

16 As did Rosenberg J., I adopt as correct the statement made by Anderson J. in *Crown Trust Co. v. Rosenberg* (1986), 60 O.R. (2d) 87, 67 C.B.R. (N.S.) 320n, 22 C.P.C. (2d) 131, 39 D.L.R. (4th) 526 (H.C.) , at pp. 92-94 [O.R.], of the duties which a court must perform when deciding whether a receiver who has sold a property acted properly. When he set out the court's duties, he did not put them in any order of priority, nor do I. I summarize those duties as follows:

1. It should consider whether the receiver has made a sufficient effort to get the best price and has not acted improvidently.

2. It should consider the interests of all parties.

3. It should consider the efficacy and integrity of the process by which offers are obtained.

4. It should consider whether there has been unfairness in the working out of the process.

17 I intend to discuss the performance of those duties separately.

1. Did the Receiver make a sufficient effort to get the best price and did it act providently?

18 Having regard to the fact that it was highly unlikely that a commercially viable sale could be made to anyone but the two national airlines, or to someone supported by either of them, it is my view that the receiver acted wisely and reasonably when it negotiated only with Air Canada and Canadian Airlines International. Furthermore, when Air Canada said that it would submit no further offers and gave the impression that it would not participate further in the receiver's efforts to sell, the only course reasonably open to the receiver was to negotiate with Canadian Airlines International. Realistically, there was nowhere else to go but to Canadian Airlines International. In do ing so, it is my opinion that the receiver made sufficient efforts to sell the airline.

19 When the receiver got the OEL offer on March 6, 1991, it was over 10 months since it had been charged with the responsibility of selling Air Toronto. Until then, the receiver had not received one offer which it thought was acceptable. After substantial efforts to sell the airline over that period, I find it difficult to think that the receiver acted improvidently in accepting the only acceptable offer which it had.

20 On March 8, 1991, the date when the receiver accepted the OEL offer, it had only two offers, the OEL offer, which was acceptable, and the 922 offer, which contained an unacceptable condition. I cannot see how the receiver, assuming for the moment that the price was reasonable, could have done anything but accept the OEL offer.

21 When deciding whether a receiver had acted providently, the court should examine the conduct of the receiver in light of the information the receiver had when it agreed to accept an offer. In this case, the court should look at the receiver's conduct in the light of the information it had when it made its decision on March 8, 1991. The court should be very cautious before deciding that the receiver's conduct was improvident based upon information which has come to light after it made its decision. To do so, in my view, would derogate from the mandate to sell given to the receiver by the order of O'Brien J. I agree with and adopt what was said by Anderson J. in *Crown Trust Co. v. Rosenberg* , supra, at p. 112 [O.R.]:

> Its decision was made as a matter of business judgment *on the elements then available to it* . It is of the very essence of a receiver's function to make such judgments and in the making of them to act seriously and responsibly so as to be prepared to stand behind them.
>
> If the court were to reject the recommendation of the Receiver in any but the most exceptional circumstances, it would materially diminish and weaken the role and function of the Receiver both in the perception of receivers and in the

2015 BCSC 1204
British Columbia Supreme Court

Veris Gold Corp., Re

2015 CarswellBC 1949, 2015 BCSC 1204, [2015] B.C.W.L.D. 4800, 256 A.C.W.S. (3d) 765, 26 C.B.R. (6th) 310

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

In the Matter of the Canada Business Corporations Act, R.S.C. 1985, c. C-44

In the Matter of the Business Corporations Act, S.B.C. 2002, c. 57

In the Matter of Veris Gold Corp., Queenstake Resources Ltd., Ketza River Holdings, and Veris Gold USA, Inc., Petitioners

Fitzpatrick J.

Heard: May 28, 2015
Judgment: July 10, 2015
Docket: Vancouver S144431

Counsel: J. Sandrelli, T. Jeffries for Monitor, Ernst & Young Inc.
D. Vu, for Deutsche Bank A.G.
C. Ramsay, S. Irving, K. Mak for Moelis & Company
K. Jackson, D. Toigo for Whitebox Advisors LLC, WBox 2014-1 Ltd.
R. Morse, N. Vaartunou (A/S) for Attorney General of Nevada
C. Ramsay, K. Mak for Nevada Cement
C. Brousson, J. Bradshaw (A/S) for NV Energy
J. Porter for Government of Yukon
K. Siddall for AIG
S. Ross for Linde LLC

Subject: Insolvency; International

Headnote

Bankruptcy and insolvency --- Companies' Creditors Arrangement Act — Arrangements — Approval by court — "Fair and reasonable"

Assets of petitioner companies were gold mine in USA and mining properties in Canada — Initial order was granted in June 2014 due to steps taken by major secured creditor, DB to collect debt of approximately US$90 billion — Matters were stabilized, and in October 2014 court approved interim financing from WB in amount of US$12 million — Detailed sale and solicitation process was approved, but no qualified bids were received — Eventually petitioner entered into asset sale agreement with WBVG, which was wholly owned by WB — Monitor brought application to complete asset sale agreement — Application granted — Factors set out in s. 36(3) of Companies' Creditors Arrangement Act supported granting order — Process leading to transaction were fair and reasonable — Sale was best outcome for operational stakeholders — WBVG was to be assigned contracts as this would facilitate continuation of operations — Due to exigent and extraordinary circumstances, assignments were approved subject to US court being satisfied with notification to and service on counterparties to assigned contracts who did not received direct notice of application to approve sale.

APPLICATION by monitor for order approving and completing asset sale agreement.

***Fitzpatrick J.*:**

Introduction

1 This is a proceeding pursuant to the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36 (the "*CCAA*"). The assets of the petitioner companies (collectively, "Veris Gold") principally comprise a gold mine in the State of Nevada, United States of America and mining properties in Yukon, Canada.

2 There has been no shortage of effort in these proceedings to restructure the considerable debt or monetize the assets of Veris Gold for the benefit of the stakeholders. However, in the face of considerable operational setbacks and disappointing refinancing and sale results, those stakeholders now face two stark options: (i) allow the interim lender to deal with the assets in a receivership or liquidation scenario; or (ii) allow an orderly transfer of the assets to that interim lender by way of a credit bid which would allow operations in the U.S. to continue.

3 The court-appointed monitor, Ernst & Young Inc., (the "Monitor") now applies to complete the sale to a new entity created by the interim lender, which is said to provide the best result achievable in less than desirable circumstances.

Background Facts

4 Much of the history of these proceedings was set out in my reasons for judgment issued earlier this year: *Veris Gold Corp., Re*, 2015 BCSC 399 (B.C. S.C.) . For the purposes of this application, I will summarize that history as follows.

5 On June 9, 2014, this Court granted an initial order. This filing was necessary in light of the imminent steps that were to be taken by Veris Gold's major secured creditor, Deutsche Bank A.G. ("DB") to collect its debt of approximately US$90 million.

6 The Canadian filing was immediately followed by the Monitor commencing proceedings in Nevada pursuant to Chapter 15 of the *United States Bankruptcy Cod*e, 11 U.S.C. §§ 101-1532 (the "*Bankruptcy Code*").

7 Arising from orders granted in both the Canadian and Nevada proceedings and the agreements reached between Veris Gold and DB, matters were stabilized. Those orders and agreements allowed Veris Gold to continue its efforts to restructure its debt and equity with the assistance of Raymond James & Associates. In addition, firm milestone dates were put in place to conclude any refinancing and also to commence a sales process if those refinancing efforts were not successful.

8 In October 2014, this Court approved interim financing to be obtained from WBox 2014-1 Ltd. ("WBox") in the amount of US $12 million.

9 On November 18, 2014, this Court approved a detailed sale and solicitation process to be conducted by Moelis and Company ("Moelis"), again with firm deadlines for such matters as receipt of qualified bids. Although certain of the deadlines under the sales process were extended, no qualified bids were received by the extended bid deadline, January 30, 2015.

10 Following these disappointing sale results, the Monitor engaged in discussions with Veris Gold and the two stakeholders who appeared to have the only economic interest remaining in the assets, being DB and WBox. What was critical at this time was allowing Veris Gold to continue to operate in the ordinary course while these stakeholders considered their next steps.

11 In mid-February 2015, DB issued various notices of default under its security and the agreements reached earlier with Veris Gold. This also resulted in an immediate default under the interim financing agreements between Veris Gold and WBox. With a view to securing greater oversight over the continued operations of Veris Gold, DB later applied for and was granted an order expanding the powers of the Monitor on February 23, 2015. That order was later recognized by the U.S. court in the Chapter 15 proceedings on March 2, 2015.

12 By late March 2015, both DB and WBox were continuing to consider their options, including the possibility of making a credit bid for the assets. WBox conducted due diligence of the assets toward that possibility. The Monitor reported at that time that, absent a credit bid from DB, a credit bid from WBox was the only viable alternative.

13 Accordingly, on March 30, 2015, this Court granted an order extending the stay of proceedings to April 7, 2015 to enable completion of discussions in relation to a credit bid transaction whereby certain of Veris Gold's assets would be transferred to a nominee of WBox.

14 On April 2, 2015, Veris Gold suffered yet another operational setback when a fire occurred at the processing plant, causing an estimated shutdown of one week. The already tenuous cash problems were therefore exacerbated by the deferral of revenue of approximately US$4 million as a result of the shutdown. The timing of this difficulty was unfortunate, in that by this time, the Monitor had negotiated an agreement in principle with WBox for the purchase of the assets and an increase in the interim funding to allow operations to continue to the closing date.

15 Not surprisingly, the fire and ensuing difficulties caused WBox to delay any credit bid and the provision of further financing while it considered, among other things, the impact on the cash requirements of continuing operations. In addition, in light of what the Monitor described as the "mounting challenges", the Monitor and WBox moved to a consideration of liquidation scenarios. Preliminary work on various shutdown options, including care and maintenance, indicated that significant monies would have to be expended even before the assets could be transferred on an orderly basis to environmental regulators.

16 On April 7, 2015, this Court extended the stay of proceedings to April 24, 2015 in order to enable WBox and other interested parties to assess their options and to allow the Monitor time to have further discussions with the environmental regulators. During this extension of the stay period, WBox renewed discussions with the Monitor in respect of a potential transaction that would involve the equity participation of a financial partner. It was discussed that this partner could participate in WBox's nominee, which would be the entity to hold and operate Veris Gold's mining assets.

17 Discussions were also ongoing at this time whereby WBox would provide increased financing to Veris Gold in order to allow further time to finalize a transaction.

18 On April 24, 2015, this Court granted an order extending the stay of proceedings to June 12, 2015. In addition, at the request of the Monitor, an order was granted increasing the interim funding from WBox by US$3 million to US$15 million, which would allow Veris Gold's operations to continue. WBox approved a cash flow forecast and it was agreed that WBox would maintain control over payments made from this further facility. On April 29, 2015, the U.S. court approved this amendment to the interim financing facility.

19 On May 28, 2015, Veris Gold entered into an asset sale agreement (the "Agreement") with WBVG, LLC ("WBVG"). WBVG is an entity wholly owned by WBox although, as anticipated, WBox sought and obtained the future participation of another equity partner. The transaction provides that WBox will transfer a majority interest in WBVG to 2176423 Ontario Ltd., a company owned by Eric Sprott. Mr. Sprott was already involved in Veris Gold, having a 20% equity interest and also having a royalty interest in the Nevada mining properties.

20 The salient terms of the Agreement are as follows:

a) WBVG will purchase all tangible and intangible assets of Veris Gold, subject to certain defined excluded assets;

b) the Monitor is to continue efforts to sell the Ketza assets in Yukon over a 60-day period with any sale proceeds being payable to WBVG. If no sale occurs, then those assets will be transferred to WBVG;

c) WBVG is to assume certain obligations arising under assumed contracts, including all bonds, and also pay any "cure costs" relating to such assumed contracts, limited to US$10 million;

d) WBVG will assume the amounts owing to WBox under the interim lending facility and will pay certain of the court-ordered charges, such as the administration charges, having priority over the interim lender's charge in favour of WBox to a maximum of US$1.8 million;

e) WBVG will not assume any liabilities for pre-closing obligations;

f) all employees of Veris Gold are to be terminated on closing and WBVG may offer employment to some or all of them; and

g) a "DIP Financing Cash Reserve" fund estimated in the amount of US$3.1 million is to be established to pay certain post-filing obligations that will be outstanding as of the closing date, including employee wages and amounts due to suppliers and contractors for the supply of goods and services. Any funds remaining in the DIP Financing Cash Reserve after these payables have been satisfied shall be returned to WBVG.

21 The Agreement is still conditional in that it is subject to approval by both this Court and the U.S. court. Further conditions relate to obtaining an assignment of certain critical contracts, such as bonding agreements and other arrangements with the Nevada environmental regulators.

Statutory Framework

22 The authority of this Court to approve the sale is found in s. 36 of the *CCAA*. Section 36(3) of the *CCAA* sets out a list of non-exhaustive factors to be considered by the court:

(a) whether the process leading to the proposed sale or disposition was reasonable in the circumstances;

(b) whether the monitor approved the process leading to the proposed sale or disposition;

(c) whether the monitor filed with the court a report stating that in their opinion the sale or disposition would be more beneficial to the 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 or disposition on the 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.

23 A more general test has been restated, as discerned from the above factors, namely to consider the transaction as a whole and decide "whether or not the sale is appropriate, fair and reasonable": *White Birch Paper Holding Co., Re*, 2010 QCCS 4915 (C.S. Que.) at para. 49, (2010), 72 C.B.R. (5th) 49 (C.S. Que.), leave to appeal ref'd 2010 QCCA 1950 (C.A. Que.).

24 In addition, the principles identified in *Royal Bank v. Soundair Corp.* (1991), 4 O.R. (3d) 1 (Ont. C.A.) at 6 are helpful in considering whether to approve a sale:

1. Whether the party conducting the sale made sufficient efforts to obtain the best price and did not act improvidently;

2. The interests of all parties;

3. The efficacy and integrity of the process by which offers were obtained; and

4. Whether there has been any unfairness in the sales process.

25 Various authorities support that, in considering the test under s. 36 of the *CCAA*, the principles of *Soundair* remain relevant and indeed overlap some of the specific factors set out in s. 36(3): *Canwest Publishing Inc./Publications Canwest Inc., Re*, 2010 ONSC 2870 (Ont. S.C.J. [Commercial List]) at para. 13; *White Birch Paper Holding Co., Re* at para. 50; *PCAS Patient Care Automation Services Inc., Re*, 2012 ONSC 3367 (Ont. S.C.J. [Commercial List]) at para. 54.

Discussion

(a) CCAA Factors

2009 QCCS 6460
Cour supérieure du Québec

AbitibiBowater inc., Re

2009 CarswellQue 14189, 2009 QCCS 6460, EYB 2009-171229

In the matter of the plan of compromise or arrangement of: AbitibiBowater Inc.; Abitibi-Consolidated Inc., Bowater Canadian Holdings Inc., The other Petitioners listed on Schedules "A", "B" and "C", Petitioners, and Ernst & Young Inc., Monitor, v. The ad hoc Committee of the Senior Secured Nnoteholders and U.S. Bank National Association, Indenture Trustee for the Senior Secured Notes, Respondents, and DDJ Capital Management, LLC, Newstart Factors, inc., Stichting Pensionenfonds ABP, The Foothill Group, Inc. and Foothill CLO I, Ltd., Intervening Parties

Gascon J.C.S

Heard: 25 september 2009 - 29 september 2009
Judgment: 29 september 2009
Docket: C.S. Qué. Montréal 500-11-036133-094

Counsel: *Me Sean Dunphy, Me Guy P. Martel, Me Mélanie Béland, Me Joseph Reynaud*, for Petitioners
Me Avram Fishman, Me Gilles Paquin, for the Monitor
Me Robert Thornton, for the Monitor
Me Patrice Benoît, for Investissement Québec
Me Alain Riendeau, Attorneys for Silver Oak Capital LLC et al., DDJ Capital Management, LLC et al.
Me Gerald F. Kandestin, for Alcoa
Me Frederick L. Myers, Me Robert J. Chadwick, for the Ad hoc Committee of Bondholders
Me Marc Duchesne, Me François D. Gagnon, Me Vanessa Jodoin, Me Michael J. MacNaughton, for the Ad hoc Committee of the Senior Secured Noteholders and U.S. Bank National Association, Indenture Trustee for the Senior Secured Noteholders
Me Christian Roy, for Hydro-Québec

Subject: Insolvency

***Gascon J.C.S*:**

CORRECTED JUDGMENT OCTOBER 6, 2009 ON AMENDED MOTION FOR THE ISSUANCE OF AN ORDER AUTHORIZING THE SALE OF PETITIONER ABITIBI-CONSOLIDATED COMPANY OF CANADA'S INDIRECT INTEREST IN THE MCCORMICK HYDROELECTRIC FACILITY (#233)

THE MOTION AT ISSUE

1 On April 17, 2009, the Court issued an order (the « *Initial Order* ») pursuant to the CCAA [1] in respect of (i) Abitibi-Consolidated Inc. (»*ACI* ») and subsidiaries thereof (collectively, the « *Abitibi Petitioners* »), (ii) Bowater Canadian Holdings Inc. and subsidiaries thereof (collectively, the « *Bowater Petitioners* ») and (iii) certain partnerships [2].

2 By virtue of this Initial Order, Ernst & Young Inc. ("*EYI*") was appointed as monitor of the Petitioners (the "Monitor"). A stay of proceedings in favour of the Petitioners was also granted until May 14, 2009 (the "Stay Period"). On May 14, 2009, it was extended until September 4, 2009 (the "First Stay Extension Order"), and thereafter, until December 15, 2009 (the "Second Stay Extension Order").

j) an order (the « **Net** Cash **Proceeds Order** ») which provides that the cash component of the MPCo Share Proceeds and the ULC Reserve shall be paid to and be held by the Monitor; and

k) an order (the « **ULC** Borrowing **Order** ») which provides that the Abitibi Petitioners may not borrow any portion of the ULC Reserve except on terms and conditions permitted under the Implementation Agreement, including as to amount, security, priority, interest rates, fees, default, reporting and repayment, and except upon approval of the Court made on notice to the Trustee.

35 The parties to the Proposed Transactions have agreed to use reasonable commercial efforts to finalize all of the legal documentation to implement the Proposed Transactions by September 30, 2009 and to close the Proposed Transactions by October 15, 2009. If the Proposed Transactions have not closed by December 31, 2009, any party may terminate any of its obligations to complete the Proposed Transactions.

ANALYSIS AND DISCUSSION

36 The Court has jurisdiction to approve a sale of assets in the course of CCAA proceedings, notably when such a sale of assets is in the best interest of the stakeholders generally [3] .

37 In determining whether to authorize a sale of assets under the CCAA, the Court should consider, amongst others, the following key factors:

• have sufficient efforts to get the best price been made and have the parties acted providently;

• the efficacy and integrity of the process followed;

• the interests of the parties; and

• whether any unfairness resulted from the working out process.

38 These principles were enunciated in *Royal Bank v. Soundair Corp.* [4] . They are equally applicable in a CCAA sale situation [5] .

39 In this case, the Court considers that all these factors are satisfied.

40 First, the Petitioners' sales process for the ACCC Interest was proper even if limited to only one potential purchaser. There were valid and compelling reasons for the narrow focus of the sales process. Suffice to highlight in that regard the unique characteristics of the asset, the market in which the asset is situated and the external factors that most likely deterred or failed to attract potential purchasers.

41 The regulatory environment, the restrictions on pricing for the sale of electricity and the significant risk that the expiry of the MPCo Water Rights could disrupt the power production at MPCo indefinitely easily explain why the market for the ACCC Interest was severely limited.

42 The Petitioners have acted in good faith and with due diligence in their efforts to sell the ACCC Interest.

43 Second, even though the sale of the ACCC Interest was not widely canvassed in the market, in order to assess the reasonableness of the Purchase Price contemplated in the Proposed Transactions, the Monitor performed certain financial analyses.

44 Based on the compiled trading multiples, the review of transaction multiples and the discounted cash-flows analysis that he made, the Monitor was of the view that a Purchase Price of CDN$615 million for the ACCC Interest was fair and reasonable based on the assumptions, forecasts and other financial information that he considered.

45 The Proposed Transactions will generate estimated net proceeds before holdbacks and reserves of approximately CDN $547.9 million, of which up to CDN$97.2 million will be used to repay the ACI DIP Facility.

46 Third, the evidence indicates that the sale is warranted at this time because the Petitioners need cash to repay the ACI DIP Facility in accordance with the ACI DIP Agreement and to continue and implement their restructuring. Moreover, the projected costs of holding onto MPCo are too high, as the renewal of the water rights expiring in 2011 would require important infrastructure investments.

47 From that standpoint, the sale will benefit the whole economic community because it will allow the Petitioners to monetize certain non-liquid assets, use net cash proceeds to repay certain secured creditors (including the Senior Secured Noteholders) and secure cash to fund their ongoing restructuring effort, for the benefit of all stakeholders.

48 In fact, it is fair to say there may well be material prejudice to the Petitioners' stakeholders if the transaction does not proceed because the value of MPCo's assets would likely be far less in a liquidation scenario than in the proposed going concern sale.

49 In addition, despite the fact that ACCC will have to purchase electricity at a higher price as a result of the transaction, the Petitioners are of the view that the Baie-Comeau Mill will remain competitive.

50 Fourth, the MPCo sale and the Proposed Transactions form part of the Petitioners' continuing objective and strategy to reduce costs and improve profitability. The ACCC Interest is not required to continue the operations of the Abitibi Petitioners, nor is it vital for the Petitioners to retain it to successfully restructure their business.

51 Fifth, the Amended Motion provide to the Senior Secured Noteholders assurances that prove, in the end, to be satisfactory to safeguard their rights and protect the value of their security.

52 Finally, even though it is highly unusual in a CCAA proceeding to have significant levels of pre-filing obligations satisfied in full other than through a plan of arrangement as it is the case here with the HQ pre-filing claims, the Court finds that the unique situation at hand, coupled with the importance of the sale in the present restructuring, justify adopting a flexible approach to the issue.

53 The payment of these intercompany payables was imposed as an essential condition by HQ in order to enter into the MPCo transaction. Furthermore, this condition was negotiated prior to the CCAA proceedings, when the Purchase Price agreed upon was arrived at. This price remains the same even today.

54 While it is important to maintain a fair and delicate balance between the positions of all stakeholders in a CCAA restructuring, equitable treatment does not entail inflexibility at all costs. Here, it is clear that the chances of a successful restructuring are enhanced considerably by the Proposed Transactions. From that perspective, there is a definite benefit to all stakeholders by the approval of the Implementation Agreement.

55 To some extent, the situation bears some analogy with that of a critical vendor or key supplier. This is, no doubt, a critical asset sale with the only available purchaser in the market. Having to concede the payment of these HQ claims may not be the perfect outcome, but it remains, all things considered, an acceptable one under the circumstances.

56 Indeed, although this aspect of the Proposed Transactions is unusual, the Monitor notes, rightly so, that HQ could have achieved the same net economic terms had it simply required, in order to complete the transaction, a lower Purchase Price on account of all pre-transaction outstanding liabilities, including the pre-filing liabilities stayed as a result of the filing by the Petitioners.

57 Furthermore, the Monitor notes as well that, to the extent ACCC pays a liability on behalf of BCFPI (approximately CDN $9 million), ACCC will benefit from the intercompany charge described in the Initial Order.

58 All in all, the completion of the Proposed Transactions will both materially advance the restructuring of the Petitioners and benefit stakeholders, while the failure of the Proposed Transactions would greatly complicate the restructuring if not completely frustrate it.

59 The balance of interests clearly favours approval. The Monitor supports and recommends the approval sought. The recommendation of the Monitor, a court-appointed officer experienced in the insolvency field, carries great weight with the Court in any approval process. Absent some compelling, exceptional factor to the contrary, a Court should accept an applicant's proposed sale process where it is recommended by the Monitor and supported by the stakeholders [6] .

60 In view of the urgency in closing the Proposed Transactions rapidly, and to take away any uncertainty in a context where, after much discussions and compromises, the conclusions sought are acceptable to all, the Court is satisfied that provisional execution of this Judgment should be ordered.

FOR THESE REASONS, THE COURT:

61 *GRANTS* the Petitioners' *Amended Motion for the Issuance of an Order Authorizing the Sale of Petitioners' Interests in Manicouagan Power Company* (the « *Motion* »).

62 *EXEMPTS*, if applicable, the Petitioners from having to serve the Motion and from any notice or delay of presentation.

63 *DECLARES* that, unless otherwise provided, undefined capitalized terms and expressions used herein shall have the respective meanings ascribed thereto in the Second Amended Initial Order of the Honourable Mr. Justice Clement Gascon, J.S.C. of the Court dated May 6, 2009, as amended (the « *Initial Order* »).

Approval of Implementation Agreement and Related Transactions

64 *ORDERS* that the terms and conditions of a certain Implementation Agreement (the « *Implementation Agreement*) among Abitibi-Consolidated Inc., Abitibi Consolidated Company of Canada (»*ACCC* »), Manicouagan Power Company (»*MPCo* »), Alcoa Canada Ltée and Alcoa Ltd. (collectively, « *Alcoa* »), to which has intervened HQ Energie Inc., a wholly-owned subsidiary of Hydro-Quebec, a copy of which is filed as Exhibit R-1 to the Motion, are approved.

65 *ORDERS AND DECLARES* that Petitioners are authorized to implement and complete the transactions and steps contemplated in the Implementation Agreement and the Step Plan (Exhibit A thereto) (the « *Proposed Transactions* ») with such non-material alterations, amendments, deletions or additions as the parties thereto may agree to with the consent of the Monitor, and to perform the obligations contained in the Implementation Agreement.

66 *ORDERS* that in completing the Proposed Transactions, subject to the terms and conditions of the Implementation Agreement, the Petitioners are authorized:

a) to execute the agreements and to execute and deliver any documents and assurances governing or giving effect to the Implementation Agreement (including, without limitation, the directions of payment contemplated therein) as the Petitioners, in their discretion, may deem to be reasonably necessary or advisable to conclude the Proposed Transactions, including, without limitation, the execution of such deeds, contracts or documents, as may be contemplated in the Implementation Agreement and all such deeds, contracts or documents are hereby ratified, approved and confirmed (collectively with the Implementation Agreement, the « **Transaction Documents** »); and

b) to take such steps as are, in the opinion of the Petitioners, necessary or incidental to the performance of their obligations pursuant to the Implementation Agreement.

67 *ORDERS AND DECLARES* that this Order shall constitute the only authorization required by the Petitioners to proceed with the Proposed Transactions and that no shareholder or regulatory approval shall be required in connection with the Proposed Transactions save and for those contemplated in the Implementation Agreement.

Royal Bank of Canada v. Cow Harbour Construction Ltd., [2012] A.J. No. 141

Alberta Judgments

Alberta Court of Queen's Bench

Judicial District of Edmonton

K.D. Yamauchi J.

Heard: November 2-3, 2011.

Judgment: January 23, 2012.

Dockets: 1003 11241, 1003 05560; Bkcy Action No.: 24-115359

Registry: Edmonton

[2012] A.J. No. 141 | 2012 ABQB 59 | 75 C.B.R. (5th) 99 | [2012] 8 W.W.R. 209 | 59 Alta. L.R. (5th) 215 | 19 P.P.S.A.C. (3d) 31 | 98 B.L.R. (4th) 236 | 529 A.R. 147 | 211 A.C.W.S. (3d) 265 | 2012 CarswellAlta 198

IN THE MATTER OF the Bankruptcy and Insolvency Act, R.S.C. 1985, c. B-3, as amended In the Matter of the Companies' Creditors Arrangement Act, RSC 1985, c C-36, as amended AND IN THE MATTER OF a Plan of Arrangement of Cow Harbour Construction Ltd. Between Royal Bank of Canada, Plaintiff, and Cow Harbour Construction Ltd. and 1134252 Alberta Ltd., Defendants

(222 paras.)

Counsel

Walker W. MacLeod, for GE.

Joseph J. Bellissimo, for Scott Capital.

Kentigern A. Rowan, Q.C. and Stephanie A. Wanke, for Wajax.

Ryan Zahara, for Caterpillar Financial.

Jeremy H. Hockin, for Kempenfelt Vehicle Leasing (a Division of Equirex Vehicle Leasing 2007 Inc.), Alter Moneta Corporation, Concentra Financial, and Key Equipment.

Reasons for Judgment

K.D. YAMAUCHI J.

I. Nature of the Matter

1 Various equipment lessors (collectively, the Applicants) have applied for what they claim to be their proportionate share of funds that PricewaterhouseCoopers Inc. (PWC) currently holds, pending this Court's determination of whether their leases were subject to section 11.01(a) of the *Companies' Creditors Arrangement Act*, RSC 1985, c

C-36 (*CCAA*). PWC is the court-appointed receiver and manager of the assets, property and undertaking of Cow Harbour Construction Ltd. (Cow Harbour).

II. Procedural History

2 On April 7, 2010, Cow Harbour obtained a stay of proceedings against it (Initial Order) under *CCAA* s. 11.02. This Court extended the Initial Order from time to time by a number of subsequent court orders. Pursuant to the Initial Order, this Court appointed Deloitte LLP as monitor under the *CCAA* (Monitor).

3 Cow Harbour's primary business consisted of overburden removal and general contracting services for oil extraction companies in Fort McMurray, Alberta. Its assets consisted mainly of earth moving and hauling equipment. Much of the equipment that Cow Harbour used in its operations was leased from various parties.

4 On May 21, 2010, this Court directed the Monitor to provide all interested parties with a list of those leases which it had classified as ones entitling the respective lessors to receive ongoing monthly payments pursuant to *CCAA* s. 11.01. This Court gave any party who claimed to have such a lease, but whose claim was not included in the Monitor's list, until June 2, 2010 to advise the Monitor that it was disputing the classification, failing which it was barred from subsequently asserting that its lease entitled it to those ongoing monthly payments.

5 Disputes were registered in relation to a total of 58 leases (Disputed Leases).

6 Also on May 21, 2010, this Court directed Cow Harbour to pay over to the Monitor's counsel monies representing all monthly payments from April 1, 2010, that Cow Harbour would have paid to lessors under the Disputed Leases, or leases which had not yet been categorized (Disputed Lease Funds). This Court directed the Monitor's counsel to hold the Disputed Lease Funds pending resolution of disputes pertaining to categorization of the Disputed Leases.

7 It became clear as matters progressed that Cow Harbour was not going to be able to restructure it affairs through refinancing, compromise or an equity restructuring. Rather, the proceedings evolved into a liquidation. PWC was appointed as transaction facilitator to assist the various parties in their negotiations. Acting in that capacity, PWC negotiated a potential sale of certain of Cow Harbour's assets to Aecon Group Inc. (Aecon). On August 10, 2010, PWC's acceptance of Aecon's letter of intent received this Court's endorsement, subject to the parties later applying for court approval of an asset purchase agreement and vesting order.

8 On August 25, 2010, the Royal Bank of Canada (RBC) successfully applied for a receivership order, pursuant to which this Court appointed PWC as receiver and manager of the assets, property and undertaking of Cow Harbour (Receiver). This Court then approved the asset purchase agreement and granted a vesting order in Aecon's favour. The transaction contemplated by the asset purchase agreement closed on August 26, 2010.

9 The Disputed Lease Funds were transferred to the Receiver pending resolution of the disputes over classification of the Disputed Leases.

10 RBC was paid out in full through the *CCAA* and receivership proceedings. The secured creditor holding the next general security over Cow Harbour's assets, property and undertaking is GE Capital Equipment Financing G.P. (GE).

11 The Receiver has settled many of the issues between Cow Harbour and various third parties, including many of the lessors under the Disputed Leases. However, it continues to hold back a portion of the Disputed Lease Funds until this Court's determination of entitlement to those funds.

III. Issue

12 The Applicants ask this Court to determine which of the remaining Disputed Leases fall within *CCAA* s. 11.01(a). This, in turn, will determine which party or parties are entitled to a portion of the Disputed Lease Funds.

IV. Law

A. Legislation

13 Section 11.01(a) of the *CCAA* provides:

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

(A) prohibiting a person from requiring immediate payment for ... use of leased ... property or other valuable consideration provided after the order is made.

14 Section 11.02 of the *CCAA* provides for a stay of proceedings. It states:

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.

B. General Legal Principles

15 Section 11.02 of the *CCAA* allows a court to order a stay of proceedings on an initial application under the *CCAA* in respect of a debtor company. This is in keeping with the general policy underlying the *CCAA*, which is to allow a debtor corporation to restructure its corporate or financial affairs in a way that will permit it to continue on as a going concern, without being hampered by those who wish to enforce their previously bargained for rights. As the Ontario Court of Appeal commented in ***Re Nortel Networks Corp.***, 2009 ONCA 833 at para 16, 59 CBR (5th) 23 [***Nortel***], "[t]he primary instrument provided by the *CCAA* to achieve its purpose is the power of the court to issue a broad stay of proceedings under s. 11. That power includes the power to stay the <u>debt obligations</u> of the company" (emphasis added). Courts have given the *CCAA* a wide and liberal construction to facilitate this policy objective (see *e.g.* ***Chef Ready Food Ltd. v. HongKong Bank of Canada*** (1990), 51 BCLR (2d) 84 (CA)).

16 While a debtor corporation is proceeding through the *CCAA* restructuring process, it must still carry on its business. It hardly seems fair to require a person to continue to supply the debtor corporation with goods or services, or to allow the debtor corporation to continue to use leased property, without that person being compensated for those goods, services or use. Section 11.01(a) of the *CCAA* allows for that compensation.

17 As noted in ***Re Smith Brothers Contracting Ltd.*** (1998), 53 BCLR (3d) 264 at para 3 (SC) [***Smith Brothers***], Parliament added what is now s. 11.01 to the *CCAA* as part of a set of amendments proclaimed in force on September 30, 1997. Suche J. in ***Re Winnipeg Motor Express Inc.***, 2009 MBQB 204, 243 Man R (2d) 31 [***Re Winnipeg***], leave to appeal to CA refused, 2009 MBCA 110, [2009] 12 WWR 224, suggested that Parliament may have added this provision to clarify the point made in ***Quintette Coal Ltd. v. Nippon Steel Corp.*** (1990), 51 BCLR (2d) 105 (CA) [***Quintette***], that a stay would never be used to enforce the continuous supply of goods or services without payment for current deliveries. She also commented that the amendment brought the *CCAA* in line with the *Bankruptcy and Insolvency Act*, RSC 1985, c B-3 [*BIA*], which contains a similar provision relating to proposals.

18 To further facilitate the policy objective of the *CCAA*, courts have given *CCAA* s. 11.01(a), which is an exception to the stay provision, a narrow construction (***Nortel*** at para 17). They have differentiated between a "true lease," in which the debtors' corporation is paying for use of the property, and a debt obligation clothed in the guise of a lease, i.e., a financing lease in which the debtors' corporation is "earning equity" in the property. Courts and writers have used the term "financing lease," "security lease," "financial leasing arrangement" or similar terms to describe the latter type of arrangement (referred to here as a financing lease). It is only the debtor corporation's obligations under a true lease that courts have excepted from the stay of proceedings, not its obligations under a financing lease (***Smith Brothers*** at para 61).

19 Canadian courts have accepted the conclusion of Bauman J. (as he then was) in ***Smith Brothers*** that a true lease, being a bailment of property, falls within the *CCAA* s. 11.01(a) exception, while a financing lease does not. They also have endorsed his approach to distinguishing between the two types of arrangements (see *e.g.* ***Re International Wallcoverings Ltd.*** (1999), 28 CBR (4th) 48 (Ont Ct Jus (Gen Div)) [***International Wallcoverings***]; ***Re Sharp-Rite Technologies Ltd.***, 2000 BCSC 122. In ***Re PSINET Ltd.*** (2001), 26 CBR (4th) 288 at para 19 (Ont SCJ) [***PSINET***], Swinton J. stated:

> In my view, ***Smith Brothers Contracting Ltd.*** was correct in determining that [*CCAA* s. 11.01(a)] is to apply to payments for the use of property provided after the stay order -- that is, where a party provides new credit to the debtor following the stay. The payments under the leases here are not that type of payment. These leases are clearly financing arrangements, whose purpose is to secure a loan which was provided before the stay order was made, and the payments owing are repayments for that loan. Therefore, the leases here do not fall within [*CCAA* s. 11.01(a)] of the Act, and the order of Farley J. which prohibits the company from making payments under them is consistent with the purpose of the Act. Any other determination would give the RBC an unfair advantage when compared to other creditors of the applicants, who are bound by the stay.

20 While initially having questioned in oral reasons on August 25, 2010, whether it might be worthwhile to re-examine the approach that Bauman J. took in ***Smith Brothers***, this Court concluded the approach was sound, given that *CCAA* s. 11.01(a) is to be narrowly construed. The substance and not the form of the arrangement between the debtor corporation and the other contracting party is of importance and, unless there is a sound policy reason for doing so, the court should not give an advantage to one creditor over another.

21 Why did this Court initially question the reasoning in ***Smith Brothers***?

22 Bauman J. relied heavily on Professor Ronald CC Cuming's article, "True Leases and Security Leases Under Canadian Personal Property Security Acts" (1983) 7 Can Bus LJ 251, in arriving at his conclusions. As is apparent from the title, Professor Cuming's article dealt with differentiating leases for purposes of personal property security legislation, not insolvency legislation.

23 The *CCAA* does not expressly incorporate personal property security legislation concepts. Unlike such legislation, the *CCAA* does not distinguish between a true lease and a financing lease.

24 The way in which courts have used personal property security legislation concepts when they are dealing with *CCAA* proceedings, and the tension that this approach creates, was discussed by Professor Roderick J. Wood in his article, "The Definition of Secured Creditor in Insolvency Law" (2010) 25 BFLR 341.

25 Professor Wood recognized that the *CCAA* does not expressly deem a lessor in a financing lease transaction to be a "secured creditor" rather than an owner of the goods. He remarked that the definitions of "secured creditor" and "security interest" in insolvency law (the *CCAA* and *BIA*) do not adopt personal property security legislation terminology (at p 347). He noted that courts have held that the broader definition of the term "secured creditor" in the *Income Tax Act*, RSC 1985, c one (5th Supp.) (*ITA*) does not encompass lessors under a financing lease. Professor Wood recognized the difficulty in interpreting the definition of "a secured creditor" in the *CCAA* as including a lessor under a title retention device such as a financing lease, given that courts have not done so in the context of the broader definition in the *ITA*. He expressed the view that the best way to resolve this tension would be for Parliament to clarify federal insolvency legislation, suggesting at p. 356 that:

> It would also produce a proper dovetailing of the federal insolvency provisions. For example, the insolvency statutes provide that a stay of proceedings does not prevent a lessor from requiring immediate payment for use of the leased property. This gives the lessor the ability to collect post-commencement lease payments. Courts have held that this provision only applies to true leases and not to security leases. The latter are

> treated in the same manner as other security interests and the debtor is able to retain possession of the goods without the need to satisfy the post commencement payments. This further demonstrates that the division between true leases and security leases that is produced by the application of the substance test of the *PPSA* is being recognized in insolvency law, and that an amendment of the definition of secured creditor to reflect this fact is the most sensible solution.

26 When examining ***Smith Brothers*** closely, it appears that Bauman J. was simply saying that the logic that Professor Cuming applied when differentiating between true leases and financing leases in the context of personal property security legislation applies equally to *CCAA* proceedings. Said differently, *CCAA* s. 11.01(a) protects parties who provide goods and services to the debtor corporation after a court grants an initial order, but not "creditors" to whom the debtor corporation has "debt obligations." This would put the latter in a better position *vis-a-vis* the debtor corporation than the debtor corporation's other creditors.

27 As previously stated, this Court is of the view that Bauman J's decision with respect to this issue is in keeping with the *CCAA*'s underlying policy objectives.

28 It is arguable, however, that Blair J. in ***International Wallcoverings*** left the door open for a court to find that a financing lease could fall within *CCAA* s. 11.01(a), when he said at para 4:

> While I would not go so far as to say, [*CCAA* s. 11.01(a)] requires payment under all leasing arrangements, or (on the other hand) that it could never encompass a financial leasing arrangement, I am satisfied that in the particular circumstances of this case the reasoning of ***Smith Brothers*** is applicable and that the arrangements in question are more akin to equipment purchase financing arrangements ...

29 He used the ***Smith Brothers*** true lease/financing lease analysis in reaching his conclusion. He did not speculate as to the type of situation where *CCAA* s. 11.01(a) might encompass a financing lease arrangement.

30 ***Winnipeg Motor*** could be considered one such case, and, as the result, is contrary to what might be expected when using the ***Smith Brothers*** analysis.

31 ***Winnipeg Motor*** dealt with the proper distribution of interim financing and administrative charges incurred after the court granted an initial order under the *CCAA*. The monitor recommended that the charges be distributed among the secured creditors based on a *pro rata* recovery. Two parties claimed to be true lessors. The court referred to the distinction made in ***Smith Brothers*** between true leases and financing leases. It commented that the exclusion of financing leases from *CCAA* s. 11.01(a) makes perfect sense based on the notion of ownership, as a financing lessor cannot seek the benefits of ownership when it has given it away (assuming the lessee has been acquiring equity in the leased goods). It also suggested that the narrow construction of *CCAA* s. 11.01(a) as limiting the obligation of the debtor to make payments for "use" is consistent with the idea that a supplier cannot be expected to continue to provide its product without payment.

32 The court in ***Winnipeg Motor*** noted the financing lessors' complaint that they had been unduly prejudiced by the stay of proceedings. They argued that not only were they not being paid while the debtor corporation was using their assets for the benefit of the other stakeholders, but the debtor corporation was deteriorating their underlying security in the process. They maintained that this violated one of the fundamental objectives of the stay of proceedings: preventing one creditor from obtaining an advantage over other creditors during the stay period. The court at paras 60-62 suggested that the fact true lessors were entitled to be paid aggravated the problem, stating:

> It is difficult to know how this situation can be remedied, given that the whole point of the *CCAA* is to relieve a company of ongoing financial burden to allow it the opportunity to restructure. In this case, for example, [the debtor corporation] would not have succeeded had it been obliged to pay for its equipment during the entirety of the restructuring.
>
> On the particular facts of this case, this issue became somewhat easier to address given the nature of [the debtor corporation's] business. Equipment to a transportation company is akin to raw goods to a manufacturer, and I was of the opinion that if [the debtor corporation] was going to be viable, at a certain

> point it would have to demonstrate it could pay for the essential means of production. Otherwise, there would be no purpose to continue the stay. Accordingly, I ordered that financing leases would be paid as of August 1, 2008.
>
> I say all this not to justify or revisit the basis for my earlier decision, but to get to the point that in considering what is equitable, undue prejudice is a reason to adjust what would otherwise be a uniform approach. I am satisfied that equipment lessors in a business operation such as [the debtor corporation's] do suffer undue prejudice. In this case, however, the equipment lessors were paid as of August 1. Being financing leases, those payments were not just for use, but included some amount on account of equity. I conclude, then, that the undue prejudice suffered has been recognized, *albeit* not totally, perfectly or precisely, but, in my view, in an amount sufficient amount to justify the uniform application of the methodology proposed by the monitor.

33 Of interest, the court in ***Winnipeg Motor*** required one of the debtor corporation's true lessors to contribute to the court-ordered charges, as it had derived the same benefit from the *CCAA* proceedings as the financing lessors.

34 In ***Re Clayton Construction Co. Ltd.***, 2009 SKQB 397, 59 CBR (5th) 213 [***Clayton Construction***], the debtor corporation sought an extension of a *CCAA* stay of proceedings. Rothery J. granted the extension, but also allowed the payment of interest that the debtor corporation owed to nine of its equipment lessors as a means of compensating them for the use and depreciation of their equipment. The debtor corporation required the equipment to complete its contracts. The court determined that the monthly interest payments to the equipment lessors would not prejudice the other creditors. The major secured creditor had benefited from the accounts receivable generated by the debtor's use of the equipment and the unsecured creditors likely would not have received any benefit, had the equipment lessors withdrawn their support for the restructuring process.

35 ***Winnipeg Motor*** and ***Clayton Construction*** might be responses to the non-peer reviewed journal articles that criticize the ***Smith Brothers*** approach that courts have taken to the issue before this Court (see *e.g.* Steven J. Weisz, Linc A. Rogers & Stacy McLean, "Striking an Imbalance: The Treatment of Equipment Lessors Under Section 11.3 of the *CCAA*" (2003) 20:5 Nat'l Insolv Rev 45 at 48-49; Jeffrey C. Cahart, "Should There be Special Rules in Commercial Reorganizations for Equipment Lessors?" (2002) 15:2 Comm Insol R 13; Harvey G. Chaiton and John R. Hutchins, "Equipment Lessors in Restructurings: Hostage Lenders" (2009) 21 Comm Insol R 3).

36 One of the themes that runs through these articles is that it is unfair for courts to allow creditors that hold general security to gain a benefit from the debtor corporation's use of the leased equipment during the stay period. Cahart commented at p. 15:

> ... it is simply unfair to allow a debtor to continue to use (and to depreciate) a piece of (perhaps essential) equipment which the debtor only has because of the equipment lessor's financing while the debtor pursues a reorganization and/or a sale as a going concern (as has happened in so many *CCAA* cases) possibly over a very extended period. Again, unlike lenders with more general security, equipment lessors (usually) only have recourse to a specific asset. Is it fair to allow, for instance, a mining company under *CCAA* protection to continue to use a specialized leased truck, continue to wear it down and to diminish its value, for 11 months for free, while the company pursues sale as a going concern and/or reorganization based on the company's going concern value? Among other things, the availability of the truck to the company over time: (i) contributes to the going concern value of the company (and the preservation of which is at the heart of what the *CCAA* is trying to achieve); and (ii) allows the company to produce product which is turned into cash and which goes to pay down an operating lender. Yet under the current jurisprudence, the relevant equipment lessor probably receives nothing during the stay period - not even its regular monthly payments, let alone any kind of "premium" for its contribution to the going concern value or to the ability of the company to generate cash.

37 The problem, however, is that one creditor should not receive "an unfair advantage when compared to other creditors of the applicants, who are bound by the stay" (***PSINET*** at para 19). If some creditors are to be bound by the stay of proceedings, all creditors must be bound. Any contrary approach invariably would lead to every creditor attempting to argue that its interests are being prejudiced by the stay of proceedings in one way or another, with the end result that the stay of proceedings would prove meaningless.

38 ***Smith Brothers*** concluded that courts must differentiate between true leases and financing leases. Is this what the legislation says?

39 If certain portions of *CCAA* s. 11.01(a) are emphasized, the legislation could be read differently. For example, *CCAA* s. 11.01(a) might be read as stating that: "No order made under section 11 or 11.02 has the effect of prohibiting a person from requiring immediate payment for ... use of leased ... property ... provided after the order is made" (emphasis added). In other words, the phrase "provided after the order is made" might refer to "leased property." In that case, lessors of pre-stay leases, whether true or financing, would be subject to the stay of proceedings. Only lessors of property leased post-stay could demand that the debtor corporation make its lease payments. This would be in keeping with judicial interpretation of the balance of *CCAA* s. 11.01(a). For example, a supplier may provide goods or services to the debtor corporation post-stay on the basis of "cash on delivery."

40 This type of interpretation would not be unusual, as Canadian courts, including the Alberta Court of Appeal, have taken such a grammatical-interpretative approach when they have considered, for example, *BIA* s. 178(1)(d). That section provides:

> 178(1) An order of discharge does not release the bankrupt from
>
> ...
>
> (d) any debt or liability arising out of fraud, embezzlement, misappropriation or defalcation while acting in a fiduciary capacity ...

41 The question has arisen whether the words "while acting in a fiduciary capacity" qualify only the word "defalcation" or whether they qualify all of the listed factors, including fraud, embezzlement, misappropriation and defalcation. Courts have held that the latter is the proper interpretation (see *e.g*. ***Confederation Life Insurance Co. v. Waselenak***, [1998] 5 WWR 712, 57 Alta LR (3d) 3 (QB), affd 2000 ABCA 136; ***166404 Canada Inc. v. Coulter*** (1998), 4 CBR (4th) 1 (Ont CA), leave to appeal to SCC refused, [1998] S.C.C.A. No. 231, (1998), 223 NR 395 (note); ***Ross & Associates v. Palmer***, 2001 MBCA 17, 22 CBR (4th) 140; ***Re Brant*** (1984), 52 CBR (NS) 317 (Ont SC)).

42 Including all pre-stay leases in the stay of proceedings would be in keeping with the broad and liberal interpretation that courts have given to the *CCAA*, which is to provide the debtor corporation with "breathing space" in which to determine whether it is in a position to restructure its affairs and to facilitate its survival. Including only post-stay leases under *CCAA* s. 11.01(a) also would be in keeping with the narrow interpretation of transactions that are excepted from the stay of proceedings. It would simplify *CCAA* proceedings involving equipment leases.

43 This interpretation, however, does not give weight to the word "use" in *CCAA* s. 11.01(a). In making the true lease/financing lease distinction, Bauman J. in ***Smith Brothers*** and courts in subsequent cases have sought to do just that. They have read the section as stating, "No order made under section 11 or 11.02 has the effect of prohibiting a person from requiring immediate payment for ... use of leased ... property ... provided after the order is made" (emphasis added). In other words, it is "use" of the leased property which is provided after a court makes the initial order.

44 A true lease, in essence, is a bailment contract such that ownership of the leased goods remains with the bailor/lessor and the bailee/lessee pays for "use" of those goods. In ***Punch v. Savoy's Jewellers Ltd.*** (1986), 54 OR (2d) 383 at para 17 (CA), the court defined bailment as follows:

> ... Bailment has been defined as the delivery of personal chattels on trust, usually on a contract, express or implied, that the trust shall be executed and the chattels be delivered in either their original or an altered form as soon as the time for which they were bailed has elapsed. It is to be noted that the legal relationship of bailor and bailee can exist independently of a contract. It is created by the voluntary taking into custody of goods which are the property of another.

(See also ***Visscher v. Triple Broek Holdings Ltd.***, 2006 ABQB 259, 399 AR 184 at paras 27-28; ***Letourneau v. Otto Mobiles Edmonton (1984) Ltd***., 2002 ABQB 609, 315 AR 232 at para 23).

45 The central character of a true lease is "payment for use." Bauman J. in ***Smith Brothers*** at para 48 adopted the following statement in Professor Cuming's above-referenced article to expand on this principle:

> Under a true lease, the lessor surrenders his possessory right in chattels to the lessee in return for an undertaking by the lessee to perform certain acts which usually involve the payment of money to the lessor. The lessee has obligations, but the transaction cannot be characterized as a security agreement because the interest of the lessor is not related to those obligations. In other words, the lessor does not remain owner merely to ensure or to induce performance of the lessee's obligations. He remains owner because a bailment contract does not involve the transfer of ownership to the bailee.

46 Bauman J. concluded in ***Smith Brothers*** at para 61:

> It is only payments for the use of leased property that are excepted from a s. 11 stay order under [*CCAA* s. 11.01(a)]. Payments for use and equity are not. Similarly payments for use and equity and an option to purchase are not. This is another reason to conclude ... [*CCAA* s. 11.01(a)] is not inclusive of all forms of lease.

47 This is a curious statement inasmuch as it might be seen as suggesting that a court should identify what portion of the lease payments made under the instrument is for use rather than for acquisition of equity (and, perhaps, of the option to purchase). This approach is not in keeping with other statements that Bauman J. made in ***Smith Brothers***. In this Court's view, the instrument is either a financing lease or a true lease. There is no room for finding the instrument to be a hybrid of the two, as this unnecessarily confuses the issue.

48 As acknowledged by Suche J. in ***Winnipeg Motor*** at para 31, " ... the true nature of arrangements involving the supply of equipment can be very difficult to peg." There can be a fine line between what is considered a true lease and a financing lease.

49 The determination of whether an arrangement is a true lease for purposes of *CCAA* s. 11.01(a) involves a functional analysis of the relationship between the parties based on substance as opposed to form (***Smith Brothers*** at para 26; ***Re Philip Services Corp.***, (1999) 15 CBR (4th) 107 at para 2 (Ont SCJ [Commercial List] [***Philip Services***])).

50 Professors Ronald CC Cuming and Roderick J. Wood in their *Alberta Personal Property Security Act Handbook*, 4th ed (Toronto: Carswell, 1998) at 53 [*Handbook*] emphasized the need to examine the relationship between the lessor and lessee to determine if it reflects indicia of a financing arrangement. They noted, however, that they were not referring to the traditional indicia prescribed by the common law, but rather those which would be relevant to someone examining the economic realities of the transaction.

51 In ***Smith Brothers*** at para 67, Bauman J. referred to the following non-exhaustive list of considerations mentioned by Master Powers sitting as a Registrar in Bankruptcy in ***Re Bronson*** (1995), 34 CBR (3d) 255 [***Bronson***], aff'd (1996), 39 CBR (3d) 33 (BCSC). This list includes factors considered by American courts in determining whether a document is a true lease or a security agreement, as summarized in *Teaching Material for Personal Property Security Transactions Governed by Personal Property Security Acts* by Professor Cuming in September 1991:

1. Whether there was an option to purchase for a nominal sum;
2. Whether there was a provision in the lease granting the lessee an equity or property interest in the equipment;
3. Whether the nature of the lessor's business was to act as a financing agency;
4. Whether the lessee paid a sales tax incident to acquisition of the equipment;

5. Whether the lessee paid all other taxes incident to ownership of the equipment;
6. Whether the lessee was responsible for comprehensive insurance on the equipment;
7. Whether the lessee was required to pay any and all licence fees for operation of the equipment and to maintain the equipment at his expense;
8. Whether the agreement placed the entire risk of loss upon the lessee;
9. Whether the agreement included a clause permitting the lessor to accelerate the payment of rent upon default of the lessee and granted remedies similar to those of a mortgagee;
10. Whether the equipment subject to the agreement was selected by the lessee and purchased by the lessor for this specific lease;
11. Whether the lessee was required to pay a substantial security deposit in order to obtain the equipment;
12. Whether the agreement required the lessee to join the lessor or permit the lessor by himself to execute a UCC financing statement;
13. Whether there was a default provision in the lease inordinately favourable to the lessor;
14. Whether there was a provision in the lease for liquidated damages;
15. Whether there was a provision disclaiming warranties of fitness and/or merchantability on the part of the lessor;
16. Whether the aggregate rental approximated the value of purchase price of the equipment. [See also ***PSINET*** at para 12.]

52 Other courts have added that the right of the lessee to an "option to purchase" can be established through the course of conduct between the parties, if not expressly provided for in the document itself (***Philip Services*** at paras 4-5). As well, leases that are "bundled together" for financing purposes may be construed as financing transactions and not as true leases, because the transactions really involve payment for financing the acquisition of the assets rather than payment for use (***Philip Services*** at para 9).

53 Neither Professor Cuming nor the court in ***Smith Brothers*** said that a lease must contain all of the foregoing indicia to be classified as a financing lease. Indeed, the main factor on which Bauman J. relied in deciding that the arrangement before him was a financing lease was the default clause.

54 A court may use some or all of the ***Smith Brothers*** factors when assessing whether a particular transaction is a true lease or a financing arrangement. It is the substance of the transaction that is determinative.

55 Michael E Burke, in his article "Ontario *Personal Property Security Act* Reform: Significant Policy Changes" (2009) 48 Can Bus LJ 289 at 291-97, undertook an empirical review of the authorities and discussed the relative weight courts have placed on these factors. He stated at 291-92:

> First, from the universe of factors or indicia that have been mentioned in the jurisprudence, some factors or indicia (referred to in this paper as "primary factors") are clearly more important than other factors or indicia (referred to in this paper as "secondary factors"). Second, the presence of a primary factor in a lease will often be determinative of the characterization of the agreement. Third, secondary factors generally have a corroborative value and are not in and of themselves determinative of the characterization. Accordingly, the presence of a number of secondary factors that are indicative of a characterization that is contrary to the characterization indicated by the primary factor will not be sufficient to overturn the weighting given by a court to the primary factor. Fourth, in those situations where the primary factor is ambiguous or absent, then the relative weighting given by a court to the secondary factors will be relevant in determining the characterization of the lease in question.

56 Topolniski J. in ***Re 843504 Alberta Ltd.***, 2011 ABQB 448 at para 63, 80 CBR (5th) 177 [***843504***] identified what Burke at 292-94 referred to as "primary factors: "

(a) Relevance of the purchase option price - whether the purchase option price is nominal or reflective of fair market value.

(b) Mandatory purchase options - whether there is a mandatory purchase option that obligates the lessee to purchase the equipment at the end of the term.

(c) Open-end leases/guaranteed residual clauses - whether the lessee is liable for any deficiency in the sale of the equipment at the end of the term.

(d) Sale-leaseback transactions - whether the transaction is structured as a sale and leaseback.

57 Topolniski J. then identified (at para 65) what Burke (at 295-98) referred to as "secondary factors":

(a) The ability to replace/exchange leased equipment is indicative of a true lease.

(b) The lessor's ability to accelerate payments and the residual value are generally inconsistent with a true lease. However, it is equally consistent with a true lease if the acceleration clause limits the lessor's damages to the present value of the remaining rents, plus the present value of the residual value at the end of the term, minus the value of net proceeds from a sale of the assets. If the acceleration clause is more narrowly crafted, it favours a security lease.

(c) A full payment lease may be indicative of either form of lease, depending on the language of the provision.

(d) A security deposit is indicative of a security lease.

(e) A substantial down payment is indicative of a security lease.

(f) Covenants relating to maintenance, insurance and risk of loss can be indicators of either type of lease. They are weak evidence of a security lease.

(g) Whether the lessor uses different forms for different types of transactions may be some evidence of intention.

58 Burke also identified (at 297) some factors, such as the exclusion of warranties on the lessor's part, as "red herrings" because their presence (or lack of presence) in a lease is equivocal: see also Weisz, Rogers & McLean at 48-49.

59 On an application for leave to appeal this Court's assessment that a particular agreement at issue in these proceedings was a financing lease, the Alberta Court of Appeal in ***De Lage Landen Financial Services Canada Inc. v. Royal Bank of Canada***, 2010 ABCA 394 at para 60 [***De Lage Landen (CA)***], refusing leave to appeal 2010 ABQB 637, 37 Alta LR (5th) 82 [***De Lage Landen (QB)***] expressly rejected the suggestion that there should be a hierarchy of factors that a court should use to determine if a lease is a true lease or a financing lease. In denying the leave application, Ritter J.A. stated at para 15:

> The applicant points to a British Columbia decision which suggests in *obiter* that there should be a hierarchy of factors used to determine if a lease is a true lease or a financing lease. In my view, this *obiter* runs contrary to current trends about how to weigh the factors in a legal test and about the deference afforded to courts of first instance in this respect. <u>If one factor trumps the others, there is simply no point in including the others in the test</u>. [Emphasis added].

60 During the present hearing before this Court, counsel spent a significant amount of time attempting to rationalize ***843504*** and ***De Lage Landen (CA)***. In this Court's view, there is no conflict between the two. Topolniski J. in ***843504*** cited the Court of Appeal's decision in ***De Lage Landen (CA)*** and quoted (at para 60) this Court's observation in ***De Lage Landen (QB)*** at para 32 that:

> ... no one factor "is the *sine qua non* for determining whether a document is a true lease or a financing lease. One must look at the whole document to get a flavour of the [parties'] intentions ..."

While Topolniski J. referred to Burke's discussion of how courts weigh certain factors and outlined the results in her case of applying his "primary" and "secondary" factors, she did not necessarily endorse the view that there is a "hierarchy" of factors in every case.

61 Topolniski J. considered (at para 64) a provision in the lease before her which provided that:

* the lessee could return the vehicle at the end of the six-month minimum lease term;
* once the lessee returned the vehicle, the lessor would sell the vehicle;
* the lessee would keep the surplus if the sale proceeds exceeded the termination book value; and
* if the sale proceeds did not exceed the termination book value, the lessee would be liable for the shortfall.

She found this provision was indicative of a security lease since it rendered the lessee liable for a deficiency on the vehicle's sale at the end of the term.

62 Topolniski J. also applied Burke's "secondary" factors to the lease that was before her. There would have been no point in her doing so had she accepted that the lessee's liability for the deficiency trumped any and all secondary factors. She concluded that the secondary factors were not determinative of the proper characterization of the lease (at para 67). The presence of some secondary factors was insufficient to outweigh the clear effect of the primary factors in her case.

63 GE suggests that Topolniski J. acknowledged that the presence of a primary factor often can be determinative of the characterization, while absence or ambiguity in respect of the primary factors can make weighing of the secondary factors more relevant. In fact, Topolniski J. did not make such a statement. She simply quoted the Burke article where Burke made that argument.

64 GE argues that while the presence of one of Burke's "primary" factors is significant, absence or ambiguity in respect of a primary factor is not determinative. It simply means that other factors will be more important in the analysis. For example, GE submits that the presence of an option to purchase at nominal value is a primary factor, and while its presence likely will result in the agreement being characterized as a financing lease, the absence of such an option or, indeed, the presence of an option to purchase at fair market value, means that focus must be directed to the other factors. GE suggests that this approach is consistent with authorities which hold that agreements without an option to purchase may still be classified as financing leases when the other indicia of financing leases are present.

65 The proper approach is more holistic than the one advocated by GE. While the presence or absence of one or more factors may loom larger than others, in all instances the inquiry remains focussed on determining the intention of the parties and is based on an interpretation of the entire agreement. As stated by the Alberta Court of Appeal in ***De Lage Landen (CA)***, one factor cannot trump others in terms of the legal test. Courts must review the entire agreement and they must consider all factors. That is not to say, however, that certain factors may not have greater probative value than others in terms of the particular agreement before the court. In such a case, the court might give those factors greater weight. In all cases, the court must examine the various ***Smith Brothers*** factors and any other factors it considers material and relevant, balance those factors in the context of the entire agreement, and make a determination as to whether the agreement before it as a financing lease or a true lease. This is not a scientific exercise.

66 Counsel for several of the Applicants argue that payments that Cow Harbour made under leases containing an option to purchase were payments for "use," as the "purchase price" was not due and payable until Cow Harbour exercised the option to purchase or the lease came to an end and the lessee chose to pay the purchase price at a nominal sum. They cite ***Ed Miller Sales & Rentals Ltd. v. Alberta*** (1982), 42 AR 350 (QB) [***Ed Miller***] in support of this position. Purvis J, in that case, relied in turn on ***Ramsay v. Pioneer Machinery Co.*** (1981), 28 AR 429 (CA) [***Ramsay***].

67 The issues in ***Ramsay*** were whether a transaction fell within the *Conditional Sales Act*, RSA 1970, c 61 and, if it did, whether the conditional seller could recover the purchase price through the sale of the equipment or by suing the conditional buyer. This was called the "seize or sue" provision. The Alberta Court of Appeal stated at para 20:

> ... Until the option is exercised the lessor is not pursuing his "right to recover the purchase price". If he chooses to recover the chattel he is exercising his right of possession on default, which is a right independent of any money claim. I have no hesitation in saying that [the seize or sue provision] is not applicable unless the lessor is seeking to recover the purchase money and he cannot seek to recover the purchase money until the option is exercised. It may be that a "lessor" who is found to be, in substance, a "conditional sales vendor" should be treated as a vendor claiming his purchase price within the section, but that is not this case.

68 In ***Ed Miller***, the court considered whether lessors holding leases with options to purchase could maintain a priority claim to a builders' lien fund. The court applied the analysis in ***Ramsay*** in finding that until the lessees exercised the options to purchase, the lessors were not "sellers" under the *Conditional Sales Act* and, " ... [t]hey are not attempting to recover a purchase price, but are attempting to establish priority against a lien fund for rental for equipment" (at para 49). As a result, the court held that the lessors' claims were not for payment of purchase moneys but for rental and, as a result, they were entitled to advance a claim for a lien for a reasonable and just rental of the equipment while used on the contract site (at para 50).

69 The now repealed *Conditional Sales Act* contained specific provisions concerning registration and remedies available to conditional sellers. The courts, when considering that statute, were more interested in the structure of the transaction than the parties' intention. In fact, the court in ***Ed Miller*** commented, "Stevenson J.A. [in ***Ramsay***] found that it was sufficient to bring the transaction within the relevant sections of the *Conditional Sales Act* if it was established that the lessee merely had it within his power to acquire ownership. It was not necessary to establish intention" (at para 43).

70 When a court undertakes the true lease/financing lease analysis under the *CCAA*, substance, including the parties' intention, is one of the paramount considerations. The form the transaction takes is not. The "all or nothing" argument advanced by certain of the Applicants could just as easily result in all lessors of true and financing leases being precluded from receiving anything during the stay of proceedings.

71 Accordingly, it is of the utmost importance that this Court examine each lease individually to determine whether it falls within the category of a true lease or a financing lease.

72 Finally, it is a fundamental principle of contractual interpretation that a court must interpret an agreement as at the date it was made, as the exercise is intended to discern the intention of the parties at the time the contract was formed (***McDonald Crawford v. Morrow***, 2004 ABCA 150 at para 72, 348 AR 118).

V. Specific Leases

A. Scott Capital Group Inc. (Scott Capital) Leases

1. The leases

73 Five of the Disputed Leases are between Cow Harbour and Scott Capital. The lease details are as follows:

Lease number	Date day/month/year	Term (months)	Capital Cost of Items	Monthly Rental	Option Price	Security Deposit
6049520 Schedule 001	1/10/2009	60	$559,951	$10,469	25% of original capital cost	$55,995 = 10% of original capital cost
6049520 Schedule 002	30/10/2009	48	$801,250	$18,184	20% of original capital cost	$160,250 = 20% of original capital cost
6049520 Schedule 003	18/12/2009	48	$234,000	$5,295	Fair market value	$46,800 = 20% of original capital cost
6049520 Schedule 004	4/2/2010	48	$664,832	$16,717	Fair market value	$132,966 = 20% of original capital cost
6049520 Schedule 005	5/2/2010	48	$286,020	$7,190	Fair market value	$57,204 = 20% of original capital cost

74 All of the Scott Capital leases are subject to the terms of the Scott Capital Master Equipment Lease that the parties entered into on October 1, 2009 (Scott Master Lease). Scott Capital's affiant deposed that the Scott Master Lease had been in effect for 30 years, with the last revision having been made about ten years ago. He confirmed that Scott Capital used the same form for what Scott Capital intended to be true leases and financing leases. The number 6049520 refers to the Scott Master Lease to which all of the Scott Capital leases being considered are subject. This Court will refer to each lease by its Schedule number.

75 Scott Capital leased eight pieces of heavy equipment or vehicles to Cow Harbour under these five leases. It entered into all of these leases with Cow Harbour within six months prior to Cow Harbour's *CCAA* filing. In the case of the Schedule 001 lease, the equipment was only commissioned for use by Cow Harbour in July 2010, which was well into the *CCAA* proceedings.

76 The evidence of Scott Capital's affiant was that Cow Harbour sourced the equipment, negotiated the sale price and approached a broker to seek assistance with acquisition of the assets. The broker then contacted Scott Capital and the equipment went straight from the third party vendor to Cow Harbour.

77 Scott Capital's affiant deposed that Scott Capital generally structured its leases as true leases. His due diligence on Cow Harbour suggested that Cow Harbour might be in a precarious financial position. As a result, Scott Capital had no intention of providing "financing leases" to Cow Harbour. He deposed that Scott Capital made it clear to Cow Harbour, and Cow Harbour accepted and acknowledged at the time they negotiated the leases, that the lease options to purchase were to be at fair market value.

78 All of the leases identify the option price as being fair market value. In three of the leases, that value is not specified. In the other two, the fair market value of the equipment is pre-estimated and agreed by the parties to be a particular percentage of the original capital cost of the equipment (25 percent in the Schedule 001 lease and 20 percent in the Schedule 002 lease).

79 The security deposits that Scott Capital required Cow Harbour to pay under the leases amounted to 10 percent of the capital cost of the equipment in the case of the Schedule 001 lease and 20 percent of the capital cost of the equipment in the other four leases.

2. <u>Lease-specific arguments of the parties</u>

(a) Scott Capital

80 Scott Capital asserts that it did not structure its leases in such a way that Cow Harbour was financing its purchase of the equipment or accruing equity in the equipment over the lease term. Rather, Scott Capital structured the leases to ensure that the use, condition and value of the equipment were being controlled and maintained, as Scott Capital expected that Cow Harbour would return the equipment to it at the end of the lease terms. As the affiant stated on cross-examination:

> A. You will see that the terms on these leases are different. And part of that is because we feel that certain equipment may be perhaps more abused. Certain equipment naturally has a different life than other equipment.
>
> But that type of an analysis is factored into whether or not we will enter into a 48-month lease or perhaps a 60-month lease. If we think that equipment will be used gingerly, then we will perhaps enter into a longer-term lease. If we think that equipment will be used harshly in harsh conditions, we want to put it on a shorter-term lease. There always has to be value on that equipment in the event that it's returned.

[Transcript of the cross-examination of Brian Jagt, 26 October 2010, p. 20, ll 21-34.]

81 The Schedule 003, Schedule 004 and Schedule 005 leases, in addition to other detailed terms concerning the maintenance and condition of the equipment, specified usage maximums in the return provisions of the lease. Scott Capital did this with specific care and concern for the equipment's condition, having regard to how Cow Harbour intended to use the equipment. The affiant explained that Scott Capital was concerned about the number of hours that Cow Harbour intended to use the equipment, rather than the number of kilometres of recorded use, as Scott Capital anticipated that the buses and trucks would be running constantly but not travelling great distances.

82 The purchase option prices set out in the Schedule 001 and the Schedule 002 leases (25 and 20 percent, respectively, of the original capital cost of the equipment) were not arbitrary figures. Rather, Scott Capital determined those prices and Cow Harbour agreed to those prices as a reasonable pre-estimate of the equipment's fair market value at the end of the lease term, based on Cow Harbour's anticipated use and the nature of the use.

83 Scott Capital points out that the present value of the rentals under each lease was less than 90 percent of the original equipment cost.

(b) Monitor

84 The Monitor suggests that the Schedule 001 and Schedule 002 leases are best characterized as financing leases because, among other factors, the end of term purchase option price appears to be arbitrary and bears no direct connection to the actual value of the leased equipment at the time Cow Harbour was to exercise the option. In other words, Cow Harbour appears to have acquired equity in the leased equipment because the fair market value of the leased equipment at the time Cow Harbour was to exercise the option may exceed the purchase option price.

85 In addition, the Schedule 001 and Schedule 002 leases overwhelmingly exhibit other indicia of a financing lease, as discussed in ***Smith Brothers***, which militates against them being considered true leases. Specifically, the leases contain the ***Smith Brothers*** financing lease factors 3 to 10 and 13 to 16.

86 The Monitor points out that the aggregate rental under the Schedule 001 and Schedule 002 leases approximated the value of the purchase price of the equipment, factoring in interest and carrying costs (***Smith Brothers*** factor 16), as the equipment in the Schedule 001 lease originally was valued at $559,951 plus applicable tax, while the total amount to be paid by Cow Harbour during the course of the term was $628,140 plus applicable tax. In the Schedule 002 lease, the equipment originally was valued at $801,249.96 plus applicable tax, while the total amount to be paid by Cow Harbour over the course of the term was $1,033,079.83 plus applicable tax.

87 In the Schedule 003, Schedule 004 and Schedule 005 leases, the end of term purchase option was referred to as "fair market value" (with no approximated value of what that value might be). While this factor militates in favour of each such lease being characterized as a true lease, the Monitor notes that, as in ***Bronson***, these leases contained default provisions which guaranteed to Scott Capital the residual value of the equipment. These three leases contained financing lease ***Smith Brothers*** factors 3 to 10 and 13 to 15.

(c) GE

88 GE takes the position that the Scott Master Lease bears the indicia of a financing lease as ***Smith Brothers*** factors 4 to 11 and 13 to 15 are present.

89 It says the present value of the rental payments is irrelevant. The more important factor is that the aggregate cost of the rental payments exceeded the value of the equipment at the commencement of the lease.

90 GE points to the evidence of Scott Capital's affiant that the amount of the security deposit that Cow Harbour paid at the outset of the Schedule 002 lease was equal to the amount of the purchase option at the conclusion of the term. It contends this was equivalent to a nominal purchase option price and suggestive of a financing lease as Cow Harbour, at the outset of the lease, paid the amount of the purchase price due at the conclusion of the lease.

91 GE maintains that, if this Court accepts Scott Capital's assertion that the purchase price options in the Schedule 003, Schedule 004 and Schedule 005 leases were for fair market value, it would be accepting form over substance. Scott Capital's affiant confirmed that the amount of the security deposit that Cow Harbour paid in respect of each of these three leases at the outset of the leases was equal to Scott Capital's internal estimate of the remaining value of the equipment at the conclusion of the leases. Said differently, Cow Harbour, at the outset of the lease, paid what was estimated to be the equipment's remaining value at the conclusion of the lease, leaving Cow Harbour with a nominal purchase option.

3. <u>Decision</u>

92 Applying the ***Smith Brothers*** criteria to the five Scott Capital leases reveals the following:

1. Whether there was an option to purchase for a nominal sum - No, the purchase price was reflective of fair market value (see discussion below).
2. Whether there was a provision in the lease granting the lessee an equity or property interest in the equipment - No.
3. Whether the nature of the lessor's business was to act as a financing agency - The affiant acknowledged financing leases are a small portion of its business.
4. Whether the lessee paid sales tax incidental to acquisition of the equipment - Yes.
5. Whether the lessee paid all other taxes incidental to ownership of the equipment -Yes.

6. Whether the lessee was responsible for comprehensive insurance on the equipment - Yes.
7. Whether the lessee was required to pay any licence fees for operation of the equipment at its expense - Yes.
8. Whether the agreement placed the entire risk of loss on the lessee - Yes.
9. Whether the agreement included a clause permitting the lessor to accelerate payment of rent on default by the lessee and granted remedies similar to those of a mortgage - Yes.
10. Whether the equipment subject to the agreement was selected by the lessee and purchased by the lessor for this specific lease - Yes.
11. Whether the lessee was required to pay a substantial security deposit in order to obtain the equipment - Yes.
12. Whether the agreement required the lessee to join the lessor or permit the lessor by himself to execute a UCC financing statement - Not applicable.
13. Whether there was a default provision in the lease inordinately favourable to lessor - Yes.
14. Whether there was a provision in the lease for liquidated damages - Yes.
15. Whether there was a provision disclaiming warranties of fitness and/or merchantability on the part of the lessor - Yes.
16. Whether the aggregate rentals approximated the value of the purchase price of the equipment - Yes.

93 What do these results establish?

94 Scott Capital's affiant conceded that Cow Harbour sourced the equipment and then approached a broker to seek assistance with acquisition of the assets. The broker would then contact Scott Capital. The way in which the leases came about is more reflective of a financing lease transaction than a true lease situation. However, it is important for this Court to examine the structure of each transaction to characterize properly the agreement.

95 All of the leases had purchase options. This Court must attempt to value the purchase price option as at the date Cow Harbour and Scott Capital executed the lease agreements. As stated in the *Handbook* at 55:

> A clause in a lease giving the option to purchase the goods at less than their expected market value (<u>as determined at the date of execution</u>) indicates that the lessee has acquired an equity in the goods not unlike that which he would have acquired under an instalment purchase contract. [Emphasis added.]

96 In ***Re Ontario Equipment (1979) Ltd.*** (1981), 33 OR (2d) 648 at para 9 (HCJ), aff'd (1982), 35 OR (2d) 194 (CA), Henry J.considered the nature of the option to purchase to be a critical factor in distinguishing between true leases and financing leases in personal property security legislation cases, stating:

> The test in determining whether an agreement is a true lease or a conditional sale is whether the option to purchase at the end of the lease term is for a substantial sum or a nominal amount ... If the purchase price bears a resemblance to the fair market price of the property, then the rental payments were in fact designated to be in compensation for the use of the property and the option is recognized as a real one. On the other hand, where the price of the option to purchase is substantially less than the fair market value of the leased equipment, the lease will be construed as a mere cover for an agreement of conditional sale.

97 Whether a purchase option price is nominal is fact-specific. A purchase option for a nominal sum is indicative of a financing lease. On the other hand, a purchase option at fair market value is highly suggestive of a true lease. The rationale, according to Burke, is that, "[i]f the lessee is required to pay the actual value of the property at the end of the lease at a time when the property still has value, then the lease payments cannot reasonably be said to have been payments towards an equity interest in the property" (at 293).

98 However, as noted by the Master in ***Bronson*** at para 55 and confirmed by the British Columbia Supreme Court in that case (at para 7), the mere existence of a fair market value purchase option price in the agreement is not necessarily determinative of whether the agreement is a true lease or a financing transaction.

99 In ***Smith Brothers***, Bauman J. commented that simply because the lessee can purchase the equipment at its fair market value at the end of the lease does not prevent a court from characterizing the transaction as a financing transaction if the end of the lease term is roughly equivalent to the end of the equipment's useful life (at para 76).

100 Professors Cuming and Wood explained in their *Handbook* at 55 that:

> A clause in a lease giving the lessee the option to purchase the goods at less than their expected market value (as determined at the date of execution) indicates that the lessee has acquired an equity in the goods not unlike that which he would have acquired under an instalment purchase contract. The economic reality is that it is quite predictable the lessee will pay this amount to the lessor. Consequently, the transaction is likely to be characterized as a security agreement. However, the fact that at the end of a lease term roughly equivalent to the useful life of the goods the lessee can purchase the goods at their then market value does not prevent characterization of the transaction as a security agreement. If one or more of the major indicia of a security agreement are present, the transaction may be a security agreement. Accordingly, if the lease is for all or the greater part of the useful life of the leased equipment and the lessee is obligated to pay rental equivalent to the capital cost of the goods and an appropriate credit charge, the fact that the lessee is given the right to buy the goods at the end of the term for their then small market price should play no role in the characterization process. A consideration of the option price is relevant to the characterization of the transaction only if the option can be exercised at a time when the goods have significant commercial value. It may be possible to show that the option price was not designed to ensure that the lessor is fairly compensated for his interest in the goods, but was included for some other purpose (such as satisfying income tax authorities). This provides strong evidence that the parties recognize that by the time the option is exercised the lessor has been fully compensated through rental payments and that it matters little to either the lessor or the lessee that the option is or is not exercised.

101 In the Schedule 001 and Schedule 002 leases, the purchase option price was expressed to be the "fair market value" of the equipment, pre-estimated and agreed by the parties to be 25 percent and 20 percent, respectively, of its original capital cost. These percentages equated to purchase prices of $139,987.75 (Schedule 001 lease) and $160,249.99 (Schedule 002 lease). These are not nominal amounts.

102 Scott Capital's affiant deposed that Scott Capital used a "combination of past experience, extensive equipment knowledge, market knowledge and the application or intended use of the equipment to determine the value of any purchase option at lease end such that it is a reasonable estimate of fair market value."

103 The Schedule 003, Schedule 004 and Schedule 005 leases all stated that the purchase option price was "fair market value." There is no evidence to suggest that the parties meant or intended otherwise.

104 This Court finds that the options were for fair market value or a reasonable pre-estimate of such.

105 There was no evidence that 60 months in the case of the Schedule 001 lease or 48 months in the case of the Schedule 002, Schedule 003, Schedule 004 and Schedule 005 leases was roughly equivalent to the end of the useful life of the equipment involved in those leases. In fact, Scott Capital's affiant stated that Scott Capital structured the leases to ensure there was value in the equipment at the end of the lease term.

106 These leases did not contain any mechanism, either in a default situation or at full term, whereby the surplus value of the equipment would go to Cow Harbour. If, at the end of the term of each lease, Cow Harbour did not exercise the purchase option to acquire the equipment, Cow Harbour had to return the equipment to Scott Capital. Scott Capital could then deal with the equipment as it saw fit for its own benefit and account. Cow Harbour was not responsible under any of these leases for any deficiency or shortfall on the sale of the equipment at the end of the term.

107 The Scott Master Lease s 13(f) contained a default clause allowing for liquidated damages to consist of the present value of rents owing to the end of the term, plus the present value of the residual value of the equipment "which Lessor expected to receive at the expiry of the term of the lease, which is equal to the Fair Market Value of the Equipment as set out in the Equipment Schedule ...," minus the net proceeds from a sale or lease of the equipment. The lease schedules stated that if Cow Harbour defaulted in its obligations under the lease, Scott Capital would retain the security deposit as liquidated damages.

108 The default provisions in ***DaimlerChrysler Services Canada Inc. v. Cameron***, 2007 BCCA 144 [***DaimlerChrysler***], rev'g 2006 BCSC 1992, 32 CBR (5th) 188 were similar (other than retention of the security deposit). The court found that the lease secured the payment of the residual value by the lessee in the contingency of default (at para 28). The court went on at para 37 to say:

> ... the basis for calculating damages does not distinguish a true lease from a security lease. The ability to claim accelerated damages in *Langille* was not a consequence of the character of the lease, i.e., a true lease or a security lease. Rather, it was simply the proper measure of damages for breach of a chattel lease. Generally, the basis for calculating damages can provide only some insight as to whether an impugned lease secures payment or performance of an obligation. I emphasize that it cannot serve as a decisive factor.

109 The Chambers Judge had concluded in ***DaimlerChrysler*** that the transaction was a security lease, following ***Bronson***, which found that the default clause secured payment of both the lease payments and the option price. On appeal, the court determined that the chambers judge had placed undue weight on the default provision as it can have only corroborative effect (at para 46).

110 According to Burke at 294:

> If, however, the lessee's residual value guarantee only applies in the case of an early termination of the lease, whether voluntarily by the lessee or by the lessor as a result of the occurrence of a default, but not at the end of the scheduled lease term, then such a residual value guarantee will not constitute a primary factor that is indicative of a security lease.

111 In the case before this Court, the default provisions contained in the Scott Capital leases are equivocal.

112 The aggregate of rental payments for each of these leases is greater than the original capital cost of the equipment. Professors Cuming and Wood expressed their view in the *Handbook* that if the lessee must pay the equivalent of the lessor's capital investment plus a credit charge at the rate existing at the date of the agreement, there is strong but not conclusive evidence of a secured sale (at 54). However, Burke commented at 296:

> If a lessee is required to pay what is the equivalent of the original cost of the leased property (i.e., the lessor's capital investment), plus a finance charge based on the rate existing at the date of the lease agreement, it does not necessarily follow that such an agreement is a security lease, especially if the lease contains a true fair market value purchase option.
>
> In such a lease, it is possible that the lessee has simply agreed to pay a premium for the use of the leased property.

113 The Schedule 003, Schedule 004 and Schedule 005 leases contain specific use limitations with corresponding excess use charges. In ***DaimlerChrysler***, the Chambers Judge found that excess kilometre charges and maintenance obligations were indicative of a true lease as they protected the lessor against reduction of market value on expiry of the lease term due to excess "wear and tear" (at para 25). Burke, however, considered such provisions equally consistent with a financing lease, as they suggest that the lessee bears some risks of ownership (at 296). This Court finds that those provisions are equivocal in the case of the Scott Capital leases.

114 All five Scott Capital leases required substantial security deposits. The evidence of Scott Capital's affiant on cross-examination was that for four of the five Scott Capital leases, the amount of the security deposit was equivalent to the purchase option price in the lease or the anticipated purchase option price (transcript of the cross-examination of Brian Jagt, 26 October 2010, pp 43-45). He explained that in terms of the Schedule 003, Schedule 004 and Schedule 005 leases (which have purchase options simply stated to be at "fair market value"), the security deposit was based on the "estimated" fair market value of the equipment, but that this was just Scott Capital's internal estimate (transcript of the cross-examination of Brian Jagt, 26 October 2010, pp 39-42). Scott Capital did not provide this information to Cow Harbour. Cow Harbour had the ability to purchase the equipment at the end of the term of the lease for the "fair market value," irrespective of whether that amount turned out to be less than, equal to, or greater than the amount of the security deposit.

115 During cross-examination, the Scott Capital affiant gave the following evidence:

Q. And would I be correct in stating as well that typically if a purchaser or if a lessee does exercise an option to purchase the equipment at the end of the lease, the deposit will be utilized in some fashion to acquire the equipment?

R. It depends on the customer. Some customers want us to reimburse in the form of a cheque their security deposit, and then they pay us a separate cheque for the full amount if they purchase it. And other customers just tell us to net it against their purchase option, making sure that the bill of sale records the correct gross purchase price and then with the reflection that the other amount has been applied.

S. And was there any discussion with Cow Harbour at any point in time with respect to how the deposit, whether the deposit would be utilized for the purchase price of the asset if Cow Harbour did exercise an option to purchase?

T. There was no discussion with Cow Harbour.

[Transcripts of the cross-examination of Brian Jagt, 26 October 2010, p 25, ll 8-26.]

116 This Court finds that Scott Capital's estimated fair market value at the end of the lease term was a reasonable "security deposit" amount to protect against its risk that Cow Harbour might not return the equipment to it when the lease ended because of some total loss event or that Cow Harbour would return the equipment to Scott Capital in such poor condition that the equipment no longer had value. In such cases, the security deposit would have served its stated purpose of being a recourse for Scott Capital's damages under the lease.

117 There are certainly indicia of a financing arrangement. There are hypothetical situations under which Cow Harbour could indeed have built up equity and paid only the residual amount of the equipment's capital cost plus a financing charge; *e.g.* if it defaulted in its obligations under the leases. Those hypothetical situations did not occur, however, and based on the wording of the leases, Cow Harbour was paying for use of the equipment.

118 Although the security deposits are relatively substantial, there was no obligation on Cow Harbour's part to forfeit the security deposits at the end of the lease term. It could simply return the equipment and demand the security deposits (less any additional charges that it had incurred in the meantime). This is especially so with respect to the Schedule 001 lease, where the purchase option price was 25 percent of the equipment's original capital cost, while the security deposit was ten percent. Although Burke suggested (at 296) that a substantial security deposit is indicative of a financing lease in that the lessee is required to post collateral to obtain the equipment, considering the whole of the Scott Capital lease agreements, this factor is not determinative and, in fact, it assists Scott Capital in its position.

119 For the foregoing reasons, this Court concludes that the Scott Capital leases are true leases.

B. Caterpillar Financial Services Limited (CFSL) Lease

1. The Lease

120 Cow Harbour leased a Caterpillar off-highway truck from CFSL pursuant to a lease dated March 27, 2006. According to CFSL's affiant, the original cost of the truck was $2,235,456. The amount shown in the floating rate addendum was $500 more, which CFSL's affiant explained was a fee payable by Cow Harbour (transcript of the cross examination of Renee Bertha Fournier, 21 October 2011, p. 7, ll 32-41). The lease term was 60 months. The lease required Cow Harbour to pay irregular monthly payments pursuant to the terms of the irregular payment schedule attached to the CFSL lease (6 months at $100,000 and 54 months at $28,397.86). The aggregate amount of those rents was about $2,133,485.

121 If Cow Harbour exceeded the maximum hours of use of the equipment, it was to pay an excess hour charge.

122 The CFSL lease contained an end of term purchase option price of $524,535.

2. Lease-specific arguments of the parties

(a) CFSL

123 CFSL argues that the most probative factor is that the purchase option price was neither a nominal sum nor arbitrarily selected. Rather, it calculated the purchase option price after considering factors such as depreciation, historic resale market for like equipment, application, exchange rate and annual hours of usage. The purchase option price represented 102 percent of the standard residual amount, which CFSL calculated to be $514,250, and was more than 15 percent of the value of the truck at the commencement of the term.

124 According to CFSL, the purchase option price was an amount intended to represent a reasonable pre-estimate of the fair market value of the truck at the end of the lease term. It relies on the statement by Burke (at 293) that, "[i]f the lessee is required to pay the actual value of the property at the end of the lease at a time when the property still has value, then the lease payments cannot reasonably be said to have been payments towards an equity interest in the property." CFSL says that the term of the lease did not exceed 75 percent of the economic useful life of the truck, which it estimated to be 120 months.

125 The net present value of the rental payments is $1,865,621.73, which is less than 90 percent of the equipment's value at the beginning of the term. CFSL points out that the rental payments could not be applied in satisfaction of the purchase option price.

126 CFSL maintains that other factors point to this being a true lease, including:

* the lack of any requirement for a security deposit or down payment
* Cow Harbour was not required to pay the equivalent of the original cost of the truck, plus a financing charge based on a rate existing at the date of the CFSL lease
* Cow Harbour was required to maintain certain minimum standards of repair with respect to the truck.

CFSL submits that the latter factor is consistent with it attempting to protect its interest in the residual value of the truck on its return at the end of the lease.

127 Cow Harbour was not required to make a residual payment at the end of the lease term or to guarantee residual value. Cow Harbour could exercise the option or return the truck to CFSL.

128 CFSL asserts that the presence of other factors, such as the inability of Cow Harbour to exchange or replace the truck; a default provision favourable to CFSL; and the inclusion of the floating rate addendum, should be given less weight in comparison with the fair market value option to purchase. Equipment lessors are in the business of making money and the floating rate addendum simply reflects its cost of capital or a return of investment.

129 CFSL relies on ***DaimlerChrysler*** in arguing that the acceleration of rent on default is equivocal.

130 CFSL submits that given Cow Harbour's operations, the specialized equipment it was leasing and the relatively remote location of the oil sands site where it was working, it was only logical that CFSL would impose the obligation for insurance, maintenance and the risk of loss on Cow Harbour. Accordingly, these are neutral factors.

(b) Monitor

131 The Monitor contends that the CFSL lease is best characterized as a financing lease because, among other factors, the end of term purchase option price (approximately 23 percent of the original value of the equipment) appears to be arbitrary and bears no direct connection to the actual value of the leased equipment at the time Cow Harbour exercises the option. In other words, Cow Harbour appears to have acquired equity in the leased equipment because the fair market value of the leased equipment at the time when the option could be exercised might exceed the purchase option price. This leads to the conclusion that the lease is a financing agreement and/or a lease pursuant to which payments are made for "use and equity."

132 The Monitor suggests that the CFSL lease exhibits other indicia of a financing lease, as discussed in ***Smith Brothers***, which militates against it being considered a true lease. Specifically, ***Smith Brothers*** factors 4 to 6, 8, 9 and 13 to 16 are present in the CFSL lease. The Monitor notes that the equipment originally was valued at $2,235,956 plus applicable tax, while the total amount that Cow Harbour was to pay during the course of the term was $2,658,019.44 plus applicable tax. Therefore, the aggregate rentals approximated the value of the purchase price of the equipment factoring in interest and carrying costs.

(c) GE

133 GE focuses on the floating rate addendum, which provided that the rental payments were subject to an interest rate adjustment. It says this resulted in the lease operating like a credit or loan agreement. GE notes that:

* CFSL charged interest to Cow Harbour equivalent to its cost of acquiring the truck;
* the interest rate that CFSL charged fluctuated over the term of the lease, according to the cross-examination of CFSL's affiant (transcript of the cross-examination of Renee Bertha Fournier, 21 October 2011, p.6, ll 5-8);
* Cow Harbour had the option, at any time over the term of the lease, to lock into a fixed interest rate equal to the rate of interest charged to CFSL on fixed rate loans (transcript of the cross-examination of Renee Bertha Fournier, 21 October 2011, p.8, ll 30-41; p.9, ll 1-4);
* at the end of the lease, Cow Harbour's final rent payment was subject to a credit or debit adjustment on the interest rate fluctuation over the term of the lease.

GE suggests that this is the most significant evidence the lease was a financing arrangement.

3. <u>Decision</u>

134 The following results from applying the ***Smith Brothers*** criteria to the CFSL lease:

1. Whether there was an option to purchase for a nominal sum - No, the purchase price was reflective of fair market value.
2. Whether there was a provision in the lease granting the lessee an equity or property interest in the equipment - No.
3. Whether the nature of the lessor's business was to act as a financing agency - It acted as both a financing and a leasing company, according to its affiant.

4. Whether the lessee paid sales tax incidental to acquisition of the equipment - The lessee was to pay any taxes due on its exercise of the sale option.
5. Whether the lessee paid all other taxes incidental to ownership of the equipment - Yes.
6. Whether the lessee was responsible for comprehensive insurance on the equipment - Yes.
7. Whether the lessee was required to pay any licence fees for operation of the equipment at its expense - Not specifically in the lease agreement
8. Whether the agreement placed the entire risk of loss on the lessee - Yes.
9. Whether the agreement included a clause permitting the lessor to accelerate payment of rent on default by the lessee and granted remedies similar to those of a mortgage - Yes.
10. Whether the equipment subject to the agreement was selected by the lessee and purchased by the lessor for this specific lease - Yes.
11. Whether the lessee was required to pay a substantial security deposit in order to obtain the equipment - No.
12. Whether the agreement required the lessee to join the lessor or permit the lessor by himself to execute a UCC financing statement - Not applicable.
13. Whether there was a default provision in the lease inordinately favourable to lessor - Yes.
14. Whether there was a provision in the lease for liquidated damages - Yes
15. Whether there was a provision disclaiming warranties of fitness and/or merchantability on the part of the lessor - Yes.
16. Whether the aggregate rentals approximated the value of the purchase price of the equipment - Yes, if interest payments are added to the rent.

135 Cow Harbour selected the truck and CFSL acquired the truck to lease to Cow Harbour.

136 This Court finds that the purchase option price for the CFSL equipment was a reasonable pre-estimate of the truck's fair market value at the end of the 60-month lease term. It was approximately 23 percent of the truck's original price. Based on CFSL's estimate that the truck had an economic useful life of 120 months, it was reasonable for CFSL to believe that the truck would still have value at the end of the lease term. No evidence was led which would suggest otherwise.

137 The lease did not require Cow Harbour to pay a security deposit or down payment. While CFSL was entitled to accelerate rental payments on default, Cow Harbour was not responsible for the residual value, if any, of the truck.

138 The aggregate rent was about five percent less than the truck's original value. However, as is apparent from the floating rate amortization schedule attached to the lease, the rent payments and option purchase price together amounted to the capital cost of the truck, plus a seven percent interest rate (Toronto Dominion prime plus 1.50 percent).

139 GE argues that a "payment for use" contract will not impose an obligation on the lessee to pay interest on the funds that the lessor uses to acquire the leased equipment. However, in this Court's view, it is just as likely that such a charge will be included in a true lease, *albeit* it may be incorporated in the overall rental amount rather than being identified as interest or a financing charge.

140 Some of the terminology that CFSL used in the floating rate addendum suggests that it is an addendum to a financing lease agreement. The terminology includes "principal balance," which is defined as "equal to the amount of <u>credit extended</u> of $2,235,956.00, as adjusted by amortization during the term of the Contract" (emphasis added). Also, "gross lease" was defined as meaning "the total <u>Amount of Credit Extended and Aggregate Finance</u>

Charge(s) payable hereunder" (emphasis added). These definitions, however, are not definitive and this Court must look at the lease as a whole.

141 Cow Harbour was not obliged to exercise the purchase option. If it did, the purchase option price was a significant amount and CFSL was not guaranteed the residual value of the truck unless Cow Harbour exercised the option. This Court finds that Cow Harbour simply agreed to pay a premium for the use of the leased property.

142 In looking at the CFSL lease as a whole, this Court holds that it was a true lease.

C. Wajax Industries (Wajax) Leases

1. The Leases

143 Wajax had three leases with Cow Harbour, as set out below:

Lease number (Monitor's Report)	Date day/month/ year	Initial Term (months)	Original Cost of Equipment	Monthly Rental	Option Price	Assessed Value June 2010
196	12/11/2008	6	$439,810	$16,500	$439,810, less a % of rent payments	$130,000
198	8/4/2009	6	$1,681,500	$40,000	$1,681,500, less a % rent payments	$450,000
197	8/4/2009	6	$991,860	$30,000	$991,860, less a % of rent payments	$175,000

144 The leases were for a maximum six-month initial term, with month-to-month extensions allowed after the initial term. Cow Harbour could exercise the option to purchase at any time during the initial term of the lease, or within 6 months after that, if CFSL extended the term of the lease.

145 Cow Harbour was responsible to pay the specified monthly rental, unless it used the equipment for more than 200 hours in a month, in which case it was required to pay overtime charges.

146 The option to purchase was for the original cost of the equipment, but if Cow Harbour exercised it during the initial six-month term, 85 percent of the rental payments that Cow Harbour had made was to be credited towards the purchase price. Wajax had the sole option to extend the option to purchase for a further six-month term. If Cow Harbour exercised the option during the second six-month term, Wajax was to credit towards the purchase price 85 percent of the rental payments that Cow Harbour had made during the first six month term and 50 percent of the rental payments that Cow Harbour had made during the second six-month term.

147 Cow Harbour did not exercise the option to purchase during the initial six-month term and Wajax did not extend the option to purchase beyond that term. At the date this Court granted the Initial Order, Cow Harbour no longer had an option to purchase the equipment.

2. Lease specific arguments of the parties

(a) Wajax

148 Wajax's affiant deposed that Wajax is not in the business of providing equipment financing. He stated that, in this case, Wajax entered into short-term rental agreements with Cow Harbour to accommodate Cow Harbour's need for the equipment and to permit Cow Harbour time to find third party financing for payment of the purchase price.

149 The affiant stated that Wajax set the rental rate with a view to covering the equipment's depreciation during the rental period, as Cow Harbour could have returned the equipment after the initial six-month term without incurring any further obligation to Wajax.

150 Wajax emphasizes that the focus on this application should be on whether the lease agreements secured payment of the purchase price for the equipment. Wajax suggests that this Court should bear in mind the distinctions between leasing consumer goods to an individual versus leasing a large piece of equipment that generates revenue for a business.

151 Wajax submits that the percentage of the rental payments credit that Cow Harbour would have received had it elected to exercise the option to purchase the equipment was minimal when compared to the purchase price for the equipment. It asserts this credit was not "equity" given the equipment's depreciation, as demonstrated by the Ritchie Brothers valuations that were undertaken in these proceedings and the evidence of Wajax's affiant.

152 Wajax notes that there was no mandatory purchase option and no liability for any deficiency on the sale of the equipment following the expiry of the lease. It says these were not sale-leaseback transactions. Under the leases, Wajax could replace the equipment with a comparable piece of equipment if Cow Harbour did not exercise the purchase option during the first six months. Further, if Cow Harbour defaulted, Wajax was entitled only to the amounts that Cow Harbour owed to it under the agreement plus 30 percent of the aggregate rental charges for the unexpired portion of the term as a pre-estimate of liquidated damages. Wajax maintains this was a weak default clause.

153 Wajax points out that the assessed fair market value of the equipment in June of 2010 was significantly less than the purchase option price, even after the second term. As a result, Cow Harbour had not built up equity in the equipment through the lease agreements.

(b) Monitor

154 The Monitor acknowledges that the Wajax leases could be characterized as financing leases or true leases, depending on the approach used in performing the characterization analysis.

155 The Monitor says the Wajax leases were not security agreements under a personal property security analysis. However, it maintains that Cow Harbour made payments for use of and earned equity in the equipment during the first six months of the leases. This militates in favour of the leases being considered financing leases.

156 The Monitor notes that the six-month purchase option period had expired under each of the leases, and Wajax had not given any indication of its election to extend the purchase option period. Therefore, it would appear that Cow Harbour no longer had any equity in the leased equipment, which would militate in favour of each lease being considered a true lease.

(c) GE

157 GE contends that the Wajax leases bear several indicia of financing leases, including Cow Harbour's:

* obligation to pay all taxes incidental to ownership;
* responsibility for insuring the equipment;

* responsibility for payment of license fees for maintenance of the equipment;
* bearing the entire risk of loss

As well, it asserts that the default provisions were inordinately favourable to Wajax, and the leases contained a provision providing for liquidated damages.

158 GE contends that the rental payments earned Cow Harbour a significant equity interest in the equipment over the term of the leases. It says that the most significant factor is that Wajax intended to sell the equipment to Cow Harbour pursuant to the leases, as confirmed by Wajax's affiant. As well, Cow Harbour previously had purchased a number of pieces of the same type of equipment from Wajax.

3. Decision

159 Application of the ***Smith Brothers*** criteria to the Wajax leases reveals the following:

1. Whether there was an option to purchase for a nominal sum - No, the option purchase price was reflective of fair market value.
2. Whether there was a provision in the lease granting the lessee an equity or property interest in the equipment - Yes, but contingent on the option to purchase being exercised.
3. Whether the nature of the lessor's business was to act as a financing agency - No.
4. Whether the lessee paid sales tax incidental to acquisition of the equipment - Yes.
5. Whether the lessee paid all other taxes incidental to ownership of the equipment - Yes
6. Whether the lessee was responsible for comprehensive insurance on the equipment - Yes.
7. Whether the lessee was required to pay any licence fees for operation of the equipment at its expense - Yes.
8. Whether the agreement placed the entire risk of loss on the lessee - Yes.
9. Whether the agreement included a clause permitting the lessor to accelerate payment of rent on default by the lessee and granted remedies similar to those of a mortgage - Yes, but only 30 percent of the aggregate rental charges for the unexpired portion of the term, as a pre-estimate of liquidated damages.
10. Whether the equipment subject to the agreement was selected by the lessee and purchased by the lessor for this specific lease - Wajax is the exclusive dealer for Hitachi equipment in Canada. The equipment was new when it provided the equipment to Cow Harbour.
11. Whether the lessee was required to pay a substantial security deposit in order to obtain the equipment - No. However, rent for the minimum rental period was payable before delivery of the equipment.
12. Whether the agreement required the lessee to join the lessor or permit the lessor by himself to execute a UCC financing statement - Not applicable.
13. Whether there was a default provision in the lease inordinately favourable to lessor - No (see discussion below).
14. Whether there was a provision in the lease for liquidated damages - Yes (see discussion below).
15. Whether there was a provision disclaiming warranties of fitness and/or merchantability on the part of the lessor - Yes.
16. Whether the aggregate rentals approximated the value of the purchase price of the equipment - No.

160 The parties' intent in this case was that Cow Harbour would purchase the equipment, which was the subject of these leases, if it could find a third party to finance its purchase of the equipment.

161 If Cow Harbour exercised the option to purchase within the first six-month term of the leases, it would be credited with 85 percent of the rental payments made. Professors Cuming and Wood commented in the *Handbook* at 56 on this type of situation:

> Some leases provide that rental payments made up to the point when the option is exercised are to be "credited" to the lessee and deducted from the amount payable under the option. Under an economic realities test, the amount "credited" to the lessee has little significance; it remains necessary to determine if the amount of new money to be paid by the lessee represents the reasonably expected fair market value of the goods at the time of exercise of the option. If the new money is equal to or near the market value of the goods, the "credit" is of no significance. If the amount of new money is significantly less than the market value of the goods, the term providing for the credit is an overt recognition that the debtor has purchased an "equity" in the goods through his lease payments. It is inevitable that, as a rational person, the lessee will exercise the option in order to realize that equity.

162 This Court finds that the purchase option price or "new money" in this case was a reasonable pre-estimate of what the market value of the equipment would be if and when Cow Harbour exercised the option, taking into account depreciation, which was reflected by the rental "credit." These were relatively short term leases. In any event, the six-month option had expired for each lease and Wajax did not extend them for a second term.

163 While there was a default clause in each case which allowed for acceleration of rents, it was only for 30 percent of the aggregate rental charges for the unexpired portion of the term. Further, Cow Harbour had no liability for deficiency on sale of the leased property at the end of the term.

164 Accordingly, this Court finds that the Wajax leases were true leases.

D. Kempenfelt Vehicle Leasing (a Division of Equirex Vehicle Leasing 2007 Inc.) (Kempenfelt) Leases

1. <u>The Leases</u>

165 Kempenfelt had four leases with Cow Harbour, as described below:

Lease number	Date day/month/year	Initial Term (months)	Original Cost of Equipment	Monthly Rental	Option Price
ZNCS1001	2/2/ 2010	66	$202,738.90	$4,122.95 (plus one initial payment of $20,468)	$20,268 at 60 months, FMV at 66 months
ZNEW1002	10/2/2010	66	$145,000.00	$2,979.99 (plus one initial payment of $14,700)	$14,500 at 60 months, FMV at 66 months
ZEX1002	2/2/ 2010	66	$101,369.00	$2,061.48 (plus one initial payment of $10,334)	$10,134 at 60 months, FMV at 66 months
ZNEY1002	10/2/2010	66	$101,369.00	$2,061.48 (plus one initial payment of $10,334)	$10,134 at 60 months, FMV at 66 months

166 All the leases required Cow Harbour to make an initial payment, roughly equivalent to 10 percent of the original cost of the equipment, and approximately the same amount as the purchase option price. These payments are not identified as security deposits. However, clause 20 of each lease makes reference to a security deposit, which is refundable at the termination date of the lease, provided Cow Harbour has not defaulted under the lease.

2. <u>Lease-specific arguments of the parties</u>

(a) Kempenfelt

167 Kempenfelt takes the position that all of these leases fall within C*CAA* s. 11.01(a). In the alternative, Burke's primary/secondary factor approach applies, as the ***Smith Brothers*** factors are not equally probative of the issue as to whether the leases are true leases or financing leases.

168 Kempenfelt points out that under each lease, Cow Harbour was entitled to purchase the leased equipment for approximately 10 percent of its original value at the end of 60 months, or at fair market value at the end of the 66-month term. Kempenfelt's affiant deposed that the purchase option price was the estimated fair market value of the equipment at the conclusion of the lease term. She did not specify how Kempenfelt arrived at, or calculated, that value.

169 Kempenfelt notes that the leases contained a guaranteed residual clause, but only if Cow Harbour defaulted or on early termination of the leases. Kempenfelt contends that the acceleration of rents on default is typical of both true leases and financing leases. It says the leases were not full payment leases. Cow Harbour was not required to pay a security deposit or down payment. All payments were described in the leases as "rent."

(b) Monitor

170 The Monitor submits that the leases are best characterized as financing leases because the 60-month purchase option price (approximately 10 percent of the original value of the equipment) appears to be arbitrary and bears no direct connection to what the actual value of the leased equipment might be at the time Cow Harbour exercised the option.

171 The Monitor says the leases overwhelmingly exhibit other ***Smith Brothers*** indicia of a financing lease. Specifically, ***Smith Brothers*** financing lease factors 3 to 7, 9, 10 and 13 to 15 are present in the Kempenfelt leases. The Monitor asserts that the aggregate rental approximated the value of the purchase price of the equipment, factoring in interest and carrying costs. It points out that under the terms of lease ZNCS1001, the equipment originally was valued at $202,738 plus applicable tax, while the total amount Cow Harbour was to pay during the lease term, including the initial payment, was $288,459.95 plus applicable tax. In both leases ZEX1002 and ZNEY1002, the equipment originally was valued at $101,369 plus applicable tax, while the total amount Cow Harbour was to pay during the lease term of each lease, including the initial payment, was $144,330.30 plus applicable tax. In lease ZNEW1002, the equipment originally was valued at $145,000 plus applicable tax, while the total amount Cow Harbour was to pay during the lease term, including the initial payment, was $208,399.35 plus applicable tax.

(c) GE

172 GE contends that the Kempenfelt leases are full payment leases. GE notes that the aggregate cost of the rental payments exceeded the equipment's original cost in each case.

173 GE notes that the purchase option price exercisable after 60 payments was less than the remaining payments due under the leases. Therefore, the economic reality was that Cow Harbour would be inclined to purchase the equipment for that lower price.

3. <u>Decision</u>

174 The following are the results of applying the ***Smith Brothers*** criteria to the Kempenfelt leases:

1. Whether there was an option to purchase for a nominal sum - See discussion below.
2. Whether there was a provision in the lease granting the lessee an equity or property interest in the equipment - No.
3. Whether the nature of the lessor's business was to act as a financing agency - Yes.
4. Whether the lessee paid sales tax incidental to acquisition of the equipment - Yes.
5. Whether the lessee paid all other taxes incidental to ownership of the equipment - Yes.
6. Whether the lessee was responsible for comprehensive insurance on the equipment - Yes
7. Whether the lessee was required to pay any licence fees for operation of the equipment at its expense - Yes.
8. Whether the agreement placed the entire risk of loss on the lessee - Yes.
9. Whether the agreement included a clause permitting the lessor to accelerate payment of rent on default by the lessee and granted remedies similar to those of a mortgage - Yes.
10. Whether the equipment subject to the agreement was selected by the lessee and purchased by the lessor for this specific lease - Yes.

11. Whether the lessee was required to pay a substantial security deposit in order to obtain the equipment - The leases refer to a security deposit in clause 20.
12. Whether the agreement required the lessee to join the lessor or permit the lessor by himself to execute a UCC financing statement - Not applicable.
13. Whether there was a default provision in the lease inordinately favourable to lessor - Kempenfelt was permitted to accelerate rent on default.
14. Whether there was a provision in the lease for liquidated damages - Yes.
15. Whether there was a provision disclaiming warranties of fitness and/or merchantability on the part of the lessor - Yes.
16. Whether the aggregate rentals approximated the value of the purchase price of the equipment - Yes.

175 Each lease referred to a security deposit and stated that Cow Harbour would not earn any interest on the deposit. Kempenfelt was to return the security deposit to Cow Harbour on the termination of the lease. The leases, however, did not identify any security deposit, unless it was meant to be the first payment, which in each case was approximately 10 percent of the original value of the equipment, or five times the other monthly rental payments.

176 The aggregate of the rental payments, not including the initial payment, was more than the original cost of the equipment in each case. The purchase option price available at 60 months was approximately the same as the remaining five monthly rental payments, less interest.

177 At the end of the term of each lease, the lessee could return the equipment to Kempenfelt or exercise the option to purchase the equipment at fair market value.

178 This Court finds that the option served merely as window dressing. The economic reality was that Cow Harbour would have exercised the 60-month option, whether the first payment was considered a security deposit or actual rent.

179 Considering all of the ***Smith Brothers*** factors, this Court concludes that the Kempenfelt leases were financing leases.

E. Concentra Financial (Concentra) Lease

1. The Lease s

180 Concentra's lease 7958-1, dated February 24, 2006, was for a new off-highway mining truck. The original cost of the truck was $2,335,456, according to the Monitor's brief. The vendor was shown as Finning (Canada). The initial term of the lease was 60 months. The lease required one payment of $100,000 and 59 monthly payments of $35,224.79. The end of term resale value was identified as $415,000.

181 Under clause 10 of lease 7958-1, Cow Harbour unconditionally guaranteed the end of term minimum resale value of the equipment, on or at expiry of the lease or any renewal term.

182 Attached as part of an appendix to the Monitor's 13th Report was a Concentra lease credit approval relating to this equipment. Concentra approved a "loan" of $2,075,000, with an "origination fee" of $21,000 and contract initiation fee of $5,188. Monthly rental was shown as $35,224.78, with the term being 60 months. Approval was said to be subject to a "rental" payment in advance of $100,000. Also attached was a Capital City Savings amortization schedule for a $2,075,000 loan, at a nominal annual rate of 8.321 percent, compounded monthly, showing the payments noted above in the lease document, plus a $415,000 payment on February 20, 2011. The copies of these document that this Court reviewed were not signed and Concentra's affiant was not cross-examined on them.

183 The other lease is referred to as "Alter Moneta Equipment Schedule Number 2 to Master Lease No.

CCB5314A." It is dated April 18, 2007 and was assigned to Concentra by Alter Moneta Corporation on September 27, 2007. The subject of the lease was a new CAT off-highway truck and accessories, the net price of which was shown as $2,558,295. The term of the lease was 60 months. The payment schedule addendum provided for an initial payment of $683,295 and 59 monthly payments of $40,372.39 each. The lease contained an option to purchase for $1 at the end of the initial lease term or end of any renewal period

2. <u>Lease-specific arguments of the parties</u>

(a) Concentra

184 Concentra notes that under clause 9 of lease 7958-1, if either party elected not to renew the lease or elected to cancel it during the renewal period, the lessee could return the equipment to Concentra.

185 Concentra suggests the default clause is typical, presumably meaning it is equivocal.

186 Lease 7958-1 did not have an option to purchase. Nor was there a mandatory option requirement. There was no ability for the lessee to exchange equipment. Concentra concedes the $100,000 payment was a down payment.

187 In terms of the Alter Moneta Corporation assigned lease, Concentra argues that even an option at a nominal purchase price is irrelevant until such time as Cow Harbour exercises the option (***Ed Miller***; see this Court's discussion above). Concentra notes that the option did not state that it was mandatory. As well, there was a guaranteed residual clause. Concentra contends that it is a matter of interpretation whether the termination options or the end of term options make the lease open-ended. The lease was not stated to be a full payment lease and there was no security deposit. The down payment was only about 20 to 25 percent of the equipment's initial acquisition cost.

(b) Monitor

188 The Monitor says that lease 7958-1 is best characterized as a financing lease because, among other things, it contained a "guaranteed residual clause" in clause 10, thereby constituting it a security agreement under a personal property security analysis. The Monitor asserts that because it is a security agreement under a personal property security analysis, it falls outside of the scope of *CCAA* s. 11.01(a).

189 As well, the Monitor submits that lease 7958-1 overwhelmingly exhibits the ***Smith Brothers*** indicia of a financing lease. Specifically, ***Smith Brothers*** factors 3 to10 and 13 to16 are present. It notes that the equipment originally was valued at $2,335,456 plus applicable tax, while the total amount that Cow Harbour was to pay during the course of the lease term was $2,593,261.84 plus applicable tax. Therefore, the aggregate rental approximated the value of the purchase price of the equipment, factoring in interest and carrying costs.

(c) GE

190 GE takes the position that both leases have indicia of financing leases. Under lease 7958-1, Cow Harbour guaranteed the end of term resale value of the equipment ($415,000) to Concentra, which suggests this is financing lease.

191 GE says the Alter Moneta Corporation assigned lease was substantively identical to the Alter Moneta Corporation lease (discussed below) in having a mandatory end of term purchase obligation for $1. This also points to it being a financing lease.

3. <u>Decision</u>

192 The following are the results of applying the ***Smith Brothers*** criteria to the Concentra leases:

1. Whether there was an option to purchase for a nominal sum - No option to purchase in lease 7958-1, but end of term resale value guaranteed; nominal option price for the Alter Moneta Corporation assigned lease.
2. Whether there was a provision in the lease granting the lessee an equity or property interest in the equipment - No.
3. Whether the nature of the lessor's business was to act as a financing agency - Yes.
4. Whether the lessee paid sales tax incidental to acquisition of the equipment - Yes.
5. Whether the lessee paid all other taxes incidental to ownership of the equipment - Yes.
6. Whether the lessee was responsible for comprehensive insurance on the equipment - Yes
7. Whether the lessee was required to pay any licence fees for operation of the equipment at its expense - Yes.
8. Whether the agreement placed the entire risk of loss on the lessee - Yes.
9. Whether the agreement included a clause permitting the lessor to accelerate payment of rent on default by the lessee and granted remedies similar to those of a mortgage - Yes.
10. Whether the equipment subject to the agreement was selected by the lessee and purchased by the lessor for this specific lease - Yes.
11. Whether the lessee was required to pay a substantial security deposit in order to obtain the equipment - There was a down payment for both leases.
12. Whether the agreement required the lessee to join the lessor or permit the lessor by himself to execute a UCC financing statement - Not applicable.
13. Whether there was a default provision in the lease inordinately favourable to lessor - Yes.
14. Whether there was a provision in the lease for liquidated damages - Yes.
15. Whether there was a provision disclaiming warranties of fitness and/or merchantability on the part of the lessor - Yes.
16. Whether the aggregate rentals approximated the value of the purchase price of the equipment - Yes, in terms of lease 7958-1, but the aggregate would not account for financing charges on the full amount. However, the aggregate was equal to a lesser amount with monthly compounded interest. Yes, in terms of the Alter Moneta Corporation assigned lease.

193 Lease 7958-1 did not contain an option to purchase. At the end of the term, end of any renewal period, or on default, Cow Harbour was required to pay the residual value of the equipment. Cow Harbour, however, also was required to return the equipment to Concentra. If Concentra sold the equipment and the sale yielded an amount less than the end of term minimum resale value, Cow Harbour was responsible for the deficiency (at Concentra's option), but was not entitled to any surplus.

194 Burke stated at 294 that:

> Where the lessee is liable under an open-end lease for any deficiency in the sale of the leased property following its return at the end of the scheduled lease term, the current line of authority is to treat such a lease as a security lease, because a lessor is "guaranteed" to receive a minimum return on the transaction.

195 Burke cited ***Crop & Soil Services, Inc. v. Oxford Leaseway Ltd.*** (2000), 48 OR (3d) 291 (CA) as authority for this proposition. That case, however, and those referred to in it, involved situations where the lessee was entitled, as well, to any surplus on the sale of the equipment.

196 Burke suggested (at 296) that a substantial down payment is indicative of a financing lease in that the lessee may be viewed as acquiring an equity interest in the leased property.

197 The parties presented no evidence that 60 months was the anticipated useful life of the truck. There was no purchase option. Even though Concentra had a residual value guarantee and Cow Harbour made a substantial down payment, Cow Harbour was required to return the truck at the end of the lease term or renewal period, and it was not entitled to any surplus above the end of term minimum resale value, this Court finds that the Concentra lease was a true lease.

198 The aggregate of rents for the Alter Moneta Corporation assigned lease was approximately $3,065,266, which was greater than the $2,558,295 net price. A substantial down payment was required. The assigned lease contained an option to purchase for $1. The economic reality is that Cow Harbour would have exercised that option. The lease contained other lesser indicia of a financing lease. This Court concludes that the Alter Moneta assigned lease was a financing lease.

F. Alter Moneta Corporation (Alter Moneta) Lease

1. The Lease

199 The lease dated January 21, 2008 between Alter Moneta and Cow Harbour was Equipment Schedule No. 003 to Master Lease No. CCB5314A.

200 The net price of the leased equipment, a new 2008 Caterpillar off-highway truck, was shown as $2,737,433. The lease term was 60 months. Addendum 4 to the lease called for an initial payment of $273,743.30 and 59 monthly payments of $53,116.94.

201 At the end of the initial term or renewal period, Cow Harbour, if not in default, had the option to purchase the lessor's interest and title in the equipment for $1 or to renew the lease for a further 12 months for the same monthly lease payment.

2. Lease-specific arguments of the parties

(a) Alter Moneta

202 Alter Moneta advanced the same arguments as those advanced in relation to the Alter Moneta lease that Alter Moneta assigned to Concentra. In particular, it argued that the nominal purchase option price was irrelevant until such time as Cow Harbour exercised the option.

203 Alter Moneta notes that the option to purchase was not mandatory, there was no residual guarantee clause and the document did not relate the amount of payments to the purchase price. Alter Moneta says that the document refers to all payments as rent, but the initial payment is different from the others.

(b) GE

204 GE notes that the aggregate value of the rental payments over the term of the lease ($3,407,643) exceeded the cost of the leased equipment ($2,737,433).

205 GE asserts that, inasmuch as the option to purchase was for $1, the economic reality is that Cow Harbour would have bought the leased equipment.

3. Decision

206 The following results from application of the ***Smith Brothers*** criteria to the Alter Moneta lease:

1. Whether there was an option to purchase for a nominal sum - Yes, the option purchase price was $1 at the end of the term.
2. Whether there was a provision in the lease granting the lessee an equity or property interest in the equipment - No.
3. Whether the nature of the lessor's business was to act as a financing agency - Yes.

4. Whether the lessee paid sales tax incidental to acquisition of the equipment - Yes.
5. Whether the lessee paid all other taxes incidental to ownership of the equipment - Yes.
6. Whether the lessee was responsible for comprehensive insurance on the equipment - Yes
7. Whether the lessee was required to pay any licence fees for operation of the equipment at its expense - Yes.
8. Whether the agreement placed the entire risk of loss on the lessee - Yes.
9. Whether the agreement included a clause permitting the lessor to accelerate payment of rent on default by the lessee and granted remedies similar to those of a mortgage - Yes.
10. Whether the equipment subject to the agreement was selected by the lessee and purchased by the lessor for this specific lease - Yes.
11. Whether the lessee was required to pay a substantial security deposit in order to obtain the equipment - There is a large down payment required, although it is referred to as "rent."
12. Whether the agreement required the lessee to join the lessor or permit the lessor by himself to execute a UCC financing statement - Not applicable.
13. Whether there was a default provision in the lease inordinately favourable to lessor - Yes.
14. Whether there was a provision in the lease for liquidated damages - Yes.
15. Whether there was a provision disclaiming warranties of fitness and/or merchantability on the part of the lessor - Yes.
16. Whether the aggregate rentals approximated the value of the purchase price of the equipment - Yes.

207 The aggregate of the lease payments was greater than the net price of the equipment. Cow Harbour was required to make a substantial down payment. The lease contained an option to purchase for $1. Alter Moneta's affiant deposed that the option was for the estimated fair market value of the equipment at the end of the lease term. If it is seen as a nominal purchase option price, the economic reality is that Cow Harbour would have exercised that option. If it is a reflection that the equipment was expected to be at the end of its useful life at the conclusion of the lease, Alter Moneta, in essence, was giving credit to Cow Harbour for its purchase of the equipment. The lease contained other ***Smith Brothers*** indicia of a financing lease.

208 As with the Alter Moneta lease that Alter Moneta assigned to Concentra, this Court concludes that this lease was a financing lease.

G. Key Equipment Finance Canada Ltd. (Key Equipment) Lease

1. The Lease

209 Key Equipment was the assignee of a lease agreement dated November 15, 2006 between Alter Moneta and Cow Harbour (assigned June 27, 2008) relating to a hydraulic excavator. The agreement was described as Equipment Schedule No. 001 to Master Lease No. CCB5314A

210 The equipment's value at the time of the lease agreement was stated to be $1,484,277.99. The lease term was 60 months. Addendum 4 to the lease agreement called for an initial payment of $148,429.80, with 59 monthly payments of $26,777.34.

211 Addendum 3 to the lease provided that if the lease had not been terminated earlier and if the lessee was not in default, the "Lessee shall... elect for one of the following options" (emphasis added). The three options were to: (1) purchase the equipment on November 15, 2011 (the option date) for $148,429.80 plus taxes (the purchase option price), which was said to be the estimated fair market value of the equipment at that date; (2) find a third party to purchase the equipment on the option date for the purchase option price; or (3) rent the equipment for a further period and periodic rent to be established by the lessor acting reasonably.

212 Clause 27 of the Master Lease provided that if there was a substantial adverse change in Cow Harbour's financial circumstances, the lessor could terminate the lease, at the lessor's sole option.

2. Lease-specific arguments of the parties

(a) Key Equipment

213 Key Equipment argues that the purchase option price was not nominal. Instead, it was an amount to which the parties agreed at the outset to be the estimated fair market value of the equipment at the end of the lease term. Key Equipment takes no position on whether the option can be characterized as mandatory.

214 Key Equipment points out that the termination provision in clause 27 of the Master Lease is common to all Alter Moneta leases (including this one and the one Alter Moneta assigned to Concentra). Key Equipment says that the lease agreement did not contain a guaranteed residual clause and it is a matter of interpretation whether the renewal provision made this an open-ended lease. The lease did not state that it is a full payment lease. Key Equipment submits that all payments under the lease were rent.

(b) Monitor

215 The Monitor submits that this lease was a financing lease since the end of term purchase option price (approximately 10 percent of the original value of the equipment) appears to be arbitrary, rather than bearing some connection to what the actual value of the equipment might be at the time Cow Harbour could exercise the option.

216 The Monitor maintains that the lease overwhelmingly exhibits other ***Smith Brothers*** indicia of a financing lease, which militates against it being considered a true lease. Specifically, ***Smith Brothers*** factors 3 to 10 and 13 to 16 are present, indicating a financing lease. The Monitor points out that the equipment originally was valued at $1,484,297.99 plus applicable tax while the total amount Cow Harbour was to pay during the course of the term was $1,728,292.86 plus applicable tax. Therefore, the aggregate rental approximated the value of the purchase price of the equipment, factoring in interest and carrying costs.

(c) GE

217 GE notes that the aggregate of rental payments exceeded the cost of the equipment, which suggests that this lease agreement was a financing lease. It points out that Cow Harbour was required to purchase the equipment at an option purchase price of $148,429.80 plus tax, find a purchaser for it at the purchase option price, or renew the lease. Cow Harbour could not return the equipment to Key Equipment.

3. Decision

218 Application of the ***Smith Brothers*** factors to the Key Equipment lease produces the following results:

1. Whether there was an option to purchase for a nominal sum - There was an option, but it was not for a nominal sum.
2. Whether there was a provision in the lease granting the lessee an equity or property interest in the equipment - No.
3. Whether the nature of the lessor's business was to act as a financing agency - Yes.
4. Whether the lessee paid sales tax incidental to acquisition of the equipment - Yes.
5. Whether the lessee paid all other taxes incidental to ownership of the equipment - Yes.
6. Whether the lessee was responsible for comprehensive insurance on the equipment - Yes.
7. Whether the lessee was required to pay any licence fees for operation of the equipment at its expense - Yes.
8. Whether the agreement placed the entire risk of loss on the lessee - Yes.

9. Whether the agreement included a clause permitting the lessor to accelerate payment of rent on default by the lessee and granted remedies similar to those of a mortgage - Yes.
10. Whether the equipment subject to the agreement was selected by the lessee and purchased by the lessor for this specific lease - Yes.
11. Whether the lessee was required to pay a substantial security deposit in order to obtain the equipment - There was a substantial down payment.
12. Whether the agreement required the lessee to join the lessor or permit the lessor by himself to execute a UCC financing statement - Not applicable.
13. Whether there was a default provision in the lease inordinately favourable to lessor - Yes.
14. Whether there was a provision in the lease for liquidated damages - Yes.
15. Whether there was a provision disclaiming warranties of fitness and/or merchantability on the part of the lessor - Yes.
16. Whether the aggregate rentals approximated the value of the purchase price of the equipment - Yes.

219 The purchase option price in this case was approximately 10 percent of the original cost of the equipment, which is not a nominal amount. The parties agreed that this was a pre-estimate of the market value of the equipment at the end of the lease term. Ordinarily, a fair market value option would be highly suggestive of a true lease. In this case, however, Key Equipment was guaranteed the option price, as Cow Harbour was required to exercise the option, find a third party who would pay the option price, or renew the lease for a term and at a rate selected at the sole option of Key Equipment. This was equivalent to a mandatory purchase option. Cow Harbour could not return the equipment to Key Equipment. As Burke stated (at 294):

> ... leases that do not provide the lessee with the option to return the equipment (i.e., the only available options to a lessee at the end of the scheduled term of the lease are either to purchase the leased property or to renew the lease) can be expected to be construed as conditional sales, because the inability of the lessee to return the leased property at the end of the term will likely be construed as effectively requiring the lessee to acquire the leased property.

220 The Key Equipment lease also contained other indicia of a financing lease. This Court concludes that it was a financing lease.

VI. Conclusions

221 This Court categorizes the Disputed Leases as follows:

A. Scott Capital's leases were true leases.
B. CFSL's lease was a true lease.
C. Wajax's leases were true leases.
D. Kempenfelt's leases were financing leases.
E. Concentra's lease was a true lease. The Alter Moneta lease assigned to Concentra was a financing lease.
F. Alter Moneta lease was a financing lease.
G. The Alter Moneta lease assigned to Key Equipment was a financing lease.

222 The true leases are subject to *CCAA* s. 11.01(a).

K.D. YAMAUCHI J.

Bed Bath & Beyond Canada Ltd. (Re), [2023] O.J. No. 2165

Ontario Judgments

Ontario Superior Court of Justice

Centre

G.B. Morawetz C.J.S.C.J.

Heard: April 11, 2023.

Judgment: April 11, 2023.

Released: April 14, 2023.

Court File No. CV-23-694493-00CL

[2023] O.J. No. 2165 | 2023 ONSC 2308

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 BBB Canada Ltd.

(26 paras.)

Counsel

Shawn Irving, Emily Paplawski and Blair McRadu, for the Applicant Bed Bath & Beyond Ltd.

Jeffrey Levine and Wael Rostom, for Sixth Street Specialty Lending, Inc. (FILO Agent).

Linda Galessiere, for Landlords of BBB Canada, namely, RioCan; Ivanhoe, SmartCentre; corp and Royop.

Max Freedman, U.S. Counsel to the Applicant.

Kevin Zych, Michael Shakra and Joshua Foster, for the Monitor, Alvarez & Marsal Canada Inc.

Roger M. Jaipargas, for 1431582 Alberta Inc.

Evan Cobb, for JPMorgan Chase (ABL Lenders).

Nate Fennema, Mike Shakra, Sean Zweig and Joshua Foster, for the Monitor, Alvarez & Marsal Canada Inc.

John C. Wolf, for Sun Life Assurance Company, Heritage Greene Development Corporation, Skyline Retail Real Estate Holdings Inc., and Queensway 427 Centre Inc.

Monique Sassi, for the Hilco Merchant Retail Solutions, ULC, Gordon Brothers Canada ULC, Tiger Asset Solutions Canada, ULC, and B. Riley Retail Solutions ULC.

Craig Firth, for Preston West Properties Ltd.

Steven Weisz, for Canadian Tire Corporation.

Kyle Plunkett, for DKB Capital.

Heather Meredith, for Langley City Square Properties Ltd., Sunstone Opportunity (2007) Realty Trust and Fiera Real Estate Core Fund GP Inc. on behalf of Fiera Real Estate Core Fund LP.

Dina Peat, for 1651051 Alberta Ltd., 1826997 Ontario Inc., Yonge Bayview Holdings Inc., Airport Highway 7 Developments Limited, Woodhill Equities Inc. and Winston Argentia Developments Limited.

ENDORSEMENT

G.B. MORAWETZ C.J.S.C.J.

1 On February 10, 2023, BBB Canada Ltd. (the "Applicant"), along with Bed Bath & Beyond Canada L.P. ("BBB LP", and together with the Applicant, "BBB Canada"), was granted protection under the *Companies' Creditors Arrangement Act*, R.S.C. 1985 c. C-36 (the "CCAA") pursuant to an Initial Order (the "Initial Order"). Alvarez & Marsal Canada Inc. was appointed to act as the Monitor (the "Monitor"). On February 21, 2023, the court granted an Amended and Restated Initial Order (the "ARIO") and a Sale Approval Order.

2 BBB Canada has retained Retail Ventures CND Inc. ("RVC") as its exclusive listing agent for the purpose of facilitating the sale of leases and other property rights for some or all of BBB Canada's retail stores across Canada (the "Leases").

3 BBB Canada brings this motion for an order approving the Omnibus Assignment and Assumption of Leases, FF&E and Trade Fixtures Agreement, dated March 28, 2023 (the "DKB Capital Agreement") between BBB LP, Bed Bath & Beyond Inc. ("BBBI") and 11607987 Canada Inc., dba DKB Capital ("DKB Capital"). Under the terms of the Amended and Restated Order ("ARIO"), court approval is required for the DKB Capital Agreement.

4 The Applicant accordingly seeks the following orders:

(a) an order approving the DKB Capital Agreement;

(b) an order assigning certain Leases to DKB Capital pursuant to section 11.3 of the CCAA on an unopposed basis;

(c) an order vesting BBB LP's right, title and interest in and to certain Leases and other purchased assets in DKB Capital free and clear of all Encumbrances other than permitted encumbrances identified in, or pursuant to, the DKB Capital Agreement; and

(d) an order directing that the unredacted copy of the DKB Capital Agreement be treated as confidential and sealed, and not form part of the public record, until the earlier of: (1) the closing of the DKB Capital Agreement, (2) disclaimer of the Leases subject to the DKB Capital Agreement, or (3) any further order of the Court.

5 The Applicant submits that the DKB Capital Agreement is the culmination of a marketing process and should be approved on the basis that the criteria set out in section 36(3) of the CCAA are clearly satisfied.

6 The Applicant further submits that the consideration paid by DKB Capital for the applicable Leases is fair and reasonable in the circumstances. It represents the highest, non-overlapping executable offer received within the marketing process.

7 The Monitor supports the position of the Applicants and no party opposed the requested relief.

8 The facts regarding this motion are fully set out in the affidavit of Wade Haddad.

9 The following issues are raised on this motion:

(a) should the court approve the DKB Capital Agreement and grant the proposed Assignment, Approval and Vesting Order;

(b) should the court assign certain Leases to DKB Capital pursuant to section 11.3 of the CCAA on an unopposed basis; and

(c) should the court grant an order directing that the unredacted DKB Capital Agreement be treated as confidential and sealed, and not form part of the public record, until the earlier of: (1) the closing of the DKB Capital Agreement, (2) disclaimer of the Leases subject to the DKB Capital Agreement, or (3) any further order of this court.

10 Section 36 of the CCAA sets out the legal test for obtaining court approval that applies where a debtor company seeks to sell assets outside the ordinary course of business during a CCAA proceeding.

11 The Applicant submits that, taking into account the criteria listed in Section 36(3) of the CCAA, the court should approve the DKB Capital Agreement and grant the proposed Assignment, Approval and Vesting Order.

12 I am satisfied that the record establishes that the process followed by the listing agent was comprehensive and garnered significant interest from third parties.

13 Further, the Monitor has been involved in the marketing process and supports the requested relief. The Monitor's views in this respect are entitled to deference.

14 BBB Canada, RVC, and the Monitor are each of the view that the consideration to be received by BBB Canada under the DKB Capital Agreement is fair and reasonable.

15 The Applicant submits that BBB Canada and the listing agent undertook a comprehensive sales and marketing process for the sale of the Leases. I am satisfied that the evidence establishes there is ample evidence that the market has been thoroughly tested in order to obtain the best price.

16 I am also satisfied that the DKB Capital Agreement is beneficial to the creditors and other stakeholders of the Applicant.

17 The DKB Capital Agreement provides that certain of the Leases will be assigned in accordance with section 11.3 of the CCAA on an unopposed basis.

18 Section 11.3 of the CCAA gives this Court jurisdiction and the discretion to make an order assigning the rights and obligations of the debtor company.

19 The Applicants submit that the requested assignments are critical to closing the transactions contemplated in the DKB Capital Agreement and are essential to the ability of the Applicant to realize upon the value of these transactions for the benefit of all stakeholders. In addition, there can be no suggestion that counterparties are being treated unfairly, as each of the requested assignments are proceeding on an unopposed basis.

20 I accept these submissions and I am satisfied that the assignment of certain Leases should be approved.

21 It is noted, however, that the parties have expressly agreed that in respect of any leases not subject to this Order assigning leases pursuant to s. 11.3 of the CCAA, the issue of whether the test under s. 11.3 of the CCAA has been met in respect of any future motion under s. 11.3 of the CCAA is to be treated as de novo in respect of any further motion to compel assignment of any other leases. The issuance of this Order assigning leases shall not be directly or indirectly argued as the basis for granting such relief in the future.

22 Finally, the Applicant requests that the unredacted copy of the DKB Capital Agreement be temporarily treated as confidential and sealed, and not form part of the public record, until the earlier of: (1) the closing of the DKB

Capital Agreement, (2) disclaimer of the Leases subject to the DKB Capital Agreement, or (3) any further order of this Honourable Court.

23 The test for a sealing order was established by the Supreme Court in *Sierra Club*, and subsequently recast in *Sherman Estate*. The test requires the court to consider whether:

(a) court openness poses a serious risk to an important public interest;

(b) the order sought is necessary to prevent this serious risk to the identified interest because reasonable alternative measure will not prevent this risk; and

(c) as a matter of proportionality, the benefits of the order outweigh its negative effects.

24 The request for the proposed sealing order is supported by the Monitor.

25 Having considered the *Sherman Estate* test, I am satisfied that it is appropriate to grant the sealing order. The proposed order is limited both in scope and time and is appropriate in the circumstances.

26 The motion is granted and the order has been signed.

G.B. MORAWETZ C.J.S.C.J.

Bankruptcy and Insolvency Act, R.S.C. 1985, c. B-3, s. 84.1

Canada Statutes

R.S.C. 1985, c. B-3, s. 84.1 | L.R.C. 1985, ch. B-3, art. 84.1

Canada Statutes > Bankruptcy and Insolvency Act [ss. 1-285] > PART IV PROPERTY OF THE BANKRUPT [ss. 67-101.2] > General Provisions [ss. 70-84.2]

Notice

Current Version: Effective 15-12-2009

SECTION 84.1

Assignment of agreements
84.1 (1) On application by a trustee and on notice to every party to an agreement, a court may make an order assigning the rights and obligations of a bankrupt under the agreement to any person who is specified by the court and agrees to the assignment.
Individuals
(2) In the case of an individual,

(a) they may not make an application under subsection (1) unless they are carrying on a business; and

(b) only rights and obligations in relation to the business may be assigned.

Exceptions
(3) Subsection (1) does not apply in respect of rights and obligations that are not assignable by reason of their nature or that arise under

(a) an agreement entered into on or after the date of the bankruptcy;

(b) an eligible financial contract; or

(c) a collective agreement.

Factors to be considered
(4) In deciding whether to make the order, the court is to consider, among other things,

(a) whether the person to whom the rights and obligations are to be assigned is able to perform the obligations; and

(b) whether it is appropriate to assign the rights and obligations to that person.

Restriction
(5) The court may not make the order unless it is satisfied that all monetary defaults in relation to the agreement - other than those arising by reason only of the person's bankruptcy, insolvency or failure to perform a nonmonetary obligation - will be remedied on or before the day fixed by the court.
Copy of order
(6) The applicant is to send a copy of the order to every party to the agreement.

Ford Credit Canada Ltd. v. Welcome Ford Sales Ltd., [2011] A.J. No. 592

Alberta Judgments

Alberta Court of Appeal

Edmonton, Alberta

K.G. Ritter, P.W.L. Martin and M.B. Bielby JJ.A.

Heard: March 4, 2011.

Judgment: May 27, 2011.

Dockets: 1003-0089-AC, 1003-0362-AC

Registry: Edmonton

[2011] A.J. No. 592 | 2011 ABCA 158 | [2011] 8 W.W.R. 221 | 77 C.B.R. (5th) 278 | 505 A.R. 146 | 2011 CarswellAlta 883 | 44 Alta. L.R. (5th) 81

Between Ford Motor Company of Canada, Limited, Appellant, (Applicant), and Welcome Ford Sales Ltd. and Royle Smith, Respondents, (Respondents) And between Ford Motor Company of Canada, Limited, Appellant, (Applicant), and Welcome Ford Sales Ltd., by its Receiver, Manager and Trustee in Bankruptcy, Myers Norris Penny Ltd. and Bank of Montreal, Respondents, (Respondents)

(73 paras.)

Counsel

K.B. Mills, K.J. Bourassa, for the Appellant.

J.H. Hockin, B.P. Maruyama, for the Respondents, Welcome Ford Sales Ltd., Royle Smith and Welcome Ford Sales Ltd., by its Receiver, Manager and Trustee in Bankruptcy, Meyers Norris Penny Ltd.

R.C. Rutman, A.L. Murray, for the Respondent, Bank of Montreal.

Memorandum of Judgment

The following judgment was delivered by

THE COURT

INTRODUCTION

1 This appeal was dismissed from the bench with reasons to follow.

2 This was an appeal from a decision granting permission to a bankruptcy trustee to sell an auto dealership agreement to a third party over the objections of the other party to the agreement, an auto manufacturer, pursuant to the provisions of the relatively new s. 84.1 of the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3 ("BIA").

3 Welcome Ford, owned by Royale Smith ("Smith"), operated a franchise dealership with the Appellant, Ford Motor Company of Canada, Limited ("Ford") in Fort Saskatchewan, Alberta pursuant to the terms of a written dealership agreement. The dealership ceased operations on January 13, 2010 after Ford Credit Canada Ltd. ("Ford Credit"), while conducting a physical audit on its premises, discovered a large defalcation apparently made by a senior employee of the dealership. The following day, the chambers judge, acting as *de facto* case manager, appointed Myers Norris Penny ("MNP") the Receiver of Welcome Ford on the application of Ford Credit.

4 Ford Credit tendered evidence in support of that application showing that over $3.7 million to which it was entitled had been misappropriated. At that time, Welcome Ford owed Ford Credit approximately $7.7 million and owed the Bank of Montreal ("BMO") approximately $2.7 million. Ford Credit had priority in relation to the vehicle inventory, while BMO had a priority claim to all other assets. As a result, Ford Credit seized and removed all vehicles over which it had security. It is an unsecured creditor for any shortfall on its debt remaining after the sale of those vehicles.

5 The order appointing the Receiver stayed all rights and remedies against Welcome Ford; in particular, it ordered that no agreements then in place, including the dealership agreement, be terminated without consent of the court. Ford advised as early as January 29, 2010 that it would not consent to the assignment/sale of the dealership agreement to any party. However, on March 23, 2010, the chambers judge granted an order authorizing MNP to market the dealership while adjourning Ford Credit's application to lift the stay so as to be able to terminate the dealership agreement ("the March order").

6 On May 19, 2010, BMO obtained an order placing Welcome Ford into bankruptcy with MNP as trustee, which had the effect of making the administration subject to the BIA, including s. 84.1 of that statute.

7 MNP marketed the dealership to existing Ford dealers only, receiving offers to purchase from the ultimate purchaser and two others. Ford maintained its refusal to consent to a sale, even to one of its own dealers, notwithstanding that the offer made by the ultimate purchaser, the highest bidder, would have produced sufficient funds to retire the debt to BMO in its entirely and produce a further $570,000 (before professional fees) to be distributed among the unsecured creditors. In comparison, liquidation of the assets without sale of the dealership agreement was expected to produce a far smaller sum, one which would leave more than $1 million of the debt to BMO unpaid and produce nothing for any other creditor.

8 On December 10, 2010, the chambers judge approved MNP's application to assign the rights and obligations of Welcome Ford under the dealership agreement to the ultimate purchaser pursuant to s. 84.1 of the BIA. At the same time, he dismissed Ford's application for a declaration that the dealership agreement could not be assigned without its consent and to lift the stay ("the December orders"). This appeal was then brought against each of the March and December orders.

9 The BIA was amended on December 15, 2009 by the addition of s. 84.1, which allows a court, upon being satisfied that certain prerequisites are met, to grant an order assigning the rights and obligations of the bankrupt under any agreement to a purchaser, even without the consent of the counter-party to the agreement.

10 The Respondents argued that the dealership agreement was properly assignable to the ultimate purchaser under this section, even absent Ford's consent. Ford argued that the dealership agreement had been terminated as a result of a fundamental breach occurring before the granting of the receivership order such that there was nothing left to assign to the ultimate purchaser. It, alternatively, argued that the dealership agreement is not assignable by reason of its nature and, as such, the issues of whether the ultimate purchaser is able to perform the obligations under it and whether it is appropriate to assign it are irrelevant.

11 The issues raised on appeal are:

(A) Has the dealership agreement terminated because of fundamental breach?

(B) How is s. 84.1 of the BIA to be interpreted?

(i) Is s. 84.1(3) to be interpreted without reference to s. 84.1(4)?

(ii) Are the rights and obligations imposed by the dealership agreement not assignable by reason of their nature because:

(a) the estate will not benefit from the assignment?; or

(b) they are personal in nature?

(iii) Should the dealership agreement not be assigned because of the capacity of the proposed assignee or because it is inappropriate to assign Welcome Ford's rights and obligations under s. 84.1(4)?

STANDARD OF REVIEW

12 The standard of review to be applied to the interpretation of s. 84.1 of the BIA, a question of law, is that of correctness. The chambers judge's findings of fact and application of facts to the law are subject to deference absent palpable and overriding error. The application of deference is amplified when, as here, the decision was not issued by a chambers judge in the normal course but by a case management judge whose decision is part of a series of decisions in relation to the same matter: see ***De Lage Landen Financial Services Canada Inc. v. Royal Bank of Canada***, 2010 ABCA 394 at para. 13.

ANALYSIS

(A) Has the dealership agreement terminated because of fundamental breach?

13 Ford argued that Welcome Ford "fundamentally breached" the dealership agreement before the appointment of the Receiver, with the result that the agreement came to an end such that nothing remained for the trustee to assign to the ultimate purchaser. It submitted the acts amounting to "fundamental breaches" include the abandonment of the business on January 13, 2010 and Smith's failure to properly supervise employees.

14 We note the decision of the Supreme Court of Canada in ***Tercon Contractors Ltd. v. British Columbia (Transportation and Highways)***, 2010 SCC 4, [2010] 1 S.C.R. 69 to the effect that the concept of fundamental breach no longer exists, at least in relation to exclusion clauses. The Court stated at 62:

> On the issue of fundamental breach in relation to exclusion clauses, my view is that the time has come to lay this doctrine to rest, ..."

and at 82:

> On this occasion we should again attempt to shut the coffin on the jargon associated with "fundamental breach". Categorizing a contract breach as "fundamental" or "immense" or "colossal" is not particularly helpful. ...

15 As no party raised this issue, and the breaches in question here were not of exclusion clauses, we will proceed to our analysis on the basis of the case as argued. That said, it may well be that the simple answer to the issue of whether the dealership agreement was terminated as a result of fundamental breach must be "no" because no such breach was possible.

16 Ford agreed the test for fundamental breach and its application to a franchise agreement is that relied upon by the chambers judge, established in ***Shelanu Inc. v. Print Three Franchising Corporation*** (2003), 64 O.R. (3d) 533 (C.A.) at paras. 113 and 114 as follows:

> [113] In *Majdpour v. M & B Acquisition Corp.* (2001), 56 O.R. (3d) 481, 206 D.L.R. (4th) 627 (C.A.), the event alleged to have triggered a fundamental breach of the franchise agreement by the franchisor was a bankruptcy. Because the franchisee was able to carry on the commercial purpose of the agreement intact after the bankruptcy, MacPherson J.A. dismissed the franchisee's claim [sic] it was discharged from further performance. That reasoning is equally applicable in this case.

> [114] In dismissing the claim for fundamental breach, MacPherson J.A. noted that the test was a restrictive one, namely, whether the conduct of one party deprived the other party of "substantially the whole benefit of the contract" as stated by Wilson J. in *Hunter Engineering, supra*, [1989] 1 S.C.R. 426. This is the classic formulation of the test as set out by Diplock L.J. in *Hongkong Fir Shipping Co. Ltd. v. Kawasaki Kisen Kaisha Ltd.*, [1962] 1 All E.R. 474, [1962] 2 Q.B. 26 (C.A.) at p. 66 Q.B.:
>
>> [D]oes the occurrence of the event deprive the party who has further undertakings still to perform of substantially the benefit which it was the intention of the parties as expressed in the contract that he should obtain in consideration for performing those undertakings?

17 In application of this test to the facts in this case, the question becomes whether the "abandonment" of the business or Smith's failure to supervise employees, leading to the defalcation, deprived Ford of the ability to carry on the commercial purpose of the dealership agreement.

18 The chambers judge concluded that the reason Welcome Ford had not operated since mid-January, 2010 was not for lack of trying by the Receiver, but rather because it was met at every step by resistence from Ford. Without receipt of new product and manufacturer's support of that product, the Receiver could not operate the dealership. He found that the proposed sale of the dealership including the dealership agreement would substantially, if not entirely, cure all of the alleged defects under that agreement.

19 It is not clear from the evidence that the dealership business was "abandoned", as suggested by the Appellant. Rather, Ford Credit arrived unannounced to conduct an audit in early January, 2010. The manager, Greg Duffy, sent the staff home on January 13. He remained on the premises both that day and the next, when the receivership order was obtained. He advised the Receiver that he had been involved in improprieties relating to cars, money or business arrangements on the premises for the past eight years and that the owner of the dealership had for years been residing in the Dominican Republic.

20 MNP did not reopen the dealership. It pressed Ford for its consent to a sale/assignment of the dealership agreement. On January 29, 2010, Ford advised that it would not consent, a position it consistently maintained thereafter. It advised by letter dated February 12, 2010 that it had no obligation under the dealership agreement to do business with the Receiver or its assignee. Ford Credit removed the vehicles upon which it had security. For the first time on February 24, 2010, Ford took the position that there had been a fundamental breach of the dealership agreement.

21 Ford argued the dealership agreement provided that a closure of the business for seven days constituted an event allowing for termination of the agreement (see clause 17(b)(3)(ii)). However, clause 17(b) of that agreement also provides that termination is only effective upon such an event occurring where Ford elects to terminate and gives the dealer 15 days written notice of its intention to do so. In this case, the first notice of termination given by Ford was six weeks after the Receiver was appointed, well after Ford had taken the position it would not cooperate with any assignment.

22 Ford argued this situation is akin to that faced by Yamauchi, J. in ***Canada Western Bank v. 702348 Alberta Ltd.***, 2009 ABQB 271, 472 A.R. 297, commonly known as the ***Guild*** decision, where he found fundamental breach of various leases of a commercial building in relation to a builder who went into receivership prior to the completion of construction. The Receiver did not have sufficient funding to complete construction and did not do so. Justice Yamauchi declared that two of the tenants had properly terminated their leases, finding fundamental breach had occurred because of the indefinite delay in construction. The Receiver had provided no evidence as to when a potential purchaser might recommence construction.

23 The chambers judge properly distinguished ***Guild*** by noting that there the Receiver decided not to remedy the lease breaches through completion of construction, whereas here Ford advised the Receiver early on that it would not consent to the Receiver's operation of the dealership. Here, in other words, it was the counter-party to the agreement who refused performance rather than the Receiver. He found that it was Ford which was blocking the breach from being remedied by refusing to cooperate with the reopening of the business by the Receiver.

24 In ***Guild***, it was not clear when, if ever, the buildings which were the subject of the leases in question would be completed (i.e., when the tenants would obtain the commercial benefit they were intended to receive under the leases). Here, Ford would obtain the commercial benefit under the dealership agreement immediately upon its consenting to the Receiver operating it or, alternately, to its sale to a party who could operate it. Ford's refusal to cooperate was the only reason the agreement could not be performed. It, as franchisee, was capable of carrying on the commercial purpose of the dealership agreement; it simply chose not to do so, which falls far short of meeting the test for fundamental breach established in ***Shelanu***.

25 In relation to the argument that Smith failed to properly supervise his employees with the result that the defalcation occurred, Ford tendered a Statement of Claim which maintained that a Welcome Ford manager misappropriated over $1.2 million by way of fraud. The chambers judge noted the lack of evidence that Smith was involved in the fraud or any convincing evidence of resulting damage to Ford's reputation. Needless to say, the manager in question was no longer employed by the time the sale was approved. There was no evidence before the chambers judge to support the suggestion that the manager's alleged prior activities would cast a pall over the operation of a Ford dealership in Fort Saskatchewan in the future.

26 The ultimate purchaser stood ready to reopen the dealership for business upon receiving court approval of the purchase. Any deficiencies in Smith's supervision disappeared with his removal from the business. Upon the reopening of the dealership, there is nothing to suggest that Ford would not be able to carry on the commercial purpose of the dealership agreement. It would not be deprived of the benefits it was intended to receive; indeed, the sooner the sale was effected, the sooner the flow of those benefits would resume.

27 The chambers judge concluded at para. 95 of the December decision: "I am comfortable that the proposed sale of the Welcome Ford dealership will substantially cure the breaches of the [dealership agreement], of which Ford Motor complains". The proposed sale cured the effect of those breaches in that it put a financially sound, experienced person in charge of the resumed operation in the form of a new business operating outside of the receivership. The chambers judge also expressly observed that Ford's rights and remedies will continue unchanged, including the right of first refusal and the right to take steps to terminate the dealership agreement if the purchaser defaults in the future.

28 The standard of review in relation to the chambers judge's findings of fact and application of facts to the law are subject to deference absent clear and palpable error. The application of deference is amplified when, as noted above, the judge is a case management judge whose decision is part of a series of decisions. His decision that no fundamental breach of the dealership agreement had occurred was reasonable and is entitled to our deference. Indeed, had we been required to consider the issue of correctness, we would have concluded his decision to be correct. The ultimate purchaser will be able to perform the dealers obligations under the agreement such that its commercial purpose will be effected. Ford will receive the benefit the parties intended it to receive when that agreement was created.

(B) How is s. 84.1 of the BIA to be interpreted?

29 The position at common law was always that if one party breached a condition (and not a mere warranty) in a contract, the other party to that contract had an election, either to treat the contract as continuing and insist on future performance, or to accept the repudiation and bring the contract to an end. In the latter case certain obligations survived the termination depending upon the construction of the contract.

30 The effect of s. 84.1 of the BIA is to override the common law unilateral right of the innocent party to the contract to accept the repudiation and end the contract. It has been designed to preserve the value of the estate as a whole, even if the contractual rights of some creditors, such as Ford in this case, are compromised. Therefore, even if Ford otherwise had the right to terminate the dealership agreement for breach of condition, and its assignment clause was not one which survived the termination, s. 84.1 nonetheless allows the trustee to apply to the Court for permission to assign the contract so long as the provisions of the statute are met.

31 Ford argues that the provisions of s. 84.1 which are prerequisite to granting permission to assign have not been met.

32 Section 84.1 reads in part:

> (1) On application by a trustee and on notice to every party to an agreement, a court may make an order assigning the rights and obligations of a bankrupt under the agreement to any person who is specified by the court and agrees to the assignment.
>
> ...
>
> (3) Subsection (1) does not apply in respect of rights and obligations that are not assignable by reason of their nature ...
>
> (4) In deciding whether to make the order, the court is to consider, among other things,
>
> > (a) whether the person to whom the rights and obligations are to be assigned is able to perform the obligations; and
> >
> > (b) whether it is appropriate to assign the rights and obligations to that person.

33 The Appellant did not argue, nor did the chambers judge find, that s. 84.1 expressly excludes auto dealership agreements from its operation. Indeed, the word "agreement" found in that section is wide enough to cover this type of agreement. The chambers judge correctly concluded, therefore, that he had jurisdiction under s. 84.1 to order the assignment (sale) in the proper circumstances.

34 Ford argued, rather, that those proper circumstances did not exist, as discussed below.

(i) *Is s. 84.1(3) to be interpreted without reference to s. 84.1(4)*?

35 Ford argued that whether the rights and obligations of an agreement are assignable "by reason of their nature" pursuant to s. 84.1(3) must be decided before, and independently of, any consideration under s. 84.1(4) as to whether the proposed assignee is capable of performing the obligations and it is appropriate to assign the rights and obligations. If so, it is irrelevant that the ultimate purchaser is an otherwise approved dealer and a proven performer. The issue of whether the nature of the agreement precludes its assignment would thus have to be resolved independently of any consideration of whether the agreement's commercial purpose would be achieved in the hands of the proposed assignee.

36 This interpretation is not supported by the literal words found in s. 84.1 which do not make a determination under s. 84.1(3) an independent precondition to a determination under s. 84.1(4). Legislative intent may be taken into account as an aide to interpretation only in the case of ambiguity in the words of the statute. Even if such an ambiguity existed here, and one is not apparent, Parliament's intent does not support Ford's interpretation. The chambers judge concluded that s. 84.1 should be interpreted in light of Parliament's intention that the provision be used to protect and enhance the assets of the estate of a bankrupt by permitting the sale/assignment of existing agreements to third parties for value: see Houlden, Morawetz and Sarra, *Bankruptcy and Insolvency Law of Canada,* 4th ed., looseleaf (Toronto: Carswell, 2009) vol. 2 at 3-499. He purported to interpret s. 84.1 in the context of its role as remedial legislation.

37 Prior to the coming into force of s. 84.1 in 2009, a trustee in bankruptcy could not assign (sell) a contract to a third party where the counter-party to that contract opposed the assignment. As a result, a bankrupt estate was vulnerable to losing the benefit of a valuable contract to the detriment of the estate and often to the detriment of third parties.

38 The estate of a bankrupt may include various forms of property. Sometimes the most valuable property in an estate will be the contractual rights possessed by the bankrupt as of the date of bankruptcy. Those rights may be embodied in, for example, a franchise agreement, a purchase agreement, a license agreement, a lease, a supply agreement or an auto dealership agreement.

39 The clear intent of Parliament in enacting s. 84.1 of the BIA was to address this vulnerability; it made a policy decision that a court ought to have the discretion to authorize a trustee to assign (sell) the rights and obligations of a bankrupt under such an agreement notwithstanding the objections of the counter-party.

40 A statutory provision analogous to s. 84.1 is that of s. 8(2) of the *Landlord's Rights on Bankruptcy Act*, R.S.A. 2000, c. L-5. It provides that, notwithstanding the legal effect of a provision in a lease purporting to terminate the lease upon the tenant becoming bankrupt, the trustee in bankruptcy may elect to retain the leased premises for some or all of the unexpired term of the lease. The trustee may then, upon payment of all overdue rent, assign the lease to a capable third party upon securing an order to that effect from the Court of Queen's Bench. The purpose of the legislation is to enable the trustee to maximize realization without putting the landlord in any worse position that it would have been under the lease before the bankruptcy: see ***Bank of Montreal v. Phoenix Rotary Equipment Ltd.***, 2007 ABQB 86 at para. 51, 72 Alta. L.R. (4th) 321.

41 Similarly, s. 84.1 of the BIA allows a court to approve the assignment (sale) of any agreement to obtain maximum benefit for creditors upon payment of any monetary breaches and upon concluding that the rights and remedies of the counter-party will be preserved.

42 Ford suggested the contrary, offering an extract from the Briefing Book placed before Parliament when it considered this amendment. The Briefing Book gives as a reason for the enactment of the language "not assignable by reason of its nature" (then subsection 3(d)) that it "is intended to provide flexibility to the court to review each agreement in light of the circumstances to determine whether or not it would be appropriate to allow the assignment". It further states, "[s]ubsection (4) provides the courts with legislative guidance as to when an agreement may be assigned. The guidance is limited to enable the court to exercise its discretion to address individual fact situations". These stated purposes are not, however, mutually exclusive.

43 Rather, to the extent that legislative intent is at all relevant, it is as described by the chambers judge as well as Justice Romaine of the Alberta Court of Queen's Bench in ***Alberta Health Services v. Networc Health Inc.***, 2010 ABQB 373 at para. 20, 28 Alta. L.R. (5th) 118:

> The BIA is remedial legislation. It is clear that it should be given "such fair, large and liberal construction and interpretation as best ensures the attainment of its objects": *Interpretation Act*, R.S.C., 1985, c. I-21 at section 12. In *Mercure v. A. Marquette & Fils Inc.*, [1977] 1 S.C.R. 547 at 556, the Supreme Court commented:
>
>> Before going on to another point it is perhaps not inappropriate to recall that the *Bankruptcy Act*, while not business legislation in the strict sense, clearly has its origins in the business world. Interpretation of it must take these origins into account. It concerns relations among businessmen, and to interpret it using an overly narrow, legalistic approach is to misinterpret it.

44 Ford has suggested no business reason to support its interpretation of s. 84.1(3) and (4). There is no apparent reason as to why appropriateness of the assignment or the capability of the proposed assignee would not be relevant to determining whether the rights and obligations are assignable by their nature. Rather, the opposite would appear to be true.

45 Therefore, I conclude that s. 84.1(3) is to be interpreted upon considering, among other things, the capacity of the proposed assignee and whether it is appropriate to assign the rights and obligations as set out in s. 84.1(4).

(ii)(a) *Are the rights and obligations established by the dealership agreement not assignable by reason of their nature because the estate will not benefit from the assignment?*

46 Ford argued that a court should not exercise its discretion under s. 84.1 to override the Appellant's clear contractual rights to withhold consent to the sale of the dealership in the absence of very clear evidence that the bankrupt estate will benefit: see ***Teragol Investments Ltd. v. Hurricane Hydrocarbons Ltd.***, 2005 ABQB 324 at para. 11, 382 A.R. 383; ***Kelly v. Watson*** (1921), 61 S.C.R. 482 at 490, [1921] 1 W.W.R. 958. However, unlike the Courts in these two cases, the chambers judge here was not asked to re-write or make the parties' contract by implying missing terms in the existing contract. All other rights and obligations under the assigned dealership agreement were to remain unchanged but for the change in the identity of the dealer from Welcome Ford to the ultimate purchaser.

47 Ford suggested that the chambers judge lacked clear evidence that the proposed assignment would benefit the estate. However, he described the supporting evidence at para. 52 of the December decision, which he found in the addendum to MNP's fourth report. Concluding that an assignment of the dealership agreement would benefit the creditors and enhance the value of the estate, the addendum confirmed that an *en bloc* sale of the assets of Welcome Ford which included the dealership agreement would result in full satisfaction of its indebtedness to BMO, would not prejudice Ford Credit's recovery on its secured collateral, and might make funds available for the unsecured creditors. Ford submitted that this evidence is nonetheless inadequate, criticizing MNP's method of marketing the land on which the dealership was located and the fact that the proposed sale would not, as a certainty, assure any recovery for the unsecured creditors.

48 This criticism falls far short of being persuasive given that the alternative, termination of the dealership agreement, would not generate sufficient funds to satisfy even the secured creditors. The chambers judge's conclusion that the proposed assignment (sale) would benefit the estate is therefore reasonable and deserving of deference.

(ii)(b) *Are the rights and obligations established by the dealership agreement not assignable by reason of their nature because they are personal?*

49 The dealership agreement expressly provides, among other things, that:

(a) Ford reserves the sole discretion to determine, from time to time, the numbers, locations and sizes of its franchised dealers;

(b) The dealership agreement is personal in nature and Ford expressly reserves the right to execute dealership agreements with individuals and others specifically selected and approved by it;

(c) Ford has the right to approve or decline to approve any transfer or change in voting control of a dealer based on the character, automotive experience, management, capital and other qualifications of the acquirer of the voting control, or the equity or beneficial interest, or the dealership business or its principal assets;

(d) Ford acknowledges a responsibility to ensure that dealers are owned and operated by qualified individuals of good reputation who are able to meet the requirements of the dealership agreement and the challenges of the marketplace;

(e) The dealership agreement may be terminated upon the happening of a number of events, including any transfer or attempted transfer by the dealer of any interest, right, privilege or obligation under the dealership agreement, or transfer by operation of law or otherwise of the principal assets of the dealer without the consent of Ford which "shall not be unreasonably withheld"; and

(f) Where there is a change in voting control of the principal owners of the dealership or a transfer of the dealership business or its principal capital assets, Ford's written approval is required; in declining any such approval (not to be unreasonably withheld), Ford has the right to consider the character, automotive experience, management capital and other qualifications of the proposed acquirer.

50 Ford argued that these provisions characterize the dealership agreement as "personal" to the parties who executed it, and therefore non-assignable notwithstanding the express provision permitting assignment with Ford's permission. The chambers judge concluded otherwise. The dealership agreement was not a "personal contract" which by its "nature" could not usefully be performed by another. Instead, he described it as "a rather standard commercial franchise which could be performed by virtually any business person and entity with some capital and experience in automotive retailing" (para. 73). As such, it did not fall within the s. 84.1(3) exception.

51 The dealership agreement is the same type of agreement as that found to be distinguishable from an employment or "personal service arrangement" by the Ontario Superior Court of Justice in ***Struik v. Dixie Lee Food Systems Ltd.***, [2006] O.J. No. 3269, 2006 CarswellOnt 4932 at para. 69.

52 Parties to a contract cannot insulate it from the effect of s. 84.1 simply by including a clause describing it as creating "personal" obligations where the contract is, in fact, a commercial one which could be performed by many others than the contracting parties.

53 Ford correctly pointed out that s. 84.1(3) does not speak of a personal contract as being the only type of contract which contains rights and obligations that are not assignable by their nature. It argued that the above terms of the dealership agreement evidence that it is not assignable by reason of its nature even if it is not a personal contract.

54 However, those express provisions - including those which describe it as personal in nature as well as Ford's reservation of the right to execute dealership agreements with those specifically selected and approved by it - are not sufficient to attract the application of s. 84.1(3) if other circumstances suggest the contrary. Otherwise, s. 84.1(4) would have no meaning, if a simple contractual provision to the effect that it was not "by reason of its nature" capable of unilateral assignment would be enough to make that so.

55 Ford accepted that the test to be applied to determine if the dealership agreement contains rights and obligations which by their nature are not assignable is that set out in ***Black Hawk Mining Inc. v. Manitoba (Provincial Assessor)***, 2002 MBCA 51 at paras. 79, 81-82, [2002] 7 W.W.R. 104. At para. 82 of ***Black Hawk Mining***, the Manitoba Court of Appeal cited ***Maloney v. Campbell*** (1897), 28 S.C.R. 228 at 233 as follows:

> Agreements are said to be personal in this sense when they are based on confidences, or considerations applicable to special personal characteristics, and so cannot be usefully performed to or by another.

56 Ford argued that it requires its dealers to have special personal characteristics, including specific requirements of knowledge, capital and experience. It led evidence that the value of a dealership is based primarily on the ability of the person operating it. However, the test for "non-assignability" found in ***Black Hawk Mining*** is not that it is important to Ford who would be performing the rights and obligations of Welcome Ford in the future, but rather whether those rights and obligations cannot be performed by the proposed assignee.

57 In any event, the evidence did not support the argument that it was important to Ford to have Smith and no other act as the Welcome Ford dealer. The chambers judge relied upon the fact that there was no evidence Ford had made any inquiry in respect of Smith, the owner of Welcome Ford, before signing the original dealership agreement or its most recent renewal in 2007, even to the extent of a credit check or confirmation as to his or the dealership's financial status from their bankers. Indeed, Ford did not know that Smith had relocated to the Dominican Republic well before the receivership order was granted; there was no evidence that it monitored him or stayed in regular contact with him throughout the period he controlled Welcome Ford.

58 Ford responded that it had no ability to review the qualifications of dealers when the 2007 renewal was signed; it was the dealers alone who had the obligation of signing onto the new form or continuing with the extant form of agreement. However, Ford was presumably responsible for the drafting of the original dealership agreement signed by Smith. If it failed to provide for ongoing proof of financial and other stability, that is an indicator that Ford did not consider those factors to be important.

59 The gist of the dealership agreement is that Ford agreed to provide automobiles to Welcome Ford, who in turn agreed to purchase and pay for them, and thereafter to promote their sale and provide after-market service. The operation of this agreement unfolded in a commercial manner. The evidence did not disclose anything which Smith alone could or did provide. The conclusions of the chambers judge that nothing in the agreement rendered it unassignable, either because it was said to be "personal" or not to be assigned without Ford's consent, are reasonable and should be accorded deference.

(iii) Should the dealership agreement not be assigned because of the capacity of the proposed assignee or because it is inappropriate to assign Welcome Ford's rights and obligations under s. 84.1(4)?

60 Section 84.1(4) of the BIA directs a judge, in determining if an order approving an assignment (sale) is to be made, to consider whether the party to whom the rights and obligations are proposed to be assigned can perform those obligations in the same manner as the original dealer. If not, court approval of the assignment should be withheld.

61 Ford argued the chambers judge did not have sufficient evidence to be able to conclude that the principal of the ultimate purchaser, the proposed assignee, would be able to perform the dealership obligations in the same fashion as had Smith. Notwithstanding the fact that principal was already successfully operating another Ford dealership in the area, Ford argued there was no evidence before the chambers judge as to i) the financial capability of its principal (even though he was proposing to make the purchase without the need of financing), ii) a business plan for operating multiple dealerships, or iii) his ability to satisfy Ford's criteria for owning and operating multiple dealerships.

62 Presumably some, if not all, of this evidence would have been internally available to Ford, yet it led no evidence to show any disability on the part of the ultimate purchaser. The chambers judge expressly relied on unchallenged affidavit evidence from another local Ford dealer to the effect that the proposed assignee had an excellent track record in terms of operating a profitable Ford dealership and had received many national awards from Ford over the years; the quality of its business premises met Ford's standards, unlike those which Ford had permitted Welcome Ford to operate. From this, the chambers judge inferred that the proposed assignee had both the capital and relevant experience in automotive retailing to enable him to operate the Welcome Ford dealership.

63 Ford went on to argue that the "good faith" obligation imposed on the parties under the dealership agreement takes into account the particular dealer. It is akin to the duty of good faith found in an employment contract: see ***Transamerica Life Canada Inc. v. ING Canada Inc.*** (2003), 68 O.R. (3d) 457 at para. 46 (C.A.). This means Ford would have a right of action for damages where a dealer breached the duty of fair dealing in the performance or enforcement of the dealership agreement: see Frank Zaid, *Canadian Franchise Guide*, looseleaf (Toronto: Thomson Reuters, 1992) at 2-142Z.36.

64 An assignment to any third party could conceivably increase the risk of that party not honouring its good faith obligation. However, the dealership agreement will be assigned only upon the court finding the appropriate prerequisite capability, with the resulting reduction in risk that the new dealer will be less honest than the old. Indeed, in this situation where the former dealership encountered a significant problem with employee misappropriation, these risks will likely be well reduced by the proposed assignment to an existing Ford dealer who presumably operates its other dealerships under a similar "good faith" obligation.

65 Section 84.1(4) of the BIA also directs a judge, in determining if an order approving an assignment (sale) should be made, to consider whether it is appropriate to assign the rights and obligations under the agreement.

66 The chambers judge assumed, for the purposes of his decision, that "the consent of Ford Motor to the proposed assignee is required", and that the unreasonable failure to provide that consent is a consideration in determining that it is appropriate to nonetheless assign (sell) the agreement. There is nothing in s. 84.1 which expressly requires that the consent of the contracting party be canvassed as a prerequisite to the application for approval of an assignment of an agreement. The chambers judge did not find that such canvassing was required; he simply assumed it was for the purpose of his analysis. There is no reason to interpret the section as containing such an implicit prerequisite. Rather, an unreasonable withholding of consent is simply one factor to consider in determining whether it is otherwise appropriate to assign the agreement pursuant to s. 84.1(4).

67 The chambers judge found that Ford would never consent to the assignment of this dealership agreement because it would not consent to the assignment of any dealership agreement where a dealership had ceased operation. In withholding consent, Ford had not taken into account the merits of the proposed assignee. The chambers judge therefore concluded that Ford had unreasonably withheld its consent.

68 Ford argued that a wider investigation needed to be undertaken when determining the appropriateness of assigning the dealership agreement than simply one of its refusal to consent. This investigation would canvass the terms of the agreement, the departing dealer's misconduct, the Receiver's failure to continue to operate the dealership pending approval of the proposed sale, Ford's standard criteria when considering a request to assign a dealership agreement outside of an insolvency context, and the results of an analysis it had done subsequent to the closure of Welcome Ford which concluded that future direct representation of the Ford brand was not warranted in the Fort Saskatchewan area.

69 While the chambers judge described his investigation into these issues as "limited", he did consider factors in addition to Ford's unreasonable refusal to consent. Those other factors were the uncontradicted evidence that the ultimate purchaser was up to the job, his conclusion that the proposed assignment would substantially cure the breaches which Ford argued were fundamental, and that all of Ford's rights and remedies under the dealership agreement would be preserved against the proposed assignee. There was no obligation upon the chambers judge to expressly address each additional factor which Ford argued should bear on his determination. His approval of the assignment conveys the results of his assessment of those arguments.

70 Ford argued that the chambers judge should not have considered its failure to consent to any assignment as a factor at all; to do so would amount to a limitation on access to justice in a new area in which it wished to test the effects of s. 84.1 of the BIA. Even if that is so today, it does not counteract the other reasons given by the chambers judge for concluding that it was appropriate to approve the assignment.

71 In summary, the chambers judge concluded the dealership agreement was assignable by reason of its nature based on an assessment of evidence showing the proposed assignee would be able to discharge the dealer's obligations thereunder and upon concluding that it was appropriate to assign the agreement based on evidence that Ford unreasonably withheld its consent, that the effect of earlier breaches of the agreement would be remedied through its assignment, and that Ford's rights and remedies under the agreement would carry on unchanged. That decision was reasonable; deference should be accorded to it.

CONCLUSION

72 The appeal is dismissed.

COSTS

73 The parties advised they had agreed each should bear their own costs of this appeal given that it involved the interpretation of a hitherto uninterpreted statutory provision. For that reason, the normal rule that the victor is entitled to costs will not be followed. Each party is to bear its own costs of this appeal.

K.G. RITTER J.A.
P.W.L. MARTIN J.A.
M.B. BIELBY J.A.

Dundee Oil and Gas Ltd. (Re), [2018] O.J. No. 3277

Ontario Judgments

Ontario Superior Court of Justice

Commercial List - Toronto, Ontario

S.F. Dunphy J.

Heard: June 11, 2018.

Judgment: June 13, 2018.

Court File No.: CV-18-591908-00CL

[2018] O.J. No. 3277 | 2018 ONSC 3678 | 293 A.C.W.S. (3d) 475 | 61 C.B.R. (6th) 68 | 2018 CarswellOnt 9960

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 Dundee Oil & Gas Limited

(40 paras.)

Counsel

E. Patrick Shea and B. Arnold for the Applicants.

Grant Moffat and Rachel Bengino, for the Monitor FTI Consulting Canada Inc.

J. Wallace for purchaser Lagasco Inc.

S. Kromkamp and B. McPherson for HMQ in right of Ontario.

Aubrey E. Kauffman for the National Bank of Canada.

M.P. Gottlieb for Canadian Overseas Petroleum Limited.

REASONS FOR DECISION

S.F. DUNPHY J.

1 Dundee Oil and Gas Limited brought an application, supported by the Monitor, seeking approval of a sale of substantially all of its assets before me on May 23, 2018. I approved the proposed sale subject to requiring further evidence regarding the requested assignment of executory contracts under s. 11.3 of the *Companies' Creditors Arrangement Act* on June 11, 2018.

2 The matter came back before me on June 11, 2018 where, based upon the new evidence filed, I approved the transaction including the assignment of the executory contracts with reasons to follow. These are those reasons.

Background facts

3 Dundee entered into an Asset Purchase Agreement subject to court approval dated April 4, 2018. The sale was the result of a long process that began in August 2017 when Dundee was operating under the protection of the proposal provisions of the *Bankruptcy and Insolvency Act*. Those proceedings were continued under the CCAA on February 13, 2018.

4 Dundee's assets consist primarily of a large number of petroleum and natural gas leases as well as associated equipment, gathering pipelines, etc. Many of the assets are in fact leased or are otherwise the subject of contractual arrangements between Dundee and the owner of the affected land. Accordingly, a significant aspect of the proposed sale transaction was a requirement that an assignment of the underlying contracts be accomplished by an order pursuant to s. 11.3 of the CCAA.

5 On May 23, 2018 I indicated to the parties that I was satisfied with the necessity and advisability of ordering the requested relief and the process leading up to it save and except one aspect. In approving an assignment using the authority vested in me by s. 11.3 of the CCAA, I am required to inquire into a number of matters about which I found the record before me that day to be deficient. One landowner, Mr. Whittle, had made a formal objection and availed himself of the opportunity to express his concerns by telephone. He raised a number of objections to what he perceived to be concerns regarding the operational stability of the purchaser and their ability to see to eventual remediation obligations.

6 During the course of the hearing, the Applicant indicated that the purchaser was prepared to proceed without an order compelling the assignment of agreements between Dundee and Mr. Whittle. The Applicant's position was that the form of agreements used in the case of Mr. Whittle's contracts at least required no consent for a valid assignment. The Purchaser was prepared to run the risk of that assessment proving accurate in Mr. Whittle's case.

7 In the result, I adjourned the hearing until June 11, 2018 in order to grant the applicant additional time to address the concerns raised by me regarding s. 11.3 of the CCAA. I indicated that there were no other issues.

8 The specific concerns raised by me were these:

a. The operation of a natural resource extraction business such as an oil and gas business is one that entails a degree of environmental risk that, in the event of insolvency of the lessee/contract holder may visit the remediation or well-capping costs upon the landowner, a factor that makes the capacity and ability of the proposed assignee to manage those responsibilities a matter of concern when assessing the suitability of the proposed assignee; and

b. The affidavit material at the motion provided no solid evidence of the expected financial stability or durability of the purchaser post-closing, a rather critical factor to assess in considering the suitability of a proposed assignee.

9 Three things happened during the intervening delay, two planned one unexpected.

10 Firstly, the Monitor arranged to notify the landowners of the delay. No further objections were received from that front. Mr. Whittle maintained his objection despite the Applicant's concession that it was not seeking to compel assignment of his agreements.

11 Secondly, the Applicant filed a Supplementary Affidavit of Jane Lowrie, President and Chief Executive Officer of Lagasco Inc, the purchaser sworn June 5, 2018. This affidavit provided further details regarding the financial status of the purchaser.

12 Lastly, one of the "runner-up" bidders (Canadian Overseas Petroleum Limited) sent a letter to the Monitor on June 7, 2018 which letter COPL decided to send directly to the court on June 8, 2018 when the Monitor did not agree to bring the letter to my attention directly.

13 This intervention generated a flurry of reaction or overreaction, depending upon your point of view. It was, in the final analysis, a tempest in a teacup.

14 The Applicant and National Bank (who strongly supports the sale and, despite the sale, will end up with a significant shortfall on its secured claim) were understandably taken aback by a last-second threat to a transaction they have worked very hard to bring to the threshold of completion and that, from their perspective at least, is clearly the best option available. They asked me not to consider the submissions of a mere "bitter bidder".

15 They needn't have had so little faith in the editorial judgment of the court. COPL had experienced counsel who was well aware of the stiff currents flowing against any attempt of an unsuccessful bidder to gain standing to upset a transaction. There was no request for standing. The principal message of the communication was an opportunistic one perhaps, but not unfair. In light of the issues raised on May 23, 2018, COPL wanted to remind the Monitor and eventually the court that it remains ready willing and able to move forward with a transaction should Lagasco drop the ball. Of course, COPL did not resist ensuring that a few helpful bits of analysis/argument that might serve to persuade the court to think about moving in that direction also managed to find their way into the communication. It was not an attempt to introduce fresh evidence through the back door.

16 As I remarked during the hearing, I did not fall off the turnip truck yesterday. The motivation behind the communication was not cloaked nor was its simple object.

17 A few take-away admonitions from this:

a. Communications directly with the judge are to be discouraged generally;

b. Where necessary, such communications should be copied to the service list generally absent some very compelling reason not to do so; but

18 I would have preferred that this course of conduct had been followed here. The Monitor was copied and the integrity of the process was in no way compromised.

19 The substantive question before me was whether I ought to approve the provisions of the requested approval and vesting order that would compel the assignment of certain executory contracts under s. 11.3 of the CCAA.

20 Section 11.3 of the CCAA authorizes the court to assign "the rights and obligations of the company" to an agreement to any person specified in the court order that is willing to accept the assignment. Post-filing contracts, eligible financial contracts and collective agreements may not be assigned in this fashion.

21 There was no issue in this case with the technical aspects of the case. Proper notice was given. No prohibited categories of contracts were proposed to be assigned. The terms of the proposed assignment were designed to ensure the payment of cure costs would be made. A procedure for resolving any disputes about cure costs was designed to avoid compromising the rights of affected parties.

22 The issue to be decided was whether this was an appropriate case for me to exercise my jurisdiction to make the order under s. 11.3. Section 11.3 does not provide an exhaustive code of the factors for me to consider. Rather, s. 11.3(3) lists three factors that, among others, I am to consider:

(a) whether the monitor approved the proposed assignment;

(b) whether the person to whom the rights and obligations are to be assigned would be able to perform the obligations; and

(c) whether it would be appropriate to assign the rights and obligations to that person.

23 In the present case, the Monitor has approved the proposed assignments and has made detailed and thoughtful submissions to me outlining the basis of that approval. The concerns expressed by me on May 23, 2018 did not fall on deaf ears.

24 The purchaser Lagasco is largely a shell company for the time being. It will own the business being purchased.

The evidence before me indicates that substantially all of the purchase price is to be debt financed -- partly through financing secured by the equipment to be purchased and party through a credit facility. On day one there will be little to no equity in the purchaser and the significant leverage will have to be serviced entirely from cash flow.

25 Taken in isolation, this factor raised grave concerns in my mind as to whether the assignee would be able to perform the obligations or whether, in light of the potential fragility of the assignee, it would be appropriate to compel the contract counterparties to accept the assignee.

26 I still have those concerns. I think it helpful that I should elaborate somewhat on what the concerns are and how I have resolved them. The Monitor's dispassionate and frank analysis of the issues has been very helpful in this process.

27 Section 11.3 of the CCAA is an extraordinary power. It permits the court to require counterparties to an executory contract to accept future performance from somebody they never agreed to deal with. But for s. 11.3 of the CCAA, a counterparty in the unfortunate position of having a bankrupt or insolvent counterpart might at least console themselves with the thought of soon recovering their freedom to deal with the subject-matter of the contract. Unlike creditors, the counterparty subjected to a non-consensual assignment will be required to deal with the credit-risk of an assignee post-insolvency and potentially for a long time. Creditors, on the other hand, will generally be in a position to take their lumps and turn the page.

28 Of course, insolvency is not always a catastrophe for such counterparties. Sometimes it is a godsend. Assets locked into long-term contracts at advantageous prices may be freed up to allow the counterparty to re-price to current market. In such cases, the creditors are at risk of seeing the debtor lose critical assets while the counterparty receives an unexpected windfall. The business and value of the debtor's assets may evaporate in the process -- be it from one large contract lost or many smaller ones.

29 Bankruptcy and insolvency always involves a balancing of a number of such competing interests. Creditors, contract counterparties - all of these have rights arising under agreements with the debtor that are either actually compromised or at risk of being compromised by insolvency. The CCAA and BIA regimes are predicated on facilitating a pragmatic approach to minimize the damage arising from insolvency more than they are concerned to advance the interests of one stakeholder over another.

30 It seems to me that a fundamental condition precedent to requiring a contract counterpart to be locked into an involuntary assignment post-insolvency is that the court sanctioning the assignment is able to conclude that the assignee will, in the words of s. 11.3(3)(b) of the CCAA, "be able to perform the obligations". This does not imply iron-clad guarantees. It does not give license to the counterparty to demand the receipt of financial covenants or assurances that it did not previously enjoy under the contract it originally negotiated with the debtor.

31 A proposed purchaser starting life with close to 100% leverage gives this judge a considerable degree of heartburn when it comes to answering the question of whether the assignee is a person who will be able to perform the obligations. That concern is amplified when one adds the prospect of landowners being made liable for environmental remediation caused by lessees and others on their land.

32 So, if that is my concern, by what process have I allayed it?

33 Firstly, the financial information before me is that cash flow from these operations has been quite solid. Dundee's insolvency has not been a result of operating losses.

34 Secondly, while any projection of future business results will always be subject to a number of contingencies and imponderables outside of the control of the parties, the forecast reserves prepared by Deloitte in this case have been prepared under NI 51.01 which means at the very least that they have been prepared to reviewable standards of reasonableness. The forecasts, such as they are, justify the inference that there is a *reasonable basis* to conclude that the cash flow from the acquired assets will sustain operations and the acquisition debt. It will be a while before an equity cushion will be built though.

35 Thirdly, the purchaser has a plan to reduce G&A and operating costs to provide a further margin of safety and a level of institutional experience to make such a plan credible.

36 Fourthly, the environmental risk is mitigated somewhat by the fact that Ontario's regulatory model operates on a "pay as you play" basis requiring the building of reserves to handle capping costs as wells move past their expected lives. Dundee has had no trouble in the past funding capping expenses from operations and these expenses are accounted for in the cash flow forecasts used.

37 Finally, the MNR has agreed to a voluntary assignment of its leases (off-shore) while no on-shore landowners have seen fit to object to the proposed assignments despite quite adequate notice being given.

38 I must also be mindful that contract counterparties are not expected to *improve* their situation by reason of an assignment. A counterpart to an executory contract that is subject to involuntary assignment under s. 11.3 of the CCAA has managed to find itself contractually bound to an insolvent debtor notwithstanding whatever contractual safeguards were negotiated to avoid that outcome. The debtor is now insolvent. The desire to ensure the assignee is a reasonably fit and proper one should not morph into an exercise in patching up contracts previously negotiated by requiring financial covenants and safeguards never before required.

39 In all the circumstances, I was led to the conclusion that it would be appropriate to assign Dundee's rights and obligations to the purchaser and that the purchaser is someone who will be able to perform the obligations assigned. I have carefully reviewed the proposed order and am satisfied that the method of ascertaining cure costs and, if needs be, resolving disputes arising about the quantum satisfies the requirements of s. 11.3(4) and s. 11.3(3)(c). There is a fair process to resolve disputes about quantum should they arise.

40 In the result, I approved the transaction and the form of Approval and Vesting Order presented to me subject to minor amendments made at the hearing.

S.F. DUNPHY J.

U.S. Steel Canada Inc. (Re), [2014] O.J. No. 5547

Ontario Judgments

Ontario Superior Court of Justice

H.J. Wilton-Siegel J.

Heard: October 8, 2014.

Judgment: October 22, 2014.

Court File No. CV-14-10695-00CL

[2014] O.J. No. 5547 | 2014 ONSC 6145 | 20 C.B.R. (6th) 116 | 247 A.C.W.S. (3d) 266 | 2014 CarswellOnt 16465

IN THE MATTER OF the Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36 as Amended AND IN THE MATTER OF a Proposed Plan of Compromise or Arrangement With Respect to U.S. Steel Canada Inc.

(48 paras.)

Case Summary

Bankruptcy and insolvency law — Companies' Creditors Arrangement Act (CCAA) matters — Compromises and arrangements — Claims — Priority — Sanction by court — Motion by applicant, who had been granted protection under Companies' Creditors Arrangement Act, to vary Initial Order allowed — Appropriate to approve debtor-in-possession loan and lender's charge to ensure stable continuing operations — Granting super-priority to Administration and Director's Charges granted in Initial Order was essential to success of any possible restructuring — Proposed key employee retention programme was approved — Currently unrepresented beneficiaries were granted representation — Extension of stay provisions in Initial Order was granted.

Motion by the applicant, who had been granted protection under the Companies' Creditors Arrangement Act, to vary the Initial Order. The applicant sought approval of a debtor-in-possession loan facility between it and a subsidiary of its largest creditor to assist its cash flow. A condition precedent to funding under the loan was an order granting the lender priority over all encumbrances. The loan was supported by the monitor and was not opposed by any of the major stakeholders. The applicant also sought to amend the Initial Order to provide that the Administration and Director's Charges granted ranked ahead of all other Encumbrances except the loan charge. It sought approval of its proposed key employee retention programme. The applicant's secured creditor and the monitor supported the programme. The applicant proposed the appointment of six representatives and representative counsel to represent the interests of beneficiaries who were currently unrepresented. It sought an extension of the stay provisions in the Initial Order.
HELD: Application allowed.

The existence of a financing facility was of critical importance to the applicant to ensure stable continuing operations. The loan would assist and enhance the restructuring process. It was appropriate to approve the loan and the lender's charge. Granting super-priority to the Administration and Director's Charges was essential to the success of any possible restructuring. The continued employment of the employees to whom the retention programme applied was important for the stability of the business. The programme was approved. The representatives were approved as the beneficiaries were an important stakeholder group and deserved meaningful representation. An extension of the stay provisions of the Initial Order was granted to provide stability. The applicant was acting in good faith and with due diligence to facilitate the restructuring process.

Statutes, Regulations and Rules Cited:

Bankruptcy and Insolvency Act, R.S.C. 1985, c. B-3,

Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36, s. 11, s. 11.01(2), s. 11.02(3), s. 11.2, s. 11.2(4), s. 11.51, s. 11.52

Ontario Regulation 99/06,

Pension Benefits Act, R.S.O. 1990, c. P.8,

Rules of Civil Procedure, Rule 10.01, Rule 12.07

Counsel

R. Paul Steep, Jamey Gage and Heather Meredith, for the Applicant.

Kevin Zych, for the Monitor.

Michael Barrack, Robert Thornton and Grant Moffat, for United States Steel Corporation and the proposed DIP Lender.

Gale Rubenstein, Robert J. Chadwick and Logan Willis, for Her Majesty the Queen in Right of Ontario and the Superintendent of Financial Services (Ontario).

Ken Rosenberg and Lily Harmer, for the United Steelworkers International Union and the United Steelworkers Union, Local 8782.

Sharon L.C. White, for the United Steelworkers Union, Local 1005.

Shayne Kukulowicz and *Larry Ellis*, for the City of Hamilton.

Steve Weisz and Arjo Shalviri, for Caterpillar Financial Services Limited.

S. Michael Citak, for various trade creditors.

Kathryn Esaw and Patrick Corney, for the Independent Electricity System Operator.

Andrew Hatnay, for certain retirees and for the proposed representative counsel.

ENDORSEMENT

H.J. WILTON-SIEGEL J.

1 U.S. Steel Canada Inc. (the "Applicant") brought an application for protection under the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36 (the "CCAA") on September 16, 2014, and was granted the requested relief pursuant to an initial order of Morawetz R.S.J. dated September 16, 2014 (the "Initial Order"). The Initial Order contemplated that any interested party, including the Applicant and the Monitor, could apply to this court to vary or amend the Initial Order at a comeback motion scheduled for October 6, 2014 (the "Comeback Motion").

arrangement or completion of a sale, upon an outside date, or upon earlier termination of employment without cause.

26 The maximum amount payable under the KERP is $2,570,378. The Applicant proposes to pay such amount to the Monitor to be held in trust pending payment.

27 The Court's jurisdiction to authorize the KERP is found in its general power under s. 11 of the CCAA to make such order as it sees fit in a proceeding under the CCAA. The following factors identified in case law support approval of the KERP in the present circumstances.

28 First, the evidence supports the conclusion that the continued employment of the employees to whom the KERP applies is important for the stability of the business and to assist in the marketing process. The evidence is that these employees perform important roles in the business and cannot easily be replaced. In addition, certain of the employees have performed a central role in the proceedings under the CCAA and the restructuring process to date.

29 Second, the Applicant advises that the employees identified for the KERP have lengthy histories of employment with the Applicant and specialized knowledge that cannot be replaced by the Applicant given the degree of integration between the Applicant and USS. The evidence strongly suggests that, if the employees were to depart the Applicant, it would be very difficult, if not impossible, to have adequate replacements in view of the Applicant's current circumstances.

30 Third, there is little doubt that, in the present circumstances and, in particular, given the uncertainty surrounding a significant portion of the Applicant's operations, the employees to be covered by the KERP would likely consider other employment options if the KERP were not approved

31 Fourth, the KERP was developed through a consultative process involving the Applicant's management, the Applicant's board of directors, USS, the Monitor and the CRO. The Applicant's board of directors, including the independent directors, supports the KERP. The business judgment of the board of directors is an important consideration in approving a proposed KERP: see *Timminco Ltd. (Re)*, 2012 ONSC 506 at para.73, [2012] O.J. No. 472. In addition, USS, the only secured creditor of the Applicant, supports the KERP.

32 Fifth, both the Monitor and the CRO support the KERP. In particular, the Monitor's judgment in this matter is an important consideration. The Monitor has advised in its First Report that it is satisfied that each of the employees covered by the KERP is critical to the Applicant's strategic direction and day-to-day operations and management. It has also advised that the amount and terms of the proposed KERP are reasonable and appropriate in the circumstances and in the Monitor's experience in other CCAA proceedings.

33 Sixth, the terms of the KERP, as described above, are effectively payable upon completion of the restructuring process.

Appointment of Representative Counsel for the Non-USW Active and Retiree Beneficiaries

34 The beneficiaries entitled to benefits under the Hamilton Salaried Pension Plan, the LEW Salaried Pension Plan, the LEW Pickling Facility Plan who are not represented by the USW, the Legacy Pension Plan, the Steinman Plan, the Opportunity GRRSP, RBC's and RA's who are not represented by the USW and beneficiaries entitled to OEPB's who are not represented by the USW (collectively, the "Non-USW Active and Retiree Beneficiaries") do not currently have representation in these proceedings. The defined terms in this section have the meanings ascribed thereto in the affidavit of Michael A. McQuade referred to in the Initial Order.

35 The Applicant proposes the appointment of six representatives and representative counsel to represent the interests of the Non-USW Active and Retiree Beneficiaries. The Court has authority to make such an order under

Nortel Networks Corp. (Re), [2010] O.J. No. 1112

Ontario Judgments

Ontario Superior Court of Justice

Commercial List

G.B. Morawetz J.

Heard: March 3, 2010.

Judgment: March 18, 2010.

Court File No. 09-CL-7950

[2010] O.J. No. 1112 | 2010 ONSC 1438 | 186 A.C.W.S. (3d) 320 | 186 A.C.W.S. (3d) 394 | 2010 CarswellOnt 1615

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

(30 paras.)

Counsel

Derrick Tay, Jennifer Stam and Suzanne Wood, for the Applicants.

Barry Wadsworth, for the CAW-Canada.

Arthur O. Jacques, for the NCCE.

M. Starnino, for the Superintendent of Financial Services as Administrator of the PBGF.

Kevin Zych, for the Internal Nortel Noteholders.

Sean Dunphy, for Genband (CVAS Purchaser).

Alex MacFarlane, for the Official Committee.

Robin B. Schwill, for Nortel Networks UK Limited (In Administration).

Jay Carfagnini and Christopher Armstrong, for Ernst & Young Inc., Monitor.

Adam Hirsh, for the Board of Directors of NNL and NNC.

ENDORSEMENT

G.B. MORAWETZ J.

1 On March 8, 2010, the record was endorsed:

> "Motion granted. Nortel Special Incentive Plan approved as is related charge. Reserve Fund approved.
>
> Adjustments to 2009 KEIP/KERP approved.
>
> Sealing Order granted in respect of Supplemental Report of Monitor and Appendices.
>
> Written reasons will follow."

2 These are those reasons.

3 This hearing was conducted by way of videoconference, with a parallel motion being heard in the United States Bankruptcy Court with His Honor Judge Gross. This hearing was conducted in accordance with the provisions of the Cross-Border Protocol, previously approved by both the U.S. Court and by this court.

4 The Applicants moved for approval of the Nortel Special Incentive Plan (the "Nortel Special Incentive Plan"), as well as for an order granting a charge (the "Nortel Special Incentive Plan Charge") in favour of the participants in the Nortel Special Incentive Plan ("Plan Participants") to secure payment of the amounts that have been determined to be payable to Plan Participants, subject to their continued employment until the applicable payment date. The proposed Nortel Special Incentive Plan Charge is not to exceed an aggregate amount of CDN $20 million. The Applicants also requested that the Nortel Special Incentive Plan Charge apply in these proceedings and any subsequent bankruptcy or receivership proceeding.

5 The Applicants also sought authorization to make additional payments which may be made to ongoing employees of the Applicants, in the sole discretion of the Applicants (and with the consent of the Monitor), which payments shall total no more than $3 million.

6 Finally, the Applicants sought approval of the third KEIP/KERP payment pursuant to the 2009 programmes to certain individuals, subject to similar relief being granted in the U.S. Court.

7 In addition, the Monitor filed a Confidential Supplement to the Thirty-Seventh Report including appendices and the Applicants' requested that these documents be sealed.

8 In support of the motion, the Applicants filed the affidavit of Elena King, sworn February 11, 2010 and the Monitor filed its Thirty-Seventh Report.

9 A number of objections were raised in the U.S. proceedings and were resolved. The objections were not filed in this court and, in my view, no further comment is required.

10 The motion was not opposed. Counsel to the Former Employees and Disabled Employees as well as counsel to the CAW did, however, request that my ruling on this motion be deferred until such time as the motion to approve a Settlement Agreement in respect of certain issues relating to the Applicants' Registered Pension Plans, certain employee benefits for pensioners and LTD beneficiaries and certain employment-related issues had been heard. Argument on the Settlement Agreement motion was concluded on March 5, 2010.

11 The Nortel Special Incentive Plan addresses compensation issues relating to Nortel employees whose function is to assist in matters relating to the disposition of assets, transitional matters and other matters, designed to enhance the asset pool, which will ultimately be available for distribution to creditors. In this respect, this motion is very different from the motion to approve the Settlement Agreement. There is, in my view, no linkage between the two motions. Although the disposition of the motion to approve the Settlement Agreement has yet to be rendered, I saw no reason to delay the disposition of the motion in respect of the Nortel Special Incentive Plan.

12 The Nortel Special Incentive Plan was developed by Nortel in conjunction with Mercer (U.S.) Inc., the Monitor and a number of its significant stakeholders to provide incentive to the many employees in Nortel Business Services ("NBS") or the corporate group ("Corporate Group") who are not being transitioned as part of the sales transactions and who will eventually work themselves out of a job.

13 Counsel to the Applicants submits that the goal of the Nortel Special Incentive Plan is to retain the Plan Participants by providing them with a level of certainty and an incentive to continue to help Nortel accomplish its goals in these proceedings.

14 Counsel further submits that in designing the Nortel Special Incentive Plan, Plan Participants are selected in accordance with criteria approved by the boards in consultation with the Unsecured Creditors' Committee of NNI (the "Committee") and the Ad Hoc Bondholders Group (the "Bondholders Committee") and the Monitor.

15 The "Plan Period" under the Nortel Special Incentive Plan extends through December 31, 2011. There are a total of 1,475 Plan Participants including 455 employees of the Applicants.

16 The payout under the Nortel Special Incentive Plan will be approximately U.S.$93 million. However, counsel to the Applicants stated that approximately 88% of that cost will be borne by the various purchasers under the sales transactions.

17 The Nortel Special Incentive Plan also contemplates a U.S.$20 million discretionary pool. However, the Applicants are not seeking authorization to make any payments out of the discretionary pool and, to the extent that any future payments will be made by the Applicants, the Applicants will seek further court approval.

18 Counsel to the Applicants also advised that modifications to the Nortel Special Incentive Plan or additional payments under the Nortel Special Incentive Plan may be necessary where the Applicants and the Monitor determine that, among other things, the terms of a Plan Participant's employment should be modified or new participants should be added, but these modifications should not result in the Nortel Special Incentive Plan exceeding its current estimated cost.

19 The Applicants also seek the creation of the Nortel Special Incentive Plan Charge. Counsel submits that the creation of the charge will provide similar levels of assurance to Plan Participants in Canada as compared to the U.S.

20 With respect to the third KEIP/KERP payment, counsel to the Applicants referenced the March 6, 2009 order, which approved the Key Executive Incentive Plan ("KEIP") and a Key Employee Retention Plan ("KERP"). Under these programmes, there were three payments to be made based on the achievement of certain milestones. The third payment was to be made on completion of the Plan of Arrangement and which was scheduled to be made on June 30, 2010.

21 Counsel to the Applicants submitted that Nortel is reaching a critical point in its global restructuring due to the efforts of the participants for which relief regarding the immediate payment of the third KEIP/KERP is sought. Under the 2009 programme, which contemplated a reorganization of Nortel rather than the sale of its businesses, the trigger for payment to certain employees participating in the 2009 KEIP has not technically been achieved. Similarly, the timing for payment under the 2009 KERP has meant that those employees who remain in NBS or the Corporate Group have not received a third payment under the 2009 KERP while others who have been or will be terminated as part of the asset sales have received earlier payment or will receive payment upon closing of the sale. Counsel to the Applicants submits that this has resulted in an inequity for those employees who have agreed to stay on to the completion of the proceedings and consequently the Applicants are requesting that the court authorize immediate payment of the third KEIP/KERP payment for those employees identified in a Confidential Appendix to the Supplemental Report who are NBS and Corporate Group employees.

22 The affidavit of Ms. King is very detailed. She concludes that throughout the proceedings, the Applicants have been focused on ensuring the best outcome for the greatest number of people including not only creditors, but employees, customers and other stakeholders. Ms. King further states that this work has been done in conjunction with the Applicants' advisors, the Monitor, the Joint Administrators, the Committee, the Bondholders Committee, Representative Counsel and other stakeholders resulting in almost all matters being concluded on a consensual basis.

23 Ms. King further states that the breadth and complexity of the work today and the remaining work for Nortel is significant in scope and requires specialized employees to bring the process to a successful conclusion. She is of the view that the employees being offered participation in the Nortel Special Incentive Plan were instrumental in the work completed to date and are essential to completing the remaining tasks. She is of the view that the creation of the Nortel Special Incentive Plan Charge provides much needed certainty regarding the ultimate receipt of the payments provided for under the Nortel Special Incentive Plan.

24 Further, Ms. King states that the loss of the Plan Participants at this time would likely result in significant delays in achieving Nortel's objectives to maximize value to its creditor constituencies.

25 The Monitor also provided a detailed review of the Nortel Special Incentive Plan. The Monitor is of the view that the commitment and retention of the remaining employees will be essential to the execution of obligations pursuant to the transitional service agreements, the completion of the Applicants' restructuring and the completion of the Plan of Arrangement.

26 The Monitor further states that it has reviewed the details of the proposed plan as well as Mercer's analysis and is of the view that the proposed Nortel Special Incentive Plan provides reasonable compensation under the current circumstances.

27 The Monitor recommends that the Nortel Special Incentive Plan be approved. The Monitor also supports the Applicants' request for the establishment of the Nortel Special Incentive Plan Charge as well as the $3 million Reserve Fund. Finally, the Monitor recommends the revised payment date for the third KEIP/KERP payment for the eligible NBS and Corporate Group employees in respect of the 2009 KERP and third milestone of the 2009 KEIP.

28 I have been satisfied that, in the circumstances of this case, it is reasonable for the Applicants to provide an incentive plan to certain employees. In my view, the terms are fair, reasonable and equitable. I am also satisfied that the creation of the Nortel Special Incentive Charge is appropriate in the circumstances, as is the request to make additional payments to certain employees (with the consent of the Monitor) out of the proposed Reserve Fund and further that it is also reasonable in the circumstances to implement the proposed revision to the 2009 KEIP/KERP programme.

29 Finally, I am satisfied that the Confidential Supplement to the Thirty-Seventh Report as well as the Confidential Appendices contain sensitive commercial information and personal information, the dissemination of which could be harmful to certain parties. Having considered the test set out *Sierra Club*, I am of the view that it is appropriate to grant a Sealing Order with respect to these documents.

30 An order shall issue to give effect to the foregoing.

G.B. MORAWETZ J.

Wage Earner Protection Program Act, S.C. 2005, c. 47, s. 1, s. 2

Canada Statutes

S.C. 2005, c. 47, s. 1, s. 2 | L.C. 2005, ch. 47, art. 1, art. 2

[Unofficial Chapter No. W-0.8]

Canada Statutes > Wage Earner Protection Program Act [ss. 1-42] > INTERPRETATION [s. 2]

INTERPRETATION

SECTION 2.

Definitions
2 (1) The following definitions apply in this Act.

Board means the Canada Industrial Relations Board established by section 9 of the *Canada Labour Code*. (*Conseil*)

eligible wages means

(a) wages other than termination pay and severance pay that were earned during the longer of the following periods:

(i) the six-month period ending on the date of the bankruptcy or the first day on which there was a receiver in relation to the former employer,

(ii) the period beginning on the day that is six months before one of the following days and ending on the date of the bankruptcy or the first day on which there was a receiver in relation to the former employer:

(A) the day on which a proposal is filed by or in respect of the employer under Division I of Part III of the *Bankruptcy and Insolvency Act* or, if a notice of intention to make a proposal is filed by or in respect of the employer under that Division, the day on which the notice of intention is filed,

(B) the day on which the most recent proceedings under the *Companies' Creditors Arrangement Act* are commenced; and

(iii) the period beginning on the day that is six months before one of the following days and ending on the day on which a court makes a determination under subsection 5(5):

(A) the day on which a proposal is filed by or in respect of the employer under Division I of Part III of the *Bankruptcy and Insolvency Act* or, if a notice of intention to make a proposal is filed by or in respect of the employer under that Division, the day on which the notice of intention is filed,

(B) the day on which the most recent proceedings under the *Companies' Creditors Arrangement Act* are commenced; and

(b) termination pay and severance pay that relate to employment that ended

(i) during the period referred to in paragraph (a), or

(ii) during the period beginning on the day after the day on which the period referred to in paragraph (a) ends and ending on the day on which the trusteeis discharged or the receiver completes their duties, as the case may be. (*salaire admissible*)

wages includes salaries, commissions, compensation for services rendered, vacation pay, termination pay, severance pay and any other amounts prescribed by regulation. (*salaire*)

Precision

(1.1) For the purpose of the definition *eligible wages*, a proposal does not include a proposal for which a certificate is given under section 65.3 of the *Bankruptcy andInsolvency Act* and a notice of intention to make a proposal does not include a notice of intention in respect of a proposal for which such a certificate is given.

Meaning of trustee

(1.2) In this Act, trustee includes a monitor as defined in subsection 2(1) of the *Companies' Creditors Arrangement Act.*

Employers subject to a receivership

(2) For the purposes of this Act, an employer is subject to a receivership when any property of the employer is under the possession or control of a receiver.

Meaning of "receiver"

(3) In this Act, "receiver" means a receiver within the meaning of subsection 243(2) of the Bankruptcy and Insolvency Act.

Words and expressions

(4) Unless otherwise provided, words and expressions used in this Act have the same meaning as in the Bankruptcy and Insolvency Act.

Related persons

(5) Despite subsection 4(5) of the Bankruptcy and Insolvency Act,

(a) for the purposes of paragraph 6(d), an individual is considered to deal at arm's length with a related person if the Minister is satisfied that, having regard to the circumstances - including the terms and conditions of the individual's employment with the former employer, their remuneration and the duration, nature and importance of the work performed for the former employer - it is reasonable to conclude that the individual would have entered into a substantially similar contract of employment with the former employer if they had been dealing with each other at arm's length; and

(b) for the purposes of subsection 21(4), individuals who are related to each other are, in the absence of evidence to the contrary, deemed not to deal with each other at arm's length while so related.

Wage Earner Protection Program Act, S.C. 2005, c. 47, s. 1, s. 5

Canada Statutes

S.C. 2005, c. 47, s. 1, s. 5 | L.C. 2005, ch. 47, art. 1, art. 5

[Unofficial Chapter No. W-0.8]

Notice

Current Version: Effective 20-11-2021

ELIGIBILITY FOR PAYMENTS

SECTION 5.

Conditions of eligibility

5 (1). An individual is eligible to receive a payment if

(a) the individual's employment ended for a reason prescribed by regulation;

(b) one of the following applies:

(i) the former employer is bankrupt,

(ii) the former employer is subject to a receivership,

(iii) the former employer is the subject of a foreign proceeding that is recognized by a court under subsection 270(1) of the *Bankruptcy and Insolvency Act* and

(A) the court determines under subsection (2) that the foreign proceeding meets the criteria prescribed by regulation, and

(B) a trustee is appointed, or

(iv) the former employer is the subject of proceedings under Division I of Part III of the *Bankruptcy and Insolvency Act* or under the *Companies' Creditors Arrangement Act* and a court determines under subsection (5) that the criteria prescribed by regulation are met; and

(c) the individual is owed eligible wages by the former employer.

(d) REPEALED: S.C. 2009, c. 2, s. 343(2), effective March 12, 2009 (R.A.).

Prescribed criteria - foreign proceeding

(2) On application by any person, a court may, in a proceeding under Part XIII of the Bankruptcy and Insolvency Act, determine that the foreign proceeding meets the criteria prescribed by regulation. If the court determines that the foreign proceeding meets the prescribed criteria, the court may appoint a trustee for the purposes of this Act.

Employment in Canada

(3) An individual who is eligible to receive a payment because of subparagraph (1)(b)(iii) is only eligible to receive a payment in respect of eligible wages earned for employment in Canada and termination pay and severance pay that relate to that employment.

Deemed bankruptcy

(4) For the purposes of this Act, if all of the conditions set out in subparagraph (1)(b)(iii) are met, the former employer is deemed to be bankrupt and the date of the bankruptcy is deemed to be the day on which all of those conditions are met.

Prescribed criteria - other proceedings

(5) On application by any person, a court may, in proceedings under Division I of Part III of the *Bankruptcy and Insolvency Act* or under the *Companies' Creditors Arrangement Act*, determine that the former employer meets the criteria prescribed by regulation.

AbitibiBowater inc. (Arrangement relatif à), [2009] Q.J. No. 19125

Jugements du Québec

Quebec Superior Court

District of Montreal

The Honourable Clément Gascon, J.S.C.

Heard: November 9, 2009.

Judgment: November 16, 2009.

No.: 500-11-036133-094

[2009] Q.J. No. 19125 | 2009 QCCS 6461 | 190 A.C.W.S. (3d) 678 | 2009 CarswellQue 14224 | EYB 2009-171231

IN THE MATTER OF THE PLAN OF COMPROMISE OR ARRANGEMENT OF: ABITIBIBOWATER INC. and ABITIBI-CONSOLIDATED INC., BOWATER CANADIAN HOLDINGS INC., The other Petitioners listed on Schedules "A", "B" and "C", Petitioners and ERNST & YOUNG INC., Monitor

(109 paras.)

Counsel

Me Sean Dunphy, Me Joseph Reynaud, Attorneys for Petitioners.

Me Robert Thornton, Attorney for the Monitor.

Me Jason Dolman, Attorney for the Monitor.

Me Alain Riendeau, Attorney for Wells Fargo Bank, N.A., Administrative Agent under the Credit and Guarantee Agreement Dated April 1, 2008.

Me Marc Duchesne, Attorney for the Ad hoc Committee of the Senior Secured Noteholders and U.S. Bank National Association, Indenture Trustee for the Senior Secured Noteholders.

Me Frederick L. Myers, Co-Counsel for the Ad Hoc Committee of Unsecured Noteholders of AbitibiBowater Inc. and certain of its Affiliates.

[Editor's note: A Corrected Judgment was released by the Court on November 23, 2009. The corrections have been made to the text and the text of the Corrected Judgment is appended to this document].

JUDGMENT

ON RE-AMENDED MOTION FOR THE APPROVAL OF A

SECOND DIP FINANCING AND FOR DISTRIBUTION OF

CERTAIN PROCEEDS OF THE MPCo SALE TRANSACTION

TO THE TRUSTEE FOR THE SENIOR SECURED NOTES (#312)

approved together. To conclude otherwise would potentially put everything at risk, at a time where stability is most required.

67 [67] Secondly, it remains that ACCC's interest in MPCo is subject to the SSNs' security. As such, all proceeds of the sale less adjustments, holdbacks and reserves should normally be paid to the SSNs. Despite this, provided they receive the CDN$200 million proposed distribution, the SSNs have consented to the sale proceeds being used by the Abitibi Petitioners to pay the existing ACI DIP Facility and to the ULC Reserve being used up to CDN$230M for the ULC DIP Facility funding.

68 [68] It is thus fair to say that the SSNs are not depriving the Abitibi Petitioners of liquidity; they are funding part of the restructuring with their collateral and, in the end, enhancing this liquidity.

69 [69] The net proceeds of the MPCo transaction after payment of the ACI DIP Facility are expected to be CDN$173.9 million. Accordingly, out of a CDN$200 million distribution to the SSNs, only CDN$26.1 million could technically be said to come from the ULC DIP Facility. Contrary to what the Bondholders alluded to, if minor aspects of the claims of the SSNs are disputed by the Abitibi Petitioners, they do not concern the CDN$200 million at issue.

70 [70] Thirdly, the ULC DIP Facility bears no interest and is not subject to drawdown fees, while a distribution of CDN$200 million to the SSNs will create at the same time interest savings of approximately CDN$27 million per year for the ACI Group. There is, as a result, a definite economic benefit to the contemplated distribution for the global restructuring process.

71 [71] Despite what the Bondholders argue, it is neither unusual nor unheard of to proceed with an interim distribution of net proceeds in the context of a sale of assets in a *CCAA* reorganization. Nothing in the *CCAA* prevents similar interim distribution of monies. There are several examples of such distributions having been authorized by Courts in Canada[7].

72 [72] While the SSNs are certainly subject to a stay of proceedings much like the other creditors involved in the present *CCAA* reorganization, an interim distribution of net proceeds from the sale of an asset subject to the Court's approval has never been considered a breach of the stay.

73 [73] In this regard, the Bondholders have no economic interest in the MPCo assets and resulting proceeds of sale that are subject to a first ranking security interest in favor of the SSNs. Therefore, they are not directly affected by the proposed distribution of CDN$200 million.

74 [74] In *Windsor Machine & Stamping Ltd.* (Re)[8], Morawetz J. dealt with the opposition of unsecured creditors to an Approval and Distribution Order as follows:

> 13 Although the outcome of this process does not result in any distribution to unsecured creditors, this does not give rise to a valid reason to withhold Court approval of these transactions. I am satisfied that the unsecured creditors have no economic interest in the assets.

75 [75] Finally, even though the Monitor makes no recommendation in respect of the proposed distribution to the SSNs, this can hardly be viewed as an objection on its part. In the first place, this is not an issue upon which the Monitor is expected to opine. Besides, in its 19th report, the Monitor notes the following in that regard:

a) According to its Counsel, the SSNs security on the ACCC's 60% interest in MPCo is valid and enforceable;

b) The amounts owed to the SSNs far exceed the contemplated distribution while the SSNs' collateral is sufficient for the SSNs' claim to be most likely paid in full;

c) The proposed distribution entails an economy of CDN$27 million per year in interest savings; and

d) Even taking into consideration the CDN$200 million proposed distribution, the ULC DIP Facility provides the Abitibi Petitioners with the liquidity they require for most of the coming year.

Sierra Club of Canada v. Canada (Minister of Finance), [2002] 2 S.C.R. 522

Supreme Court Reports

Supreme Court of Canada

Present: McLachlin C.J. and Gonthier, Iacobucci, Bastarache, Binnie, Arbour and LeBel JJ.

2001: November 6 / 2002: April 26.

File No.: 28020.

[2002] 2 S.C.R. 522 | [2002] 2 R.C.S. 522 | [2002] S.C.J. No. 42 | [2002] A.C.S. no 42 | 2002 SCC 41

Atomic Energy of Canada Limited, appellant; v. Sierra Club of Canada, respondent, and The Minister of Finance of Canada, the Minister of Foreign Affairs of Canada, the Minister of International Trade of Canada and the Attorney General of Canada, respondents.

ON APPEAL FROM THE FEDERAL COURT OF APPEAL (92 paras.)

Case Summary

Practice — Federal Court of Canada — Filing of confidential material — Environmental organization seeking judicial review of federal government's decision to provide financial assistance to Crown corporation for construction and sale of nuclear reactors — Crown corporation requesting confidentiality order in respect of certain documents — Proper analytical approach to be applied to exercise of judicial discretion where litigant seeks confidentiality order — Whether confidentiality order should be granted — Federal Court Rules, 1998, SOR/98-106, r. 151.

Sierra Club is an environmental organization seeking judicial review of the federal government's decision to provide financial assistance to Atomic Energy of Canada Ltd. ("AECL"), a Crown corporation, for the construction and sale to China of two CANDU reactors. The reactors are currently under construction in China, where AECL is the main contractor and project manager. Sierra Club maintains that the authorization of financial assistance [page523] by the government triggered s. 5(1)(b) of the Canadian Environmental Assessment Act ("CEAA"), requiring an environmental assessment as a condition of the financial assistance, and that the failure to comply compels a cancellation of the financial arrangements. AECL filed an affidavit in the proceedings which summarized confidential documents containing thousands of pages of technical information concerning the ongoing environmental assessment of the construction site by the Chinese authorities. AECL resisted Sierra Club's application for production of the confidential documents on the ground, inter alia, that the documents were the property of the Chinese authorities and that it did not have the authority to disclose them. The Chinese authorities authorized disclosure of the documents on the condition that they be protected by a confidentiality order, under which they would only be made available to the parties and the court, but with no restriction on public access to the judicial proceedings. AECL's application for a confidentiality order was rejected by the Federal Court, Trial Division. The Federal Court of Appeal upheld that decision.

Held: The appeal should be allowed and the confidentiality order granted on the terms requested by AECL.

In light of the established link between open courts and freedom of expression, the fundamental question for a court to consider in an application for a confidentiality order is whether the right to freedom of expression should be compromised in the circumstances. The court must ensure that the discretion to grant the order is exercised in accordance with Charter principles because a confidentiality order will have a negative effect on the s. 2(b) right to freedom of expression. A confidentiality order should only be granted when (1) such an order is necessary to prevent a serious risk to an important interest, including a commercial interest, in the context of litigation because reasonably alternative measures will not prevent the risk; and (2) the salutary effects of the confidentiality order, including the effects on the right of civil litigants to a fair trial, outweigh its deleterious effects, including the effects on the right to free expression, which in this context includes the public interest in open and accessible court proceedings. Three important elements are subsumed under the first branch of the test. First, the risk must be real and substantial, well grounded in evidence, posing a serious threat to the commercial interest in question. Second, the important commercial interest must be one which can be expressed in terms of a public interest in confidentiality, where there is a general principle at stake. Finally, the judge is required to consider not only whether reasonable alternatives are available to such an order but also to restrict the order as much as is reasonably possible while preserving the commercial interest in question.

[page524]

Applying the test to the present circumstances, the commercial interest at stake here relates to the objective of preserving contractual obligations of confidentiality, which is sufficiently important to pass the first branch of the test as long as certain criteria relating to the information are met. The information must have been treated as confidential at all relevant times; on a balance of probabilities, proprietary, commercial and scientific interests could reasonably be harmed by disclosure of the information; and the information must have been accumulated with a reasonable expectation of it being kept confidential. These requirements have been met in this case. Disclosure of the confidential documents would impose a serious risk on an important commercial interest of AECL, and there are no reasonably alternative measures to granting the order.

Under the second branch of the test, the confidentiality order would have significant salutary effects on AECL's right to a fair trial. Disclosure of the confidential documents would cause AECL to breach its contractual obligations and suffer a risk of harm to its competitive position. If a confidentiality order is denied, AECL will be forced to withhold the documents in order to protect its commercial interests, and since that information is relevant to defences available under the CEAA, the inability to present this information hinders AECL's capacity to make full answer and defence. Although in the context of a civil proceeding, this does not engage a Charter right, the right to a fair trial is a fundamental principle of justice. Further, the confidentiality order would allow all parties and the court access to the confidential documents, and permit cross-examination based on their contents, assisting in the search for truth, a core value underlying freedom of expression. Finally, given the technical nature of the information, there may be a substantial public security interest in maintaining the confidentiality of such information.

The deleterious effects of granting a confidentiality order include a negative effect on the open court principle, and therefore on the right to freedom of expression. The more detrimental the confidentiality order would be to the core values of (1) seeking the truth and the common good, (2) promoting self-fulfilment of individuals by allowing them to develop thoughts and ideas as they see fit, and (3) ensuring that participation in the political process is open to all persons, the harder it will be to justify the confidentiality order. In the hands of the parties and their experts, the confidential documents may be of great assistance in probing the truth of the Chinese environmental assessment process, which would assist the court in reaching accurate factual conclusions. Given the highly technical nature of the documents, the important value of the search for the truth which underlies [page525] both freedom of expression and open justice would be promoted to a greater extent by submitting the confidential documents under the order sought than it would by denying the order.

Under the terms of the order sought, the only restrictions relate to the public distribution of the documents, which is a fairly minimal intrusion into the open court rule. Although the confidentiality order would restrict individual access to certain information which may be of interest to that individual, the second core value of promoting individual self-fulfilment would not be significantly affected by the confidentiality order. The third core value figures prominently in this appeal as open justice is a fundamental aspect of a democratic society. By their very nature, environmental matters carry significant public import, and openness in judicial proceedings involving environmental issues will generally attract a high degree of protection, so that the public interest is engaged here more than if this were an action between private parties involving private interests. However, the narrow scope of the order coupled with the highly technical nature of the confidential documents significantly temper the deleterious effects the confidentiality order would have on the public interest in open courts. The core freedom of expression values of seeking the truth and promoting an open political process are most closely linked to the principle of open courts, and most affected by an order restricting that openness. However, in the context of this case, the confidentiality order would only marginally impede, and in some respects would even promote, the pursuit of these values. The salutary effects of the order outweigh its deleterious effects and the order should be granted. A balancing of the various rights and obligations engaged indicates that the confidentiality order would have substantial salutary effects on AECL's right to a fair trial and freedom of expression, while the deleterious effects on the principle of open courts and freedom of expression would be minimal.

Cases Cited

Applied: Edmonton Journal v. Alberta (Attorney General), [1989] 2 S.C.R. 1326; Canadian Broadcasting Corp. v. New Brunswick (Attorney General), [1996] 3 S.C.R. 480; Dagenais v. Canadian Broadcasting Corp., [1994] 3 S.C.R. 835; R. v. Mentuck, [2001] 3 S.C.R. 442, 2001 SCC 76; M. (A.) v. Ryan, [1997] 1 S.C.R. 157; Irwin Toy Ltd. v. Quebec (Attorney General), [1989] 1 S.C.R. 927; R. v. Keegstra, [1990] 3 S.C.R. 697; referred to: AB Hassle v. Canada (Minister of National Health and [page526] Welfare), [2000] 3 F.C. 360, aff'g (1998), 83 C.P.R. (3d) 428; Ethyl Canada Inc. v. Canada (Attorney General) (1998), 17 C.P.C. (4th) 278; R. v. Oakes, [1986] 1 S.C.R. 103; R. v. O.N.E., [2001] 3 S.C.R. 478, 2001 SCC 77; F.N. (Re), [2000] 1 S.C.R. 880, 2000 SCC 35; Eli Lilly and Co. v. Novopharm Ltd. (1994), 56 C.P.R. (3d) 437.

Statutes and Regulations Cited

Canadian Charter of Rights and Freedoms, ss. 1, 2(b). Canadian Environmental Assessment Act, S.C. 1992, c. 37, ss. 5(1)(b), 8, 54, 54(2)(b). Federal Court Rules, 1998, SOR/98-106, rr. 151, 312.

APPEAL from a judgment of the Federal Court of Appeal, [2000] 4 F.C. 426, 187 D.L.R. (4th) 231, 256 N.R. 1, 24 Admin. L.R. (3d) 1, [2000] F.C.J. No. 732 (QL), affirming a decision of the Trial Division, [2000] 2 F.C. 400, 178 F.T.R. 283, [1999] F.C.J. No. 1633 (QL). Appeal allowed.
J. Brett Ledger and Peter Chapin, for the appellant. Timothy J. Howard and Franklin S. Gertler, for the respondent Sierra Club of Canada. Graham Garton, Q.C., and J. Sanderson Graham, for the respondents the Minister of Finance of Canada, the Minister of Foreign Affairs of Canada, the Minister of International Trade of Canada and the Attorney General of Canada.

[Quicklaw note: Please see complete list of solicitors appended at the end of the judgment.]

The judgment of the Court was delivered by

IACOBUCCI J.

I. Introduction

1 In our country, courts are the institutions generally chosen to resolve legal disputes as best they can through the application of legal principles to the facts of the case involved. One of the underlying principles of the judicial process is public openness, both in the proceedings of the dispute, and in the material that is relevant to its resolution. However, some material can be made the subject of a confidentiality order. This appeal raises the important [page527] issues of when, and under what circumstances, a confidentiality order should be granted.

2 For the following reasons, I would issue the confidentiality order sought and accordingly would allow the appeal.

II. Facts

operational methods employed by the officers in their investigation of the accused. The accused opposed the motion as an infringement of his right to a fair and public hearing under s. 11(d) of the Charter. The order was also opposed by two intervening newspapers as an infringement of their right to freedom of expression.

44 The Court noted that, while Dagenais dealt with the balancing of freedom of expression on the one hand, and the right to a fair trial of the accused on the other, in the case before it, both the right of the [page540] accused to a fair and public hearing, and freedom of expression weighed in favour of denying the publication ban. These rights were balanced against interests relating to the proper administration of justice, in particular, protecting the safety of police officers and preserving the efficacy of undercover police operations.

45 In spite of this distinction, the Court noted that underlying the approach taken in both Dagenais and New Brunswick was the goal of ensuring that the judicial discretion to order publication bans is subject to no lower a standard of compliance with the Charter than legislative enactment. This goal is furthered by incorporating the essence of s. 1 of the Charter and the Oakes test into the publication ban test. Since this same goal applied in the case before it, the Court adopted a similar approach to that taken in Dagenais, but broadened the Dagenais test (which dealt specifically with the right of an accused to a fair trial) such that it could guide the exercise of judicial discretion where a publication ban is requested in order to preserve any important aspect of the proper administration of justice. At para. 32, the Court reformulated the test as follows:

> A publication ban should only be ordered when:
>
> (a) such an order is necessary in order to prevent a serious risk to the proper administration of justice because reasonably alternative measures will not prevent the risk; and
>
> (b) the salutary effects of the publication ban outweigh the deleterious effects on the rights and interests of the parties and the public, including the effects on the right to free expression, the right of the accused to a fair and public trial, and the efficacy of the administration of justice.

46 The Court emphasized that under the first branch of the test, three important elements were subsumed under the "necessity" branch. First, the risk in question must be a serious risk well grounded in the evidence. Second, the phrase "proper administration of justice" must be carefully interpreted so as not to [page541] allow the concealment of an excessive amount of information. Third, the test requires the judge ordering the ban to consider not only whether reasonable alternatives are available, but also to restrict the ban as far as possible without sacrificing the prevention of the risk.

47 At para. 31, the Court also made the important observation that the proper administration of justice will not necessarily involve Charter rights, and that the ability to invoke the Charter is not a necessary condition for a publication ban to be granted:

> The [common law publication ban] rule can accommodate orders that must occasionally be made in the interests of the administration of justice, which encompass more than fair trial rights. As the test is intended to "reflec[t] the substance of the Oakes test", we cannot require that Charter rights be the only legitimate objective of such orders any more than we require that government action or legislation in violation of the Charter be justified exclusively by the pursuit of another Charter right. [Emphasis added.]

The Court also anticipated that, in appropriate circumstances, the Dagenais framework could be expanded even further in order to address requests for publication bans where interests other than the administration of justice were involved.

48 Mentuck is illustrative of the flexibility of the Dagenais approach. Since its basic purpose is to ensure that the judicial discretion to deny public access to the courts is exercised in accordance with Charter principles, in my view, the Dagenais model can and should be adapted to the situation in the case at bar where the central issue is whether judicial discretion should be exercised so as to exclude confidential information from a public proceeding. As in Dagenais, New Brunswick and Mentuck, granting the confidentiality order will have a negative effect on the Charter right to freedom of expression, as well as the principle of open and accessible court proceedings, and, as in those cases, courts must ensure that the discretion to grant the order is exercised in accordance with Charter

Sherman Estate v. Donovan, [2021] S.C.J. No. 25

Supreme Court of Canada Judgments

Supreme Court of Canada

Present: R. Wagner C.J. and M.J. Moldaver, A. Karakatsanis, R. Brown, M. Rowe, S.L. Martin and N. Kasirer JJ.

Heard: October 6, 2020;

Judgment: June 11, 2021.

File No.: 38695.

[2021] S.C.J. No. 25 | [2021] A.C.S. no 25 | 2021 SCC 25 | 2021 CSC 25 | [2021] 2 S.C.R. 75 | 458 D.L.R. (4th) 361 | 66 C.P.C. (8th) 1 | 67 E.T.R. (4th) 163 | 72 C.R. (7th) 223 | 2021 CarswellOnt 8339 | 490 C.R.R. (2d) 237 | EYB 2021-391973 | 331 A.C.W.S. (3d) 489 | 2021EXP-1617

Estate of Bernard Sherman and Trustees of the Estate and Estate of Honey Sherman and Trustees of the Estate, Appellants; v. Kevin Donovan and Toronto Star Newspapers Ltd., Respondents, and Attorney General of Ontario, Attorney General of British Columbia, Canadian Civil Liberties Association, Income Security Advocacy Centre, Ad IDEM/Canadian Media Lawyers Association, Postmedia Network Inc., CTV, a Division of Bell Media Inc., Global News, a division of Corus Television Limited Partnership, The Globe and Mail Inc., Citytv, a division of Rogers Media Inc., British Columbia Civil Liberties Association, HIV & AIDS Legal Clinic Ontario, HIV Legal Network and Mental Health Legal Committee, Interveners

(108 paras.)

Appeal From:

ON APPEAL FROM THE COURT OF APPEAL FOR ONTARIO

Case Summary

Civil litigation — Civil evidence — Documentary evidence — Publication bans and confidentiality orders — Sealed evidence — Appeal by estate trustees from Ontario Court of Appeal decision that lifted sealing orders dismissed û-Application judge had granted sealing orders over probate files of prominent couple whose death had generated intense public interest — Privacy could be important public interest under test for discretionary limits on court openness where it could be shown protection of human dignity was at serious risk — Estate trustees had failed to establish serious risk to important public interest that overcame strong presumption of court openness — Information contained in probate files did not reveal anything particularly private or highly sensitive and did not strike at core identity of affected individuals — Record did not disclose serious risk of physical harm to affected individuals.

Wills, estates and trusts law — Proceedings — Practice and procedure — Application judge had granted sealing orders over probate files of prominent couple whose death had generated intense public interest — Privacy could be important public interest under test for discretionary limits on court openness where it could be shown protection of human dignity was at serious risk — Estate trustees had failed to establish serious risk to important public interest that overcame strong presumption of court openness —

Information contained in probate files did not reveal anything particularly private or highly sensitive and did not strike at core identity of affected individuals — Record did not disclose serious risk of physical harm to affected individuals.

Appeal by the estate trustees from a decision of the Ontario Court of Appeal that lifted sealing orders granted by the application judge. The unexplained deaths of a prominent couple in their home generated intense public interest. The estate trustees obtained sealing orders of the probate files. The orders were challenged by a journalist. The application judge sealed the probate files, finding the harmful effects of the sealing orders were substantially outweighed by the salutary effects on privacy and physical safety interests. The Court of Appeal lifted the sealing orders on the basis that the privacy interest advanced lacked a public interest quality and there was no evidence of a real risk to anyone's physical safety.
HELD: Appeal dismissed.

Privacy could be an important public interest under the test for discretionary limits on court openness where it could be shown that the protection of human dignity was at serious risk. It had to be demonstrated that the information was sufficiently sensitive such that it could be said to strike at the biographical core of the individual and that there was a serious risk that without an exceptional order, the affected individual would suffer an affront to their dignity. The estate trustees had failed to establish a serious risk to the important public interest in privacy, predicated on dignity, that overcame the strong presumption of openness. The information contained in the probate files did not reveal anything particularly private or highly sensitive and did not strike at the core identity of the affected individuals. Merely associating the affected individuals with the couple's unexplained deaths was not sufficient to constitute a serious risk to the identified important public interest in privacy, defined in reference to dignity. The record did not show a serious risk of physical harm to any affected individuals. Any inference of a serious risk of physical harm was speculative.

Statutes, Regulations and Rules Cited:

Bill C-11, An Act to enact the Consumer Privacy Protection Act and the Personal Information and Data Protection Tribunal Act and to make consequential and related amendments to other Acts, 2nd Sess., 43rd Parl., 2020

Canadian Charter of Rights and Freedoms, 1982, s. 2(b), s. 8

Charter of Human Rights and Freedoms, CQLR, c. C-12, s. 5

Civil Code of Quebec <TREATMTENT/> Article 35   R Article 41 R

Code of Civil Procedure, CQLR, c. C-25.01, Article 12

Freedom of Information and Protection of Privacy Act, R.S.O. 1990, c. F.31

Personal Information Protection and Electronic Documents Act, S.C. 2000, c. 5

Privacy Act, R.S.C. 1985, c. P-21

Subsequent History:

NOTE: This document is subject to editorial revision before its reproduction in final form in the Canada Supreme Court Reports.

Court Catchwords:

Courts -- Open court principle -- Sealing orders -- Discretionary limits on court openness -- Important public interest -- Privacy -- Dignity -- Physical safety -- Unexplained deaths of prominent couple generating intense public scrutiny and prompting trustees of estates to apply for sealing of probate files -- Whether privacy and physical safety

They argue that the importance of the open court principle is attenuated by the nature of these probate proceedings. Given that it is non-contentious and not strictly speaking necessary for the transfer of property at death, probate is a court proceeding of an "administrative" character, which diminishes the imperative of applying the open court principle here (paras. 113-14).

27 The Toronto Star takes the position that the Court of Appeal made no mistake in setting aside the sealing orders and that the appeal should be dismissed. In the Toronto Star's view, while privacy can be an important interest where it evinces a public component, the Trustees have only identified a subjective desire for the affected individuals in this case to avoid further publicity, which is not inherently harmful. According to the Toronto Star and some of the interveners, the Trustees' position would allow that measure of inconvenience and embarrassment that arises in every court proceeding to take precedence over the interest in court openness protected by the *Canadian Charter of Rights and Freedoms* in which all of society has a stake. The Toronto Star argues further that the information in the court files is not highly sensitive. On the issue of whether the sealing orders were necessary to protect the affected individuals from physical harm, the Toronto Star submits that the Court of Appeal was right to conclude that the Trustees had failed to establish a serious risk to this interest.

28 In the alternative, even if there were a serious risk to one or another important interest, the Toronto Star says the sealing orders are not necessary because the risk could be addressed by an alternative, less onerous order. Furthermore, it says the orders are not proportionate. In seeking to minimize the importance of openness in probate proceedings, the Trustees invite an inflexible approach to balancing the effects of the order that is incompatible with the principle that openness applies to all court proceedings. In any event, there is a public interest in openness specifically here, given that the certificates sought can affect the rights of third parties and that openness ensures the fairness of the proceedings, whether they are contested or not.

V. Analysis

29 The outcome of the appeal turns on whether the application judge should have made the sealing orders pursuant to the test for discretionary limits on court openness from this Court's decision in *Sierra Club*.

30 Court openness is protected by the constitutional guarantee of freedom of expression and is essential to the proper functioning of our democracy (*Canadian Broadcasting Corp. v. New Brunswick (Attorney General)*, [1996] 3 S.C.R. 480, at para. 23; *Vancouver Sun (Re)*, 2004 SCC 43, [2004] 2 S.C.R. 332, at paras. 23-26). Reporting on court proceedings by a free press is often said to be inseparable from the principle of open justice. "In reporting what has been said and done at a public trial, the media serve as the eyes and ears of a wider public which would be absolutely entitled to attend but for purely practical reasons cannot do so" (*Khuja v. Times Newspapers Limited*, [2017] UKSC 49, [2019] A.C. 161, at para. 16, citing *Edmonton Journal v. Alberta (Attorney General)*, [1989] 2 S.C.R. 1326, at pp. 1326-39, per Cory J.). Limits on openness in service of other public interests have been recognized, but sparingly and always with an eye to preserving a strong presumption that justice should proceed in public view (*Dagenais v. Canadian Broadcasting Corp.*, [1994] 3 S.C.R. 835, at p. 878; *R. v. Mentuck*, 2001 SCC 76, [2001] 3 S.C.R. 442, at paras. 32-39; *Sierra Club*, at para. 56). The test for discretionary limits on court openness is directed at maintaining this presumption while offering sufficient flexibility for courts to protect these other public interests where they arise (*Mentuck*, at para. 33). The parties agree that this is the appropriate framework of analysis for resolving this appeal.

31 The parties and the courts below disagree, however, about how this test applies to the facts of this case and this calls for clarification of certain points of the *Sierra Club* analysis. Most centrally, there is disagreement about how an important interest in the protection of privacy could be recognized such that it would justify limits on openness, and in particular when privacy can be a matter of public concern. The parties bring two settled principles of this Court's jurisprudence to bear in support of their respective positions. First, this Court has often observed that privacy is a fundamental value necessary to the preservation of a free and democratic society (*Lavigne v. Canada (Office of the Commissioner of Official Languages)*, 2002 SCC 53, [2002] 2 S.C.R. 773, at para. 25; *Dagg v. Canada (Minister of Finance)*, [1997] 2 S.C.R. 403, at paras. 65-66, per La Forest J. (dissenting but not on this point); *New Brunswick*, at para. 40). Courts have invoked privacy, in some instances, as the basis for an exception to openness under the *Sierra Club* test (see, e.g., *R. v. Henry*, 2009 BCCA 86, 270 B.C.A.C. 5, at paras. 11 and 17). At the same time, the jurisprudence acknowledges that some degree of privacy loss -- resulting in inconvenience, even in upset or embarrassment -- is inherent in any court proceeding open to the public (*New Brunswick*, at para. 40). Accordingly, upholding the presumption of openness has meant recognizing that neither individual sensibilities nor mere personal discomfort associated with participating in judicial proceedings are likely to justify the exclusion of the public from court (*Attorney General of Nova Scotia v. MacIntyre*, [1982] 1 S.C.R. 175, at p. 185; *New Brunswick*, at para. 41). Determining the role of privacy in the *Sierra Club* analysis requires reconciling these two ideas, which is the nub of the disagreement between the parties. The right of privacy is not absolute; the open court principle is not without exceptions.

32 For the reasons that follow, I disagree with the Trustees that the ostensibly unbounded privacy interest they invoke qualifies as an important public interest within the meaning of *Sierra Club*. Their broad claim fails to focus on the elements of privacy that are deserving of public protection in the open court context. That is not to say, however, that privacy can never ground an exceptional measure such as the sealing orders sought in this case. While the mere embarrassment caused by the dissemination of personal information through the open court process does not rise to the level justifying a limit on court openness, circumstances do exist where an aspect of a person's private life has a plain public interest dimension.

33 Personal information disseminated in open court can be more than a source of discomfort and may result in an affront to a person's dignity. Insofar as privacy serves to protect individuals from this affront, it is an important public interest relevant under *Sierra Club*. Dignity in this sense is a related but narrower concern than privacy generally; it transcends the interests of the individual and, like other important public interests, is a matter that concerns the society at large. A court can make an exception to the open court principle, notwithstanding the strong presumption in its favour, if the interest in protecting core aspects of individuals' personal lives that bear on their dignity is at serious risk by reason of the dissemination of sufficiently sensitive information. The question is not whether the information is "personal" to the individual concerned, but whether, because of its highly sensitive character, its dissemination would occasion an affront to their dignity that society as a whole has a stake in protecting.

34 This public interest in privacy appropriately focuses the analysis on the impact of the dissemination of sensitive personal information, rather than the mere fact of this dissemination, which is frequently risked in court proceedings and is necessary in a system that privileges court openness. It is a high bar -- higher and more precise than the sweeping privacy interest relied upon here by the Trustees. This public interest will only be seriously at risk where the information in question strikes at what is sometimes said to be the core identity of the individual concerned: information so sensitive that its dissemination could be an affront to dignity that the public would not tolerate, even in service of open proceedings.

35 I hasten to say that applicants for an order making exception to the open court principle cannot content themselves with an unsubstantiated claim that this public interest in dignity is compromised any more than they could by an unsubstantiated claim that their physical integrity is endangered. Under *Sierra Club*, the applicant must show on the facts of the case that, as an important interest, this dignity dimension of their privacy is at "serious risk". For the purposes of the test for discretionary limits on court openness, this requires the applicant to show that the information in the court file is sufficiently sensitive such that it can be said to strike at the biographical core of the individual and, in the broader circumstances, that there is a serious risk that, without an exceptional order, the affected individual will suffer an affront to their dignity.

36 In the present case, the information in the court files was not of this highly sensitive character that it could be said to strike at the core identity of the affected persons; the Trustees have failed to show how the lifting of the sealing orders engages the dignity of the affected individuals. I am therefore not convinced that the intrusion on their privacy raises a serious risk to an important public interest as required by *Sierra Club*. Moreover, as I shall endeavour to explain, there was no serious risk of physical harm to the affected individuals by lifting the sealing orders. Accordingly, this is not an appropriate case in which to make sealing orders, or any order limiting access to these court files. In the circumstances, the admissibility of the Toronto Star's new evidence is moot. I propose to dismiss the appeal.

A. *The Test for Discretionary Limits on Court Openness*

37 Court proceedings are presumptively open to the public (*MacIntyre*, at p. 189; *A.B. v. Bragg Communications Inc.*, 2012 SCC 46, [2012] 2 S.C.R. 567, at para. 11).

38 The test for discretionary limits on presumptive court openness has been expressed as a two-step inquiry involving the necessity and proportionality of the proposed order (*Sierra Club*, at para. 53). Upon examination, however, this test rests upon three core prerequisites that a person seeking such a limit must show. Recasting the test around these three prerequisites, without altering its essence, helps to clarify the burden on an applicant seeking an exception to the open court principle. In order to succeed, the person asking a court to exercise discretion in a way that limits the open court presumption must establish that:

(1) court openness poses a serious risk to an important public interest;

(2) the order sought is necessary to prevent this serious risk to the identified interest because reasonably alternative measures will not prevent this risk; and,

(3) as a matter of proportionality, the benefits of the order outweigh its negative effects.

Only where all three of these prerequisites have been met can a discretionary limit on openness -- for example, a sealing order, a publication ban, an order excluding the public from a hearing, or a redaction order -- properly be ordered. This test applies to all discretionary limits on court openness, subject only to valid legislative enactments (*Toronto Star Newspapers Ltd. v. Ontario*, 2005 SCC 41, [2005] 2 S.C.R. 188, at paras. 7 and 22).

39 The discretion is structured and controlled in this way to protect the open court principle, which is understood to be constitutionalized under the right to freedom of expression at s. 2(b) of the Charter (*New Brunswick*, at para. 23). Sustained by freedom of expression, the open court principle is one of the foundations of a free press given that access to courts is fundamental to newsgathering. This Court has often highlighted the importance of open judicial proceedings to maintaining the independence and impartiality of the courts, public confidence and understanding of their work and ultimately the legitimacy of the process (see, e.g., *Vancouver Sun*, at paras. 23-26). In *New Brunswick*, La Forest J. explained the presumption in favour of court openness had become "'one of the hallmarks of a democratic society'" (citing *Re Southam Inc. and The Queen (No.1)* (1983), 41 O.R. (2d) 113 (C.A.), at p. 119), that "acts as a guarantee that justice is administered in a non-arbitrary manner, according to the rule of law ... thereby fostering public confidence in the integrity of the court system and understanding of the administration of justice" (para. 22). The centrality of this principle to the court system underlies the strong presumption -- albeit one that is rebuttable -- in favour of court openness (para. 40; *Mentuck*, at para. 39).

40 The test ensures that discretionary orders are subject to no lower standard than a legislative enactment limiting court openness would be (*Mentuck*, at para. 27; *Sierra Club*, at para. 45). To that end, this Court developed a scheme of analysis by analogy to the *Oakes* test, which courts use to understand whether a legislative limit on a right guaranteed under the *Charter* is reasonable and demonstrably justified in a free and democratic society (*Sierra Club*, at para. 40, citing *R. v. Oakes*, [1986] 1 S.C.R. 103; see also *Dagenais*, at p. 878; *Vancouver Sun*, at para. 30).

41 The recognized scope of what interests might justify a discretionary exception to open courts has broadened over time. In *Dagenais*, Lamer C.J. spoke of a requisite risk to the "fairness of the trial" (p. 878). In *Mentuck*, Iacobucci J. extended this to a risk affecting the "proper administration of justice" (para. 32). Finally, in *Sierra Club*, Iacobucci J., again writing for a unanimous Court, restated the test to capture any serious risk to an "important interest, including a commercial interest, in the context of litigation" (para. 53). He simultaneously clarified that the important interest must be expressed as a public interest. For example, on the facts of that case, a harm to a particular business interest would not have been sufficient, but the "general commercial interest of preserving confidential information" was an important interest because of its public character (para. 55). This is consistent with the fact that this test was developed in reference to the *Oakes* jurisprudence that focuses on the "pressing and