COURT FILE NUMBER	
COURT	COURT OF KING'S BENCH OF ALBERTA
JUDICIAL CENTRE	CALGARY
	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 PEAVEY INDUSTRIES GENERAL PARTNER LIMITED, TSC STORES GP INC., GUYS FREIGHTWAYS LTD., and PEAVEY INDUSTRIES LIMITED
APPLICANTS	PEAVEY INDUSTRIES GENERAL PARTNER LIMITED, TSC STORES GP INC., GUYS FREIGHTWAYS LTD., and PEAVEY INDUSTRIES LIMITED
DOCUMENT	**BRIEF OF LAW** **(CCAA INITIAL ORDER)**

Clerk's stamp

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INTRODUCTION

1. This Brief of Law is submitted by the Applicants:

   i. Peavey Industries General Partner Limited (**Peavey GP**);

   ii. TSC Stores GP Inc. (**TSC GP**);

   iii. Guys Freightways Ltd. (**Guys**); and

   iv. Peavey Industries Limited (**Peavey Industries**).

2. The non-applicant entities in this matter are Peavey Industries LP (**Peavey**), a limited partnership, and Peavey Industries Mutual Fund Trust (**MFT**), a trust (Peavey and MFT, together with the Applicants, are hereinafter referred to collectively as the **Peavey Group**). Although Peavey and MFT are not "companies" within the meaning of the *Companies' Creditors Arrangement Act*, as amended (**CCAA**),[1] they are nevertheless integral to the business of the Peavey Group.

3. The Applicants seek an Initial Order under the CCAA and the Court's inherent jurisdiction, to, among other things:

    i. abridge the time for service of notice for the Application and all supporting materials, and deem service thereof to be good and sufficient;

    ii. confirm the Applicants are companies to which the CCAA applies;

    iii. grant a stay of proceedings (**Stay**) in favour of the Applicants through February 6, 2025 at 11:59pm (**Initial Stay Period**), subject to the exemption described below to facilitate the Peavey Group's continued access to credit;

    iv. extend the stay of proceedings, together with the other benefits and protections contained in the proposed Initial Order, to Peavey and MFT;

    v. appoint FTI Consulting Canada Inc. (**FTI**) as the monitor in this CCAA proceeding (if appointed, the **Monitor**);

    vi. confirm that the Applicants shall remain in possession and control of their current and future assets, undertakings, and properties of every nature and kind whatsoever, and wherever situate, including all proceeds thereof (**Property**), and that they shall be entitled to continue to carry on business in a manner consistent with the preservation of value;

    vii. authorize the Applicants to continue to use the Cash Management System;

    viii. authorize (but not obligate) the Applicants to pay for any amounts outstanding for inventory delivered by critical suppliers with the consent of the Monitor and the Agent;

    ix. grant the following priority charges (collectively, the **Charges**) on the Property of the Applicants, listed in the following order of priority:

        i. an administration charge (**Administration Charge**) not exceeding an aggregate amount of $500,000 for the Initial Stay period as security for the professional fees and disbursements of the Monitor, counsel for the Monitor, and counsel for the Applicants, both before and after the granting of the Initial Order;

        ii. an interim lender's charge (**Interim Lender's Charge**) not exceeding an aggregate amount of $15,000,000 for the Initial Stay period as security for any advances made from the Applicants' continued use of the 1903 Revolving Loan Facility (as defined below), from and after the commencement of these CCAA

[1] *Companies' Creditors Arrangement Act*, RSC 1985, c C-36 [***CCAA***].

proceedings. The Applicants have also sought an exemption to the stay of proceedings against the Agent, on behalf of the Lenders, to permit the maintenance of the Cash Management System and permit Peavey to continue to borrow under the existing 1903 Revolving Loan Facility. ; and

iii. a charge in favour of the Applicants' directors and officers (**D&O Charge**) not exceeding an aggregate amount of $5,000,000 for the Initial Stay Period as security for the Applicants' indemnification obligations of their offices and directors against liabilities they may incur as directors and/or officers of the Peavey Group after the commencement of these CCAA proceedings except to the extent any obligation was incurred as a result of any director's or officer's gross negligence or willful misconduct,

x. authorize continued performance under the SC Consulting Agreement, the RE Consulting Agreement and the Consignment Agreement (as such agreements are defined below).

4. In support of its Application, the Applicants rely on the Affidavit of Douglas (Doug) Anderson (**Anderson Affidavit**) and the pre-filing report of FTI as proposed Monitor (**Monitor's Pre-Filing Report**).

5. Capitalized terms not otherwise defined take their meaning from the Anderson Affidavit.

6. This Brief of Law is intended to outline the legislation and jurisprudence that is pertinent to the relief being sought by the Applicants in the proposed Initial Order.

FACTS

7. Peavey is the limited partnership through which the Peavey Group operates its retail operation across 94 store locations and six provinces.[2] Peavey employes the Peavey Group's approximately 1,900 employees (excepting approximately 20 who are employed directly by Guys), leases substantially all of its premises, purchases inventory, and carries on the retail operations.[3]

8. The general partner of Peavey is Peavey GP. The limited partners of Peavey are MFT and Peavey Industries.[4]

9. TSC GP is a related entity that has a common parent (983329 Alberta Ltd.) with, *inter alia*, Peavey GP, Peavey Industries, and the manager of MFT.[5]

10. Guys provides logistics and transportation for the Peavey Group and is wholly owned by Peavey.[6]

11. Peavey's revenue performance was negatively impacted by cautious consumer spending, given the discretionary nature of many of its goods, combined with pressures from the COVID-

[2] Anderson Affidavit at para 7.
[3] Anderson Affidavit at para 7, 11, 35, 50-51.
[4] Anderson Affidavit at para 16.
[5] Anderson Affidavit at para 17.
[6] Anderson Affidavit at para 18, 31-34.

19 pandemic, inflation, high interest rates, and strong competition from big box and e-retailers. That resulted in slowed sales and margin pressures throughout 2023 and 2024.[7]

12. Peavey estimates that it has on-hold, past due balances with approximately 820 suppliers totalling approximately $60,000,000.[8] It is clearly unable to pay its debts as they are coming due.

13. Peavey defaulted under the RBC Credit Agreement, which led to a lengthy series of loan amendments.

14. However, on December 20, 2024, Peavey entered the 1903 Credit Agreement to pay out its indebtedness under the RBC Credit Agreement and regain potential access to working capital.[9]

15. Peavey is the borrower under the 1903 Credit Agreement. The other Peavey Group members are all guarantors of Peavey's indebtedness under the 1903 Credit Agreement through unlimited guarantees (Peavey GP, TSC GP and Guys) or limited recourse guarantees (Peavey Industries and MFT).[10] Recourse against Peavey Industries and MFT is limited to their respective holdings of partnership units in Peavey.

16. Revenue performance in December 2024 and early January 2025 was such that Peavey defaulted under the 1903 Credit Agreement by January 15, 2025.[11]

17. The Agent served demands and notices of intention to enforce security under s. 244 of the *Bankruptcy and Insolvency Act* on all of the Peavey Group members on January 16, 2025 in the amount of $66,414,413.41, plus legal and professional fees, costs, charges, disbursements and expenses.[12]

18. The Peavey Group has worked constructively with the Agent to address the defaults under the 1903 Credit Agreement and the indebtedness to the Lenders by taking prompt steps to maximize value, most significantly by starting a nationwide liquidation process on January 24, 2025.

19. The Applicants have been aided in this liquidation process by Gordon Brothers Canada ULC through the provision of consulting services under a store closing consulting agreement (**SC Consulting Agreement**), a real estate services consulting agreement (**RE Consulting Agreement**), and the supply of consigned inventory under a consignment agreement (**Consignment Agreement**).[13]

20. The Applicants are continuing to rely on their Cash Management System. The Agent "sweeps" the cash accounts of Peavey daily. Peavey's ability to fund operations during the ongoing liquidation is therefore dependent on its continued access to credit under the 1903 Revolving Loan Facility, which the Agent will cut-off if not protected by an Interim Lender's Charge. The

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[7] Anderson Affidavit at paras 8, 64.
[8] Anderson Affidavit at para 53.
[9] Anderson Affidavit at para 42.
[10] Anderson Affidavit at para 44. The limited recourse guarantee of MFT was entered by Peavey Industries MFT Management Limited (a non-Applicant) on behalf of the MFT.
[11] Anderson Affidavit at para 68.
[12] Anderson Affidavit at para 69.
[13] Anderson Affidavit at para 45.

proposed Interim Lender's Charge results in post-filing sales proceeds to be used to reduce the 1903 pre-filing secured indebtedness as post-filing expenses are paid under the CCAA Interim Lender's Charge.

21. Management is committed to maximizing value, which requires the implementation of the Stay to prevent enforcement by creditors as inventory and store locations are liquidated, non-core assets are sold, and the business is evaluated to determine if any parts of it may be sold or emerge from CCAA as going concerns.

22. The Applicants therefore seek an Initial Order under the CCAA.

ISSUES

23. The issues before the Court are:

    a) Does the CCAA apply to the Applicants?

    b) Is a stay reasonably necessary and appropriate?

    c) Are the priority charges necessary and appropriate?

LAW AND ARGUMENT

a. The CCAA Applies to the Applicants

24. The CCAA applies to a debtor company if the aggregate claims against it or its affiliated debtor companies are more than five million dollars.

25. All of the Applicants meet the definition of a "company" under section 2(1) of the CCAA. They are all corporations incorporated by or under the legislature of a province.

26. Under section 2 of the CCAA, a "debtor company" includes "any company that is bankrupt or insolvent".

27. "Insolvent" is not defined in the CCAA.

28. "Insolvency" for the purposes of the CCAA is informed (but not dictated) by the definition of "insolvent person" under the *Bankruptcy and Insolvency Act* (**BIA**).[14]

29. "[I]nsolvent person" is defined in section 2 of the BIA to mean a person against whom there are provable claims of $1,000 or more and who is unable to meet its obligations as they generally become due, has ceased paying his current obligations in the ordinary course of business as they generally become due, or the aggregate of whose property is not sufficient to enable payment of his obligations, due and accruing due.[15]

30. The "insolvency" threshold under the CCAA is accepted as more liberal than under the BIA. If a company is insolvent under the BIA, it is necessarily insolvent under the CCAA.[16]

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[14] *Bankruptcy and Insolvency Act*, RSC 1985, c B-3 [***BIA***].
[15] The *BIA* at s 2; *Stelco Inc, Re,* 2004 CanLII 24933 (ONSC) leave to appeal refused, at para 22 **[*Stelco*]**.
[16] *Stelco,* para 22.

However, to give effect to the CCAA's rehabilitative objectives, a company is insolvent under the CCAA if it is "reasonably expected to run out of liquidity within a reasonable proximity of time as compared with the time reasonably required to implement a restructuring."[17]

31. The Applicants are indebted under guarantees of Peavey's indebtedness under the 1903 Credit Agreement in the amount of $66,414,413.41, plus legal and professional fees, costs, charges, disbursements and expenses, which they cannot satisfy.

32. All of the Applicants therefore have debts in excess of $5 million and are insolvent on any standard.

b. A Stay of Proceedings is Appropriate

33. An Initial Order may include any relief that is reasonably necessary for the continued operations of the debtor company in the ordinary course during the CCAA proceedings.[18]

34. Such relief may (and typically does) include a stay of proceedings, which ensures that creditor enforcement does not interfere with any restructuring or liquidation.[19] The stay of proceedings maintains the *status quo* while the company develops and implements a strategy to maximize value.[20]

35. A stay of proceedings – like all relief under the CCAA – is contingent on good faith and due diligence, which is an analysis generally not undertaken in detail at an Initial Application.[21] The existence of financially challenging circumstances is not evidence of an absence of good faith or due diligence.

36. In this case, the Applicants have acted with good faith and due diligence in addressing their liquidity and by filing under the CCAA. As is disclosed in FTI's Pre-Filing Report, the proposed Monitor has expressed satisfaction that the relief being sought by the Applicants is necessary, reasonable and justified in the circumstances.[22]

37. The proposed Initial Order provides that the stay of proceedings will not apply so as to prevent the Interim Lender from "sweeping" the Cash Management Accounts. The Applicants submit that this stay exemption is reasonable and appropriate in circumstances in which it will facilitate the Peavey Group's ongoing access to the 1903 Revolving Loan Facility.

38. The proposed Initial Order will apply not only in respect of the Applicants, but that it will also extend, together with the benefits of the other relief sought in this Application, to the limited partnership, Peavey, and the mutual fund trust, MFT.

39. Although the definition of "debtor company" under the CCAA does not include partnerships, this Court and others have held that, where a limited partnership (like Peavey) is closely

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[17] *Stelco*, para 26.
[18] *CCAA*, s 11.001; see also *Century Services* at paras 60-62.
[19] *CCAA*, s 11.02.
[20] *Lehndorff General Partner Ltd, Re*, 1993 OJ No 14, 17 CBR (3d) 24 (Ont SCJ) at paras 5-6; *Meridian Developments v Toronto Dominion Bank*, 1984 CanLII 1176 (AB KB) at para 15.
[21] *Industrial Properties* at paras 22-23.
[22] Pre-Filing Report of the Proposed Monitor, FTI Consulting Canada Inc, filed, at para ● (**Pre-Filing Report**).

connected to or intertwined with the business of a qualifying debtor company, the Court may rely on its inherent jurisdiction to extend the stay of proceedings.[23]

40. On a principled basis, the same should be true of trusts.

41. Peavey is the principal operating entity for the Peavey Group's retail operations, the employer of substantially all of its employees, the lessee of substantially all of its premises, the acquiror of inventory, and the borrower under the 1903 Credit Agreement.

42. MFT is a limited partner of Peavey and has granted a limited recourse guarantee in respect of Peavey's indebtedness under the 1903 Credit Agreement.

43. The Peavey Group continues to review its records to determine whether there are any additional corporate or other sources of contingent liability. If identified, an investigation into and the possibility of such additional sources of liability would only further support the need for a stay of proceedings protecting all members of the Peavey Group.

44. It is reasonable, appropriate and necessary to extend the stay of proceedings, together with the benefits of the other relief sought in this Application, to Peavey and MFT to ensure the objectives of the CCAA in these proceedings are achieved.

45. The threshold to obtain a stay of proceedings under the CCAA is low. A stay should be granted if it would "usefully further" the efforts to reorganize. Nothing more than a "germ" of a plan has to be put forward.[24]

46. Here, there is much more than a germ of a plan. Liquidation sales at Peavey Stores are already underway and there is a plan – supported by the Agent, Peavey's consultants, and the proposed Monitor – to proceed by:

    i. closing under-performing stores, including selling or disclaiming store leases, in accordance with the RE Consulting Agreement;

    ii. liquidating inventory in accordance with the SC Consulting Agreement;

    iii. selling non-core assets;

    iv. selling consignment merchandise at store locations, as necessary to promote customer traffic or otherwise enhance value, in accordance with the Consignment Agreement;

    v. identifying any parts of the business that may be sold or survive as going concerns; and

    vi. strategizing to further address the liquidity issues faced by the Peavey Group.

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[23] *Re Lehndorff General Partner Ltd.* (1993), 17 C.B.R. (3d) 24, 9 B.L.R. (2d) 275, 1993 CarswellOnt 183, at paras 16-21; *Calpine Canada Energy Ltd., Re*, 2006 ABQB 153, at paras 30-34; *Forest & Marine Financial Corp., Re*, 2009 BCCA 319, at paras 13-21.

[24] *Century Services* at para 70; *Industrial Properties Regina Limited v Copper Sands Land Corp*, 2018 SKCA 36 at para 21 [***Industrial Properties***]; *Alberta Treasury Branches v Tallgrass Energy Corp*, 2013 ABQB 432 at para 14.

47. Since November 1, 2019, when certain amendments to the CCAA became effective, a stay of proceedings in an Initial Order under the CCAA is limited to ten days,[25] albeit subject to extension at the comeback application and thereafter. The necessity of having a comeback application after only ten days has the effect of minimizing prejudice to creditors who receive short or no notice of the Initial Application. Any creditor with concerns about the adequacy of service is only required to wait ten days to make its case in opposition to the continuation of the stay of proceedings.

48. It is respectfully submitted that the evidence put forward supports the Applicants' request for a stay of proceedings, at least for the Initial Stay Period of ten days.

c. The Priority Charges are Necessary and Appropriate

49. The Applicants seek the below charges, which are all reasonable and appropriate in the circumstances.

i. Administration Charge

50. The Applicants seek the approval of a charge of $500,000 that would act as security for the professional fees and disbursements of the Monitor, counsel for the Monitor, and counsel for the Applicants, both before and after the granting of the Initial Order (the **Administration Charge**).

51. The CCAA authorizes the Court to grant a priority charge in respect of professional fees and disbursements on notice to secured creditors who are likely to be affected by it.[26]

52. In *Re Canwest Publishing Inc.,* the Ontario Superior Court of Justice stated that the factors to consider in determining whether to approve an administration charge include:

a) the size and complexity of the businesses being restructured;

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

c) whether there is an unwarranted duplication of roles;

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

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

f) the position of the Monitor.[27]

53. Courts have recognized that administration charges, as well as charges in favour of directors and officers, are often necessary to ensure the effectiveness of the CCAA proceedings. For example, in *Re Timminco*, Morawetz J. (now C.J.) stated that failing to provide such charges

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[25] *CCAA*, s 11.02(1).
[26] *CCAA*, s 11.52.
[27] *Canwest Publishing Inc,* 2010 ONSC 222 at para 54 [***Canwest***].

would "result in the overwhelming likelihood that the CCAA proceedings would come to an abrupt halt, followed, in all likelihood, by bankruptcy proceedings".[28]

54. In the instant case, an Administration Charge is necessary in light of the significant size and complexity of the Peavey Group's proposed restructuring and the necessary involvement of qualified professionals. The Peavey Group requires the knowledge, expertise and continuing participation of the beneficiaries of the proposed Administration Charge in order to maximize value.

55. The proposed Monitor has advised in its Pre-Filing Report that such quantum is appropriate in light of the anticipated complexity of the CCAA proceedings, and the services to be provided by the beneficiaries of the Administration Charge.[29]

ii. Interim Lender's Charge

56. The Applicants seek approval of a charge for $15,000,000 (the **Interim Lender's Charge**) as security for any advances made from the Applicants' continued use of the 1903 Revolving Loan Facility, from and after the commencement of these CCAA proceedings.

57. Section 11.2(1) of the CCAA empowers the Court to grant an Interim Lender's Charge in an amount the Court considers appropriate, having regard to the debtor company's cash flow statement, provided notice is given to secured creditors.

58. Further, Section 11.2(4) lists the following non-exclusive factors to consider when determining whether to grant such a charge:

    i. the period during which the company is expected to be subject to proceedings under this Act;

    ii. how the company's business and financial affairs are to be managed during the proceedings;

    iii. whether the company's management has the confidence of its major creditors;

    iv. whether the loan would enhance the prospects of a viable compromise or arrangement being made in respect of the company;

    v. the nature and value of the company's property;

    vi. whether any creditor would be materially prejudiced as a result of the security or charge; and

    vii. the monitor's report, if any.[30]

59. Section 11.2(5) of the CCAA states that a Court shall not grant an order for interim financing at the same time as granting an initial order unless it is satisfied that the terms of the loan are limited to those terms that are reasonably necessary for an applicant's continued operations

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[28] *Re Timminco Ltd*, 2012 ONSC 506 at para 66.
[29] Pre-Filing Report at para ●.
[30] See also *Canwest, supra* at para 41 [Tab 9].

in the ordinary course of business during the initial stay of proceedings.[31] What is "reasonably necessary" depends on the facts of each case.[32]

60. In this case, the Applicants submit that it is appropriate for this Court to exercise its discretion to approve the Interim Lender's Charge because:

    i. the Applicant will not have sufficient funds to proceed through the CCAA proceedings without drawing on the Interim Financing;[33]

    ii. the relatively recent negotiation and contemplation of the secured 1903 Credit Agreement obviates the need for a new interim financing agreement;

    iii. no creditors will be prejudiced ;and

    iv. the Monitor supports the amount of Interim Financing and the Interim Lender's Charge.

61. Further, there is precedent There is precedent for the relief sought by the Applicants in respect of the Interim Lender's Charge. Specifically, in *Re Comark Inc*, the Court approved an interim financing facility pursuant to which the company was required to deposit all cash from operations into a blocked account to pay down the pre-filing revolver facility.[34] The Court recognized that it was cash generated from Comark's post-filing operations that was being used to reduce the pre-filing indebtedness, however, the interim financing charge was found not to be securing any pre-filing obligations.[35]

62. In *Re Performance Sport Group Ltd*., the Ontario Superior Court noted that:

> Section 11.2(1) of the CCAA provides that security for a DIP facility may not secure an obligation that existed before the order authorizing the security was made. The effect of this provision is that advances under a DIP facility may not be used to repay pre-filing obligations. In this case, the ABL DIP Facility is a revolving facility. Under its terms, receipts from operations of the PSG Entities post-filing may be used to pay down the existing ABL Facility. The applicants submit that in this case, the ABL DIP Facility preserves the pre-filing status quo by upholding the relative pre-stay priority position of each secured creditor. By requiring that the PSG Entities only use post-filing cash receipts to pay down the accrued balance under the revolving credit facility, the ABL DIP Lenders are in no better position with respect to the priority of their pre-filing debt relative to other creditors. I accept that no advances under the ABL DIP Facility will be used to pay prefiling obligations.[36]

63. Pursuant to the above, the Applicants submit that the Interim Lender's Charge is required and reasonable in the circumstances.

iii. D&O Charge

64. The Applicants seek approval of a charge for $5,000,000 for continued involvement and assistance of the Applicants' directors and officers (the **D&O Charge**).

65. Under section 11.51 of the CCAA, the Court may grant a charge in favour of directors and officers in an amount the Court considers appropriate. The purpose of the D&O Charge is to

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[31] *CCAA* at s. 11.2(5)
[32] *8440522 Canada Inc., Re*, 2013 ONSC 6167 at para 30.
[33] Anderson Affidavit at paras 68-70.
[34] *Re Comark Inc,* 2015 ONSC 2010 at para 19 [***Comark***].
[35] *Ibid* at para 28.
[36] *Re Performance Sports Group Ltd*., 2016 ONSC 6800 at para 22.

indemnify directors and officers against any obligations or liabilities that may arise after the Initial Order is granted, thereby retaining the directors and officers "in place" in order to avoid destabilization and assist with the restructuring.[37]

66. Section 11.51(4) of the CCAA provides that any D&O Charge cannot apply to liabilities arising from gross negligence or wilful misconduct. This caveat is reflected in the Alberta Template CCAA Initial Order and was not modified in the Applicants' proposed form of Initial Order.

67. In addition, the Alberta Template CCAA Initial Order contemplates a directors and officers charge that does not duplicate coverage already provided by directors and officers insurance. This was not modified in the Applicants' proposed form of Initial Order.

68. In this case, a successful restructuring of the Peavey Group's business and affairs requires the continued participation of the directors and officers. These individuals have significant institutional knowledge and expertise that cannot be replicated, and they have a history of responsibility for key stakeholder relationships.

69. The proposed quantum of the D&O Charge, in the amount of $2,500,000, reflects the significant breadth of operations of the Peavey Group across Canada, including the significant number of employees, and is reasonable in the circumstances. The proposed Monitor has advised in its Pre-Filing Report that such quantum is appropriate.

70. The Peavey Group's most significant secured creditors are the Lenders under the 1903 Credit Agreement, which creditors have been given notice of the Charges. The proposed Initial Order states that the Charges do not take priority to any secured creditors pursuant to a lease or purchase money security interest that have not been served with the Initial Application materials.

71. Given the above, the Applicants respectfully submit that all three of the Charges for which approval is sought is reasonable and appropriate in the circumstances.

CONCLUSION

72. In conclusion, and in consideration of the foregoing, the Applicants respectfully request that this Honourable Court grant the Initial Order in the form attached to the Application.

ALL OF WHICH IS RESPECTFULLY SUBMITTED THIS 27 DAY OF January 2025:

Norton Rose Fulbright Canada LLP

Per: _____

Howard A. Gorman, KC, D. Aaron Stephenson
and Meghan L. Parker
Counsel for the Applicants

[37] *Canwest Global Communications Corp (Re),* 2009 CanLII 55114 (ON SC) at para 48.

TABLE OF AUTHORITIES

Tab 11

2015 ONSC 2010
Ontario Superior Court of Justice

Comark Inc., Re

2015 CarswellOnt 20810, 2015 ONSC 2010, 266 A.C.W.S. (3d) 541

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

In the Matter of a Proposed Plan of Compromise or Arrangement of Comark Inc.

G.B. Morawetz R.S.J.

Heard: March 26, 2015
Judgment: March 26, 2015
Docket: CV-15-10920-00CL

Counsel: Marc Wasserman, Caitlin Fell, for Applicant
Brian Empey, Ryan Baulke, for Proposed Monitor, Alvarez & Marsal Canada Inc.
Sam Babe, for Salus Capital Partners, LLC (DIP Lender)

Subject: Insolvency

Headnote

Bankruptcy and insolvency --- Companies' Creditors Arrangement Act — Arrangements — Approval by court — Miscellaneous

Applicant company operated 343 retail stores across Canada and had experienced declining financial results over past two years — Applicant had $112.3 million assets and $126.1 million liabilities and was financed through term loan and revolving credit facilities — Applicant was noted in default of credit agreement, so creditor made demand for repayment, which applicant was unable to make and was thus insolvent — Applicant sought initial order to provide it with breathing space to restructure and reorganize business and preserve enterprise of value — Creditor who provided revolving credit facilities had agreed to act as DIP lender, and applicant proposed $28 million draft initial order with restriction on borrowing $15 million prior to comeback hearing — Monitor stated applicant could not continue to operate without DIP facility and recommended court approve it — Company brought application for initial order under Companies' Creditors Arrangements Act — Application granted — Monitor's submissions, specifically its view the form of DIP financing did not contravene Act, were accepted — Company met definition of debtor company under Act, claims well exceeded $5 million and it was insolvent — Company was entitled to stay pursuant to s. 11.02 and DOP financing and key employee retention policy approved — Potential exposure of directors was $7.15 million, so $3 million directors' charge was necessary and appropriate — Pre-filing payments to supplier's authorized, and applicant entitled to pay donations from customers to charities for which they were intended, despite comingling with applicant's other funds.

APPLICATION by company for initial order under Companies' Creditors Arrangements Act.

***G.B. Morawetz R.S.J.*:**

1 The Applicant, Comark Inc. ("Comark"), brings this application for relief under the *Companies' Creditors Arrangement Act* ("CCAA").

2 Comark operates 343 retail stores across Canada under three distinct divisions: Ricki's, Bootlegger and Cleo (together, the "Banners"). Comark sells predominantly exclusive private label merchandise. Comark employs approximately 3,400 people.

3 Comark is a privately held corporation that is a portfolio company of an investment fund managed by KarpReilly LLC ("KarpReilly"). Comark's corporate headquarters are in Mississauga, Ontario (the "Corporate Headquarters") and employ 83 full time employees. Comark operates an essential distribution centre in Laval, Quebec, which employs approximately 200 people and processes approximately 9.3 million and 2 million units of merchandise each year for stores and online sales, respectively.

4 Comark has over 300 product suppliers, primarily located in Asia and North America. Approximately 80% of Comark's unit purchases were sourced from foreign manufacturers and the remaining 20% were sourced in North America. Purchases are typically made in US dollars.

5 Comark transports all products to its stores through third party transportation companies. Purolator is Comark's primary third party transportation provider. The Applicant is of the view that Purolator's continued services are critical to the company's ongoing operations. Approximately 90% of Comark's products are transported using Purolator.

6 Comark has over 60 third party landlords from which it leases all of its retail and distribution locations. As part of its restructuring under these proceedings, Comark anticipates that it will disclaim certain leases in respect of Comark stores.

7 Comark participates in co-brand community events and cause marketing with charitable organizations. Comark customers have donated amounts intended for various charities, and these donated funds are currently comingled with Comark's other funds. As of March 17, 2015, Ricki's has (Cdn.) $40,057, Bootlegger has (Cdn.) $108 and Cleo has (Cdn.) $107,917 in funds received from customers in respect of donations to various charitable organizations.

8 Comark has experienced declining financial results over the past two years.

9 As of February 28, 2015, Comark had total assets of (Cdn.) $112.4 million and its total indebtedness was approximately (Cdn.) $126.1 million.

10 Comark is financed primarily through a term loan and revolving credit facilities under a credit agreement dated as of October 31, 2014 between Comark, as the lead borrower, and Salus, as administrative collateral agent and lender thereto (the "Salus Credit Agreement").

11 As of March 17, 2015, the Applicant reports that there was approximately U.S.$43.1 million outstanding under the term loan facility and (Cdn.) $24.8 million outstanding under the revolving credit facility (the "Revolving Credit Facility"). The Salus Credit Agreement has a maturity date of October 31, 2018. All of the obligations of Comark under the Salus Credit Agreement are secured by all of Comark's assets.

12 Comark has been noted in default of the Agreement and Salus has made a demand for repayment. Comark advises that it is not able to repay its debt obligations to Salus.

13 Comark reports that its adjusted EBITDA fell to approximately (Cdn.) $16.5 million for the year end February 28, 2015. Comark acknowledges that this constitutes an event of default under the Salus Credit Agreement. On the occurrence of an event of default, Salus has the right to terminate the Salus Credit Agreement and declare that all obligations under it are due and payable with presentment, demand, protest or other notice of any kind.

14 Salus delivered a Reservation of Rights Letter on March 5, 2015. On March 25, 2015, Salus made a demand for repayment for all amounts owing under the Salus Credit Agreement. Comark acknowledges that it is not able to pay the full amount owing under the Salus Credit Agreement, which has become immediately due and payable as a result of the event of default and the demand made by Salus. Comark acknowledges that it is insolvent.

15 The Applicant seeks the granting of an initial order. With the benefit of the protection of the stay of proceedings, Comark is of the view that it will be provided with the necessary "breathing space" in order to allow it to develop a plan to restructure and reorganize the business and preserve enterprise of value.

16 Comark is of the view that it requires interim financing for working capital and general corporate purposes and for post-filing expenses and costs during the CCAA proceedings.

17 Salus has agreed to act as DIP lender (the "DIP Lender") and provide an interim financing facility (the "DIP Facility") under an amended and restated credit agreement with Salus (the "DIP Agreement"). It is a condition of the DIP Agreement that advances made to Comark be secured by a court ordered security interest, lien and charge over all of the assets and undertakings of Comark (the "DIP Lender's Charge").

18 The Applicant advises that under the draft initial order, the charges, including the DIP Lender's Charge, do not prime TD Bank and creditors with a purchase money security interest, which are Comark's only secured creditors. Further, the company advises that it is also an express term of the DIP Agreement that advances made thereunder may not be used to satisfy pre-filing obligations under the Salus Credit Agreement. Further, the company states that the DIP Lender's Charge will not secure any obligation that exists before the date of the initial order.

19 It is anticipated that the proceeds from Comark's operations will be used to reduce pre-filing obligations outstanding under the Salus Revolver Facility in order to free-up availability under the DIP Facility. In accordance with the DIP Facility and the current cash management system in effect, Comark's cash from business operations will be deposited into the blocked account and swept by Salus in order to reduce amounts outstanding under the Salus Revolver Facility prior to the commencement of these proceedings.

20 In his supplementary affidavit, Mr. Bachynski states that Comark requires $15 million during the week ending April 11, 2015 and as such, Comark is proposing a maximum DIP Charge of (Cdn.) $28 in the draft initial order with a restriction on borrowing of (Cdn.) $15 million prior to the proposed comeback hearing scheduled for April 7, 2015.

21 Mr. Bachynski goes on to state that Comark will not be able to satisfy its ordinary course obligations in the CCAA proceedings without the DIP Facility.

22 In its pre-filing report, the Monitor reports at length on the debtor-in-possession financing. In its report, the Monitor states that Salus has exercised cash dominion pursuant to the Blocked Account Agreement and the Salus Credit Agreement and has made demand under the Salus Credit Agreement. As a consequence, the Monitor states that Comark does not have access to liquidity to discharge its financial obligations. Further, given the deterioration in the Applicant's financial position and its current liquidity crisis, the Monitor states that the Applicant cannot continue to operate without the DIP Facility.

23 The Monitor also advises that senior management and the Applicant's advisors believe that the DIP Facility is the only realistic source of funding available, given the urgency of the proposed filing, the position of the lender in the capital structure of the Applicant and the minimal level of Comark's existing cash on hand.

24 At section 9.5 of this report, the Monitor summarizes the DIP Facility Terms. This chart is reproduced below.

Comark
Summary of DIP Facility Terms

Total Availability	• The lesser of: (a) the Maximum Amount of $32 million, (b) the Borrowing Base, or (c) extensions of credit required under and set out in the Budget, plus outstanding principal amount of pre-filing Revolving Credit Facility.
Effective Date	• Date of the Initial Order
Purpose/Permitted Payments	• Limited to amounts set out in the Restructuring Plan and the Budget approved by Salus.
Significant Terms	• Initial Order must be granted and issued and provide for a DIP Lender's Charge; • The establishment of a cash flow budget and a restructuring plan that is satisfactory to the DIP Lender; • The DIP Lender shall have received control agreements with respect to the deposit accounts of the Borrower which effectively provides for a sweeping of the Borrower's gross receipts, such collections are to be applied to reduce pre-filing Revolving Credit Facility; and • Other covenants which appear customary under the circumstances.
Fees and Interest	• Interest Rate per annum: LIBOR + 5.75 (as at March 24, 2015 LIBOR was approximately 0.25%; however, the DP Facility contains a LIBOR floor of 1.00%) • Exit fee of 4% of total outstanding borrowing at exit under the DIP, the pre-filing Revolving Credit Facility and the pre-filing Term Loan Facility • Collateral monitoring fee of US$7,000 per month
Security	• All assets and property of the Borrower and DIP Lender's Charge.
Maturity	• The earliest of: (i) completion of a transaction in compliance with the SISP; and (ii) a default.
DIP Lender's Charge	• DIP Lender's Charge to rank subordinate only to the Administration Charge and the Directors' Charge (all further defined herein). DIP Lender's Charge in amount of $32 million to ensure fees, costs and expenses are covered.

25 The DIP Facility contains various affirmative covenants, negative covenants, events of default and conditions that, in the proposed Monitor's view, are reasonable and customary for this type of financing.

26 The Monitor further comments that the DIP Facility is not a new facility layered on top of the pre-filing credit facilities, rather it is an amended version of the pre-filing Salus Credit Agreement pursuant to which Salus would be prepared to commence to provide liquidity, despite the prior default. Importantly, the Monitor comments that ultimately, the DIP Facility will not result in a greater level of secured debt than was contemplated under the pre-filing facilities (absent the default that occurred). Furthermore, the Monitor reports that as there is no indication of any deficiencies with Salus' security package, and the Applicant has advised that it does not intend that the DIP Lender's Charge prime any other secured party's purchase money security interests or statutory deemed trusts, the fact that the DIP Lender's Charge will increase while the pre-filing Revolving Credit Facility would be paid down, should have no negative impact on the other stakeholders.

27 The proposed Monitor recommends that the Court approve the DIP Facility. In arriving at this recommendation, the proposed Monitor considered:

(i) the facts and circumstances of the Applicant;

(ii) section 11.2(4) of the CCAA;

(iii) the financial terms of the DIP Facility relative to comparable facilities and the fact that it is the only realistic source of funding available given the urgency of the proposed filing, the prominent position of the Lender in the capital structure of the Applicant and the minimal level of Comark's existing cash on hand;

(iv) the stability and flexibility of the DIP Facility will provide to ensure there is sufficient liquidity to facilitate the CCAA proceedings and a Sale and Investment Facilitation Process ("SISP"), to maximize realization; and

(v) the interests of the Applicant's stakeholders.

28 In providing its recommendation, the proposed Monitor specifically stated that it has considered the provisions of section 11.2(1) of the CCAA which prohibit the DIP Lender's Charge from securing an obligation that exists before the requested order is made. The Monitor reports that having consulted with its counsel, it is of the view that since the pre-filing Revolving Credit Facility is being reduced by the use of the Applicant's cash generated from its business, the DIP Lender's Charge is only securing advances made post-filing under the DIP Facility.

29 For the purposes of this application, I accept the foregoing submissions and recommendation of the Monitor and, specifically, its view that the form of DIP Facility being proposed, does not contravene the provisions of section 11.2(1) of the CCAA.

30 Comark proposes a key employee retention plan (the "KERP") for certain employees (the "Key Employees") which Comark considers critical to a successful proceeding under the CCAA. Key Employees include certain key senior management employees, both at the Corporate Headquarters and Banner level that possess unique professional skills and experience with Comark's business and operations.

31 The proposed Monitor agrees that the KERP is reasonable in the circumstances.

32 The Applicant has retained Houlihan Lokey Capital, Inc. as financial advisor (the "Financial Advisor") to advise on a possible restructuring, refinancing or sale for Comark.

33 The Applicant also reports that it has worked with the Financial Advisor, in consultation with the proposed Monitor and Salus, to develop the Sale and Investor Solicitation Process ("SISP"). The purpose of the SISP is to solicit and assess available opportunities for the acquisition of or investment in Comark's business and property.

34 In its factum, the Applicant submits that the application addresses the following issues:

(a) the Applicant's entitlement to seek protection under the CCAA;

(b) the Applicant's entitlement to a stay of proceedings;

(c) the granting of the DIP Lender's Charge on a priority basis over the property and approval of the DIP Facility;

(d) the approval of the KERP and KERP Charge;

(e) the sealing of the KERP Schedule;

(f) the granting of the Director's Charge on a priority basis over the property;

(g) the approval of pre-filing payments to "critical" suppliers and to certain charitable organizations to which Comark's customers donated funds; and

(h) the approval of the SISP.

35 I am satisfied that Comark meets the definition of "debtor company" under the CCAA. It is a corporation incorporated under the *Canada Business Corporations Act*.

36 I am also satisfied that the total claims against Comark far exceed $5 million and that Comark is insolvent.

37 In arriving at the conclusion that Comark is insolvent, I have taken into account that, as a result of the event of default and the acceleration of all amounts due under the Salus Credit Agreement, it is apparent that Comark does not have sufficient liquidity to satisfy its liabilities as they become due.

38 The required financial statements and cash-flow statements are included in the record.

39 I am also satisfied that the Applicant is entitled to a stay of proceedings pursuant to section 11.02 of the CCAA.

40 With respect to the request to approve the DIP Facility and to grant a DIP Financing Charge on a priority basis, the authority to approve same is found in section 11.2 of the CCAA. In its factum, the Applicant specifically references section 11.2(1) and submits that it is clear on the facts that the DIP Lender's Charge meets this requirement. Counsel submits that the DIP Facility expressly provides that Comark may not use any advances under the DIP Facility to repay pre-filing obligations. Counsel goes on to state that to the extent that Salus is repaid pre-filing amounts owing to it, this repayment will be made from operational receipts as a result of lending, security and enforcement arrangements in place prior to the CCAA filing. Further, the repayment is not made out of proceeds of the DIP Facility. Rather, the payments to Salus simply maintain the status quo as of the CCAA filing date under the existing Salus asset-based lending credit facility.

41 For the purposes of this application, I accept the submissions of the Applicant and recommendations of the Monitor and have concluded that the DIP Facility should be approved and the Court should grant the DIP Lender's Charge to a maximum DIP Charge of (Cdn.) $28 million with a restriction on borrowing of (Cdn.) $15 million up to April 7, 2015.

42 Counsel to the Applicant requests approval of the KERP and the KERP Charge. Submissions in support of this request are made at paragraphs 26 - 32 of the Amended Factum. I accept these submissions and approve the KERP and the granting of the KERP Charge.

43 Insofar as the KERP Schedule contains confidential personal information, the Applicant seeks a sealing of the KERP Schedule. The Applicant references *Sierra Club of Canada v. Canada (Minister of Finance)*, 2002 SCC 41 (S.C.C.), in support of its request to seal the Schedule.

44 I am satisfied, having considered the *Sierra Club* principles, that it is appropriate to seal the confidential KERP Schedule.

45 The Applicant also seeks a Directors Charge in the amount of up to (Cdn.) $3 million, to act as security for indemnification obligations for Comark's directors' potential liabilities. It is contemplated that the Directors Charge would stand in priority to the proposed DIP Charge, but subordinate to the proposed Administration Charge.

46 Pursuant to section 11.51 of the CCAA, the Court has authority to grant a "super priority" charge to the Directors and Officers as security for the indemnity. The factors to be considered on such a request were set out by Pepall J. (as she then was) in *Canwest Global Communications Corp., Re*, [2009] O.J. No. 4286 (Ont. S.C.J. [Commercial List]).

47 Comark has estimated the potential exposure of the Directors and Officers for unpaid statutory amounts, including wages, unremitted source deductions, vacation pay, sales and service taxes, termination pay, employee health tax and unpaid workers' compensation to be approximately (Cdn.) $7.15 million.

48 I accept the submissions of the Applicant and have concluded that the Directors Charge is necessary and appropriate and is granted in the requested amount.

49 The Applicant also requests authorization to make certain pre-filing payments, specifically to critical suppliers.

50 The argument in support of the granting of this request is set out in the Amended Factum at paragraphs 44 - 52. I accept these submissions and concluded that it is appropriate to authorize Comark to make the pre-filing payments. 1 note that the Monitor will be involved in this process and that the consent of the Monitor to make such payments is required.

51 I have also been persuaded that it is appropriate for the Court to exercise its jurisdiction to authorize Comark to pay certain amounts that were donated by Comark's customers to the charitable organizations for which the amounts were intended. This authorization is made notwithstanding that the donated amounts are currently comingled with Comark's other funds.

52 The Applicant also requests approval of the SISP for the reasons set out at paragraphs 54 - 59 of the Amended Factum. I accept these submissions and authorize and approve the SISP.

53 This application was brought without notice to the creditors of Comark, with the exception of Salus. As such, I treat it as an *ex parte* application.

54 The requested relief is granted and the order has been signed to reflect the foregoing.

55 A come-back hearing has been scheduled for April 7, 2015. A further hearing has been scheduled for April 21, 2015.

56 The come-back hearing is to be neutral in all respects.

57 The stay of proceedings is in effect up to and including April 24, 2015, or such later date as the Court may order.

Application granted.

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