TAB 5

[Indexed as: **Morneau Sobeco Ltd. Partnership v. Aon Consulting Inc.**]

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 Slater Steel Inc., Slater Stainless Corp., Sorel Forge Inc., 833840 Ontario Inc., 1124207 Ontario Inc. and 3014063 Nova Scotia Company (Applicants)

And In the Matter of Section 18.6 of the Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36, as amended

And In the Matter of Slater Steel Corporation

Morneau Sobeco Limited Partnership by its general partner Morneau Sobeco Corporation (Plaintiff / Respondent) and Aon Consulting Inc. and J. Melvin Norton (Defendants / Appellants)

Ontario Court of Appeal

D. O'Connor A.C.J.O., E.E. Gillese, P. Rouleau JJ.A.

Heard: February 21, 2008

Judgment: March 19, 2008

Docket: CA C47155, C47235, 2008 ONCA 196

Ian Dick, Elizabeth Brown for Appellant, J. Melvin Norton
Barry Bresner, Markus Kremer for Appellant, Aon Consulting Inc.
Edward Babin, Jim Bunting for Proposed Third Parties
A.J. Esterbauer for Plaintiff, Morneau Sobeco Limited Partnership by its General Partner, Morneau Sobeco Corporation
Michael McGraw for Monitor
Deborah McPhail for Superintendent of Financial Services

Civil practice and procedure — Third party procedure — Practice — Instituting third party proceedings — Third party notice or claim — Corporation was administrator of pension plans for its employees — Defendants served as advisors in administration of plans — Third parties were individuals working for corporation who were given responsibility by corporation for management of plans — Corporation was placed into receivership — Plaintiff was named new administrator of plans — Plaintiff alleged large deficit existed in plans as result of defendants' poor advice to corporation — Plaintiff brought action against defendants for damages arising out of deficiency in plan assets — Defendants' motions for leave to issue claims against third parties were dismissed, and plaintiff's cross-motion to strike proposed third party claims as disclosing no reasonable cause of action was dismissed — Defendants appealed and plaintiff brought motion to quash appeals on basis leave to appeal was necessary — Appeal allowed and motion dismissed — Orders were set aside and defendants were permitted to initiate third party

claims — It was not plain and obvious that proposed third party claims could not succeed — Orders made under Companies' Creditors Arrangement Act did not preclude issuance of proposed third party claims — Claims were not barred by Termination Order.

Pensions — Practice in pension actions — Parties — Corporation was administrator of pension plans for its employees — Defendants served as advisors in administration of plans — Third parties were individuals working for corporation who were given responsibility by corporation for management of plans — Corporation was placed into receivership — Plaintiff was named new administrator of plans — Plaintiff alleged large deficit existed in plans as result of defendants' poor advice to corporation — Plaintiff brought action against defendants for damages arising out of deficiency in plan assets — Defendants' motions for leave to issue claims against third parties were dismissed, and plaintiff's cross-motion to strike proposed third party claims as disclosing no reasonable cause of action was dismissed — Defendants appealed and plaintiff brought motion to quash appeals on basis leave to appeal was necessary — Appeal allowed and motion dismissed — Orders were set aside and defendants were permitted to initiate third party claims — It was not plain and obvious that proposed third party claims could not succeed — Orders made under Companies' Creditors Arrangement Act did not preclude issuance of proposed third party claims — Claims were not barred by Termination Order.

Statutes considered:

Bankruptcy and Insolvency Act, R.S.C. 1985, c. B-3
Generally — referred to
Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36
Generally — referred to
Pension Benefits Act, R.S.O. 1990, c. P.8
Generally — referred to
s. 109(1) — considered
s. 110(2) — considered

Rules considered:

Rules of Civil Procedure, R.R.O. 1990, Reg. 194
R. 21.01(1)(b) — considered

Regulations considered:

Pension Benefits Act, R.S.O. 1990, c. P.8
General, R.R.O. 1990, Reg. 909
Generally — referred to

APPEAL by defendants from judgment reported at *Morneau Sobeco Ltd. Partnership v. Aon Consulting Inc.* (2007), 59 C.C.P.B. 286, [2007] O.J. No. 1455, 2007 CarswellOnt 2234 (Ont. S.C.J.), dismissing defendants' motion for leave to issue claims against third parties; MOTION by plaintiff to quash appeals.

E.E. Gillese J.A.:

1 These appeals involve the alleged underfunding of two pension plans. They raise a question that sounds more like a riddle than a legal question: when are

directors and officers *not* directors and officers? The question is complicated by the fact that it arises in largely uncharted legal waters — a lawsuit brought by a successor pension plan administrator.

Background

2 Slater Stainless Corp. was the sponsor and administrator of certain pension plans (the "Plans"). J. Melvin Norton was the Plans' actuary at the relevant times and Aon Consulting Inc. was his employer.

3 By order dated June 2, 2003 (the "Initial Order"), Slater was granted protection under the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36 (the "*CCAA*").

4 Prior to the making of the Initial Order, Slater had dealings with the Superintendent of Financial Services (the "Superintendent") and the Financial Services Commission ("FSCO") over alleged improprieties in the Plans' actuarial reports which had been prepared by Norton.

5 In the Initial Order, a charge of up to $17.5 million (the "D&O Charge") was made against the Slater property to indemnify the Slater directors and officers for claims that might be asserted against them (the "D&O Claims"). A process to resolve claims against the directors and officers (the "Claims Bar Process") was established by order dated April 30, 2004 (the "Claims Bar Order"). The Claims Bar Order also provided that Slater's directors and officers would be released from all claims for which the directors and officers were liable in their capacity as such and for which no claims notices had been filed by the deadline.

6 The Superintendent filed a D&O Claim (the "FSCO Claim") in which it set out a number of regulatory and compliance issues in relation to Slater's administration of the Plans. One aspect of the FSCO Claim related to the asset valuation methods adopted in the actuarial valuation reports that Slater had filed with FSCO. The reports were said to have contravened the requirements of the *Pension Benefits Act*, R.S.O. 1990, c. P.8 (the "*PBA*") and *Regulation 909*, R.R.O. 1990. It was alleged that had proper reports been filed, Slater would have been required to make additional contributions to the Plans, thereby reducing or eliminating the alleged deficits in the Plans. Pursuant to s. 109(1) of the *PBA*, the alleged contraventions constitute an offence.

7 The FSCO Claim asserted, pursuant to s. 110(2) of the *PBA*, that the Slater directors and officers were also guilty of offences under the *PBA* because they "caused, authorised, permitted, acquiesced or participated in" Slater's various contraventions and failed to take reasonable care to prevent Slater from committing the contraventions.

8 The FSCO Claim sought a fine of $100,000 against the directors and officers for the alleged offences. It also sought an order that the directors and officers pay $18 million plus interest into the Plans, that being the amount of the unremitted contributions to the Plans.

9 The *CCAA* proceedings were unsuccessful in that no plan of compromise or arrangement was reached. By order dated August 30, 2004, the *CCAA* proceedings were terminated (the "Termination Order"). Pursuant to a further order made that day under the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3, Slater was put into receivership. The Termination Order ended the provisions in the Initial Order that had granted Slater creditor protection. However, it allowed the Claims Bar Process to continue for certain claims already underway.

10 The FSCO Claim was settled. By order dated December 9, 2004, the settlement was approved in the *CCAA* proceedings (the "Settlement Order"). The Settlement Order required the receiver for Slater to pay $100,000 to FSCO from Slater's operating reserve, in lieu of a fine under the *PBA*. As well, judgment against Slater was ordered for the lesser of $18.3 million or the deficiencies in the Plans. The judgment had the status of an unsecured judgment; there are no funds available for distribution to Slater's unsecured creditors.[1]

11 On September 8, 2004, the Superintendent appointed Morneau Sobeco Limited Partnership as the successor administrator of the Plans.

12 On November 18, 2005, Morneau brought an action against Norton and Aon in which it claimed damages of $20 million, the amount by which the Plans are underfunded as a result of the allegedly improper actuarial reports prepared by Norton. The Morneau action relates to the same actuarial reports and deficiencies as were the subject of the FSCO Claim and the Settlement Order. The Morneau action alleges, among other things, that Norton breached the duties he owed to the Plans' members and beneficiaries by preparing actuarial valuations that overstated the value of the Plans' assets and enabled Slater to avoid making additional contributions to the Plans before becoming insolvent.

13 Aon and Norton each sought to institute third party proceedings (the "Proposed Third Party Claims") against certain individuals (the "Slater Personnel"). The Slater Personnel are former directors, officers or employees of Slater or a related corporation, Slater Stainless Inc., who served on Slater's Audit Committee. Slater, as administrator of the Plans, had given the Audit Committee responsibility for management and administration of the Plans. Consequently, the members of the Audit Committee performed Slater's duties as the Plan administrator at the relevant times.

14 In the Proposed Third Party Claims, Aon and Norton seek to claim against the Slater Personnel on the basis that the Slater Personnel, as employees or agents of Slater, were the governing mind of Slater *qua* administrator and caused or contributed to the alleged deficit. Aon and Norton rely on their statu-

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[1]Para. 24 of the Monitor's Nineteenth and Final Report to the Court dated August 17, 2006.

tory and common law rights to seek contribution and indemnity from the Slater Personnel for any liability they are found to have in the Morneau action.

15 The Proposed Third Party Claims allege that the Slater Personnel, in their capacity as agents or employees of the administrator, acted negligently and in breach of statutory and fiduciary duties, induced or committed breaches of fiduciary duty, placed themselves in a position of conflict of interest and engaged in wilful misconduct. The allegations include that the Slater Personnel followed a deliberate strategy to minimize the contributions that Slater would be required to make to the Plans when they knew, or ought to have known, that Slater was insolvent or on the brink of insolvency. This strategy allegedly included instructing Norton to prepare the solvency valuation using an asset "smoothing" method that adjusted the value attributed to the Plans' assets, without disclosing to Norton or Aon that there were doubts as to whether Slater would remain a going concern. The strategy also allegedly included instructions by the Slater Personnel to Norton in his dealings with the Superintendent and deliberately delaying the proceedings with FSCO in order to avoid having Slater make pension plan contributions prior to seeking protection from its creditors.

16 The Slater Personnel objected to the issuance of the Proposed Third Party Claims. They maintained that the *CCAA* orders prevented such claims from being brought. In particular, they relied on paras. 15 and 16 of the Termination Order. Those paragraphs read as follows:

> 15. THIS COURT ORDERS that any person who served as an officer or director of any of the Applicants prior to and from and after June 2, 2003 is hereby released, remised and forever discharged of and from all claims, liabilities, obligations, demands or causes of action of whatever nature, including, without limitation, any and all claims in respect of potential statutory liabilities, whether known or unknown, matured or unmatured, foreseen or unforeseen, existing or hereafter arising by reason of, out of or in connection with, such service with respect to any act or omission, transaction or dealing or other occurrence existing or taking place prior to the date of this Order, and including any claim or demand for contribution or indemnity in respect of any act or omission, transaction or dealing or other occurrence which occurred in whole or in part prior to the date of this Order, provided that this paragraph shall not extend to any person that actively and knowingly participated in the breach of any related fiduciary duties or has been grossly negligent or guilty of wilful misconduct and provided that this paragraph shall be without prejudice to the rights of any person whose claim against such directors and officers has been allowed, partially allowed or is being disputed in accordance with the Claims Bar Order.
>
> 16. THIS COURT ORDERS that, until further order of this Court, any and all persons shall be and are hereby stayed from commencing, taking, applying for or issuing or continuing any and all steps or proceedings, including, without limitation, administrative hearings or orders, declarations or assessments, against any or all past, present or future directors or officers of any of

> the Applicants in respect of any matters referred to in paragraph 15 above, save and except claims brought in accordance with the procedures contained in the Claims Bar Order.

17 Aon and Norton brought motions for declarations that the *CCAA* orders did not apply or, alternatively, for leave to bring their claims (the "Underlying Motions"). The Slater Personnel brought a cross-motion for an order striking the Proposed Third Party Claims as disclosing no reasonable cause of action.

18 In two orders, both of which are dated April 13, 2007, Spence J. dismissed the Underlying Motions and the cross-motion (the "Orders"). He was of the view that the determinative issue on the Underlying Motions and the cross-motion was whether the Proposed Third Party Claims disclosed a "proper cause of action". He held that they did not. Having decided the Underlying Motions and cross-motion on that basis, the motions judge did not address the *CCAA* issues.

19 Aon and Norton appeal. The Slater Personnel bring a motion to quash the appeals, contending that the Orders are decisions made under the *CCAA* and, thus, leave to appeal the Orders is necessary. They submit that as Aon and Norton did not seek leave to appeal the Orders, the appeals are not properly before this Court and should be quashed.

20 For the reasons that follow, I would dismiss the motion to quash and allow the appeals.

The Issues

21 In effect, the motion judge struck the Proposed Third Party Claims on the basis that they failed to disclose a reasonable cause of action. Consequently, to decide these appeals, two issues must be addressed:

1. Do the Proposed Third Party Claims disclose a reasonable cause of action?
2. If so, are they precluded by the *CCAA* orders?

The Proposed Third Party Claims

22 There is no dispute about the principles that apply on a motion to strike pleadings for failure to disclose a reasonable cause of action pursuant to rule 21.01(1)(b) of the *Rules of Civil Procedure*, R.R.O. 1990, Reg. 194. The claim is to be read generously, with allowance for inadequacies in drafting; the material facts pleaded are to be taken as true unless they are patently ridiculous or incapable of proof; and, the threshold is a high one as pleadings are to be struck only in the clearest of cases. Put another way, for the Proposed Third Party Claims to be struck on the basis they did not disclose a reasonable cause of action, the motions judge had to have concluded that it was "plain, obvious and beyond doubt" that Aon and Norton could not succeed in the claims they advanced in those pleadings.

23 In my view, it was an error for the motions judge to have reached this conclusion.

24 I understand the chain of reasoning behind the motions judge's determination that the Proposed Third Party Claims are "fundamentally defective" to be as follows.

- Aon and Norton can be held liable in the Morneau action only if they are found to have caused the Plans to suffer damage. In order to find that Aon and Norton caused the Plans to suffer damage, the court must find that Slater[2] reasonably relied on advice provided by Aon and Norton, and that the advice fell below the requisite standard of care.
- Aon and Norton have defended the Morneau action on the basis that Slater did not rely on their advice. That is, Aon and Norton defend on the basis that even if they were negligent in the preparation of the actuarial reports, it was not their negligence which caused damage. Rather, it was the improper actions of Slater that caused the Plans to suffer harm.
- If Aon and Norton succeed in convincing the court that Slater did not rely on their advice when deciding how much to contribute to the Plans, reasonable reliance on the part of the Slater will not be established. If there is no reasonable reliance, there can be no loss as a consequence of the advice, even if the advice is found to have fallen below the requisite standard. The Morneau action would fail and there would be no liability on the part of Aon and Norton. If there is no liability on the part of Aon and Norton, there is no basis on which to seek a finding of concurrent liability on the part of the Slater Personnel.
- If, however, there was reasonable reliance on the part of the Slater, then the Proposed Third Party Claims cannot succeed. That is because the Proposed Third Party Claims are based on the allegation that the Slater Personnel caused the damage. It is not possible to find both that Slater reasonably relied on Aon and Norton's advice and that Slater caused the damage.
- Consequently, the Proposed Third Party Claims were not proper claims for contribution and indemnity.

25 The motions judge erred in assuming that in order for the Morneau action to succeed, reasonable reliance on the part of Slater must be proven. The erroneous assumption flows from a failure to distinguish between Morneau's role as a successor administrator and Slater's role as the Plans' administrator, and to understand the true nature of the claims asserted.

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[2]The motions judge treats Slater and the Slater Personnel as interchangeable. For ease of reference, when summarizing the motions judge's reasoning, when I refer to Slater, it encompasses both.

26 If Slater had sued Aon and Norton, depending on the nature of the claim asserted, reasonable reliance might have been necessary for success.[3] But, it is not Slater that is suing. It is Morneau that is suing. Morneau may, as the successor plan administrator, pursue any claims that Slater might have taken. In addition, however, Morneau has the right to bring suit on behalf of the Plans' beneficiaries. Fundamentally, it is the latter which lies at the heart of the Morneau claim. The Morneau claim is asserted on behalf of the Plans' members and beneficiaries, the people who suffered or will suffer as a result of the underfunding of the Plans due to the allegedly negligent preparation of the solvency valuations. The success of the Morneau claim is not dependent on establishing that Slater reasonably relied on the reports. It is dependent on establishing that the allegedly negligent reports played a role in enabling Slater to avoid making the required payments.

27 Further, as the successor administrator, Morneau may sue for redress for acts of improper administration by a prior administrator much in the same way that a subsequent trustee can sue a prior trustee for breach of trust.

28 Moreover, the absence of reasonable reliance is not a complete defence to the Morneau action which asserts a number of other claims, including breach of fiduciary and statutory duties. If relevant at all, reliance is not determinative of those claims.

29 Accordingly, it cannot be said that it is plain and obvious that the Proposed Third Party Claims could not succeed; the cross-motion to strike the claims on that basis must be dismissed.

The Impact of the CCAA *Orders*

30 In my view, the *CCAA* Orders ought not to preclude the issuance of the Proposed Third Party Claims. I come to this view for three reasons:

1) It is not clear to me that the Proposed Third Party Claims are barred by para. 15 of the Termination Order.

2) The bulk of the claims in the Proposed Third Party Claims fall within the "carve-out" in para. 15 and, thus, are not barred.

3) Even if the stay imposed under the *CCAA* Orders applies, the court's discretion should be exercised and the stay lifted.

The Proposed Third Party Claims May Not be Barred

31 Paragraph 15 of the Termination Order protects the directors and officers from claims arising from their service as directors and officers. In the Proposed

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[3]Although I fail to see what damages Slater could sue for: if there was negligence in the preparation of the report, it appears that Slater benefited from it.

Third Party Claims, the Slater Personnel are not being sued in their capacity as directors and officers of Slater. Rather, the claims are made against them as individuals, in their capacity as agents and employees of Slater *qua* administrator.

32 The Slater Personnel argue that they served on the Audit Committee because they were directors and officers.[4] That may be so. However, this argument fails to account for the change in role that took place when the members of the Audit Committee administered the Plans. At that point, the Audit Committee became the agents and employees of the then-administrator of the Plans, Slater.

33 Recognizing the different roles that the Slater Personnel fulfilled while on the Audit Committee makes sense of the inherent conflict of interest that otherwise existed for them. Here is one example of the conflict of interest that would exist if these different roles are conflated. The Audit Committee had to decide how much money Slater would contribute to the Plans annually. If the Slater Personnel, in the guise of the Audit Committee, made that decision in their capacity as directors or officers of Slater, they did so while owing a duty to Slater. Given the financial difficulties that Slater faced, that duty would have led them to minimize the amount that Slater contributed to the Plans.

34 However, when the Audit Committee made decisions on the quantum of Slater's contribution to the Plans, it did so in order to fulfill Slater's obligations as administrator of the Plans. An administrator owes a fiduciary duty to the members of the Plans. The Audit Committee "stood in the shoes" of Slater *qua* administrator when making the decision; therefore, it too owed a fiduciary duty to the Plans' members. Fulfillment of that duty would have led to maximizing the contributions that Slater would make to the Plans as that would best protect the Plans members' pensions. In light of Slater's precarious financial position — a fact that was known or ought to have been known by the Slater Personnel — this duty was heightened because the need for solvency funding should have been apparent.

35 If the Slater Personnel are treated solely as directors and officers, they were in an impossible position. They could not fulfill their duties both to Slater and to the Plans' members. That impossibility is obviated if the roles played by the Slater Personnel are kept separate. Viewed in this way, although the Slater Personnel were appointed to the Audit Committee by virtue of their positions as directors and officers, when making decisions in respect of the Plans' administration they did so as agents and employees of Slater *qua* administrator — not as directors and officers.

36 Accordingly, the Proposed Third Party Claims would not be barred by the *CCAA* orders because those claims do not relate to the Slater Personnel in their roles of directors and officers but, rather, as individuals who were the agents and

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[4]One member of the Slater Personnel, Doug Brown, was neither a director nor officer.

employees of Slater, the Plans' administrator. Consequently, leave would not be necessary to bring the Proposed Third Party Claims and there would be no need to lift the stay.

37 These comments are not intended to be determinative of this issue. They are offered only to explain why I do not view the Proposed Third Party Claims as necessarily within the scope of para. 15 of the Termination Order.

A Majority of Claims in the Proposed Third Party Claims are not Barred

38 Recall the "carve-out" in para. 15 of the Termination Order, which reads as follows:

> ...this paragraph shall not extend to any person that actively and knowingly participated in the breach of any related fiduciary duties or has been grossly negligent or guilty of wilful misconduct ....

39 It can be seen that the carve-out provides that the release in para. 15 does not extend to claims against those who "actively and knowingly" participated in the breach of fiduciary duties or who had been grossly negligent or guilty of wilful misconduct. Many of the allegations in the Proposed Third Party Claims fall within the scope of the carve-out. Consequently, even if the stay otherwise operates, it does not preclude such claims.

Lifting the Stay if Necessary

40 Further, and in any event, I would lift the stay if that were necessary.

41 The Slater Personnel acknowledge that even if the *CCAA* orders otherwise prevent the Proposed Third Party Claims from being initiated, para. 16 of the Termination Order gives this court the power to lift the stay and allow the claims to proceed. They argue that the court should not exercise its discretion because:

1. the allegations in the Proposed Third Party Claims are frivolous, without merit and do not establish a *prima facie* case, and
2. since Slater no longer exists, the directors and officers cannot seek indemnity from it. Whatever claims the directors and officers might have against Slater if the Proposed Third Party Claims are permitted to proceed, in effect, those claims are foreclosed as a result of the *CCAA* orders and the liquidation of Slater's assets.

42 I see no merit in the first objection. As the material facts pleaded in the Proposed Third Party Claims are neither patently ridiculous nor incapable of proof, at this stage they are taken to be true. On that basis, the claims for indemnity and contribution cannot be said to be frivolous or without merit.

43 The second objection is founded on the prejudice that the Slater Personnel may suffer if the stay is lifted. In my view, in considering this objection, the court must balance that prejudice against the prejudice that Aon and Norton may suffer if the stay is not lifted. A weighing of such prejudice leads me to conclude

that the balance is in favour of Aon and Norton and, therefore, in favour of lifting the stay, if that is necessary.

44 If the stay is lifted, the Slater Personnel will face significant financial exposure for conduct that occurred while they were directors and officers of Slater or its affiliates. If they are found liable, they will be unable to seek redress from Slater. On the other hand, Aon and Norton face significant financial exposure in the Morneau action. If the stay is not lifted, they will be unable to claim against the very individuals they say caused or contributed to the damages for which they may be held liable in the Morneau action.

45 If the analysis of prejudice ended there, one might conclude that the balance is roughly even. That, however, would be to ignore the legal proceedings which bring the parties to this point. The Slater Personnel fully participated in the proceedings that now prevent them from looking to Slater for indemnification. Their interests were protected and their voices heard.

46 The same is not true for Aon and Norton. Morneau brought its action against Aon and Norton almost fifteen months after the Termination Order was issued. Aon and Norton had no notice of the *CCAA* proceedings and no opportunity to make submissions in respect of the *CCAA* Orders. They had no knowledge, or means of acquiring knowledge, of any possible claims against them and no ability to assert a D&O Claim. Unlike the Slater Personnel, they were not involved in the FSCO Settlement nor were they given the opportunity to be involved in that process. If the stay is not lifted, Aon and Norton face substantial liability for which they may not claim contribution and indemnity from the very persons whom they say caused the Plans' deficits. Their legitimate claims will have been barred by a process in which they never had the opportunity to participate.

47 In the circumstances, as I have said, the balance is in favour of Aon and Norton. Accordingly, I would lift the stay, if that is necessary.

The Court's Jurisdiction to Make the CCAA Orders

48 Aon and Norton also argue that if the *CCAA* Orders purport to bar actions against the Slater Personnel, they ought to be held to beyond the jurisdiction of the court because the *CCAA* proceedings were terminated and no proposal or compromise had been sanctioned. In light of the conclusions reached above, there is no need to address these jurisdictional arguments.

Disposition

49 Accordingly, if leave to appeal is necessary, I would grant leave. It follows that I would dismiss the motion to quash.

50 I would allow the appeals and set aside the Orders, apart from those parts of the Orders which dismiss the cross-motion. I would grant the Underlying Motions and declare that Aon and Norton may initiate third party claims. Aon's third party claim is to be substantially in the form of its First or Second Pro-

posed Claim. Norton's claim is to be substantially in the form attached to its Notice of Motion. Having said that, Aon and Norton may advance any legal ground available to them — they are not limited to those that fall within the carve-out. I would extend the time for initiating a third party claim to fourteen days from the date of release of these reasons.

51 Aon and Norton are entitled to their costs below and of these appeals from the respondents, the proposed third parties. If those parties are unable to agree on costs, they may make brief written submissions on the same within fifteen days of the date of release of these reasons. I would make no costs order in respect of the plaintiff, the Monitor and the Superintendent.

D. O'Connor A.C.J.O.:

I agree.

P. Rouleau J.A.:

I agree.

Appeal allowed; motion dismissed.

TAB 6

Under the criminal system, everybody is presumed innocent and the accused has no burden to prove anything. Under the civil system of course, the rules are different and merely pleading a defence does not get very far in the civil courts. If there was a jurisdiction to provide the funding requested, obviously the Court would have to deal with those differences and try and balance the two systems, but as I have indicated, because I find there is no jurisdiction, I will not attempt to do that and I will not attempt to balance the equities that counsel have drawn to the Court's attention.

17 So accordingly for the reasons I have just given, the application of Mr. Lysyk is dismissed.

Application dismissed.

[Indexed as: **Boutiques San Francisco Inc., Re**]

Les Boutiques San Francisco Incorporées, Les Ailes de la Mode Incorporées and Les Éditions San Francisco Incorporées (Debtors) and Ritchter & Associés Inc. (Monitor) and L'Oréal Canada inc. and Make Up For Ever S.A. (Petitioners)

Quebec Superior Court

Gascon J.S.C.

Heard: January 29, 2004

Judgment: February 10, 2004

Docket: C.S. Montréal 500-11-022070-037

Me Serge Guérette, Me Stéphanie Lapierre for Debtors
Me Philippe Buist for Monitor
Me Nicolas Plourde for L'Oréal Canada inc., Make Up For Ever S.A.

Bankruptcy and insolvency — Proposal — Companies' Creditors Arrangement Act — Arrangements — Effect of arrangement — Stay of proceedings — Composed of three retail chains, B Group obtained protection of Companies' Creditors Arrangement Act — Initial order stayed proceedings against B Group — On day of initial order, two cosmetics suppliers of B group were owed sums of money for goods delivered to B Group within 30 days preceding date of initial order — Suppliers each filed motion for stay to be lifted and declared inapplicable to them or for deposit of proceeds of sale of goods in separate trust — Motions dismissed — CCAA is flexible tool seeking to allow debtor corporation to stay in business while attempting to solve financial difficulties and to restructure — Key element of achieving CCAA objectives is maintaining status quo for time necessary to obtain creditors' approval of arrangement — Stay of proceedings is basic component of maintenance of status quo — Suppliers' motions went directly against CCAA objectives and maintenance of status quo during restructuring and would

put suppliers in preferred position — Contemplated arrangement appeared reasonable and was supported by many creditors — Granting motions would provoke avalanche of similar motions by other creditors — No precedents existed in Quebec or elsewhere in Canada to support motions — Possible situations justifying lifting stay did not exist in case at bar and application of CCAA did not of itself constitute sufficiently serious and distinct prejudice to justify lifting stay — Even if art. 1605 C.C.Q. did apply, suppliers' contracts were not resiliated as B Group was not in default, either by suppliers in writing or by operation of law — Prejudice claimed by suppliers was not serious in overall picture of restructuring B Group — As B Group's core business included cosmetics and perfumes, suppliers were within focus of restructuring and would benefit from successful restructuring — B Group did not act in bad faith towards suppliers — Neither lift of stay nor deposit was warranted.

Bankruptcy and insolvency — Proposal — Companies' Creditors Arrangement Act — Miscellaneous issues — Composed of three retail chains, B Group obtained protection of Companies' Creditors Arrangement Act — Initial order stayed proceedings against B Group — On day of initial order, two cosmetics suppliers of B group were owed sums of money for goods delivered to B Group within 30 days preceding date of initial order — Suppliers each filed motion for stay to be lifted in respect of suppliers' claims — Supplier L inc. also demanded return of display units provided to B Group — Motions dismissed — Agreement between supplier L inc. and B Group provided that parties would equally share cost of creating, constructing and installing display units and that L inc. would remain owner of units — Agreement was not traditional lease but did have several characteristics usually found in contract of lease — Situation was quite analogous to use of leased property provided after initial order was made — Since B Group was still using displays to sell L inc. products, nothing justified different treatment than that provided by s. 11.3 of CCAA — If B Group intended to continue using display units, B Group had to abide by terms of obligation agreed to, including payment of $28,000 within 90 days of delivery of units as well as $28,000 allowance as "coop-advertising" for 2003-2004 period.

Faillite et insolvabilité — Proposition — Loi sur les arrangements avec les créanciers des compagnies — Arrangements — Effet de l'ararrangement — Suspension des procédures — Groupe B, qui était composé de trois chaînes de magasins, a obtenu la protection de la Loi sur les arrangements avec les créanciers des compagnies — Ordonnance initiale a suspendu les procédures contre le Groupe B — En date de l'ordonnance initiale, le Groupe B devait de l'argent à deux de ses fournisseurs en cosmétiques pour des biens qu'ils lui avaient livrés dans les 30 jours précédant l'ordonnance initiale — Fournisseurs ont chacun présenté une requête afin que la suspension soit levée et déclarée inapplicable à eux ou afin que le produit de la vente des biens soit déposé dans un compte distinct — Requêtes rejetées — LACC est un outil flexible ayant pour but de permettre à une compagnie débitrice de demeurer en affaires pendant qu'elle tente de régler ses problèmes financiers et de se restructurer — Maintien du statu quo durant le temps nécessaire pour faire approuver l'arrangement par les créanciers constitue un élément clé de la réussite des objectifs de la LACC — Suspension est un élément fondamental du maintien du statu quo — En plus de les privilégier, les requêtes des fournisseurs allaient directement à l'encontre des objectifs de la LACC et du maintien du statu quo pendant la restructuration — Arrangement envisagé semblait raisonnable et était ap-

puyé par plusieurs créanciers — Accueil des requêtes provoquerait une avalanche de requêtes similaires par d'autres créanciers — Aucun précédent appuyant les requêtes n'existait au Québec ou ailleurs au Canada — Aucune des situations possibles justifiant la levée de la suspension n'étaient présentes en l'espèce, et l'application de la LACC ne constituait pas en soi un préjudice suffisamment grave et distinct justifiant de lever la suspension — Même si l'art. 1605 s'était appliqué, les contrats des fournisseurs n'étaient pas résiliés puisque le Groupe B n'était pas en défaut, que ce soit par écrit par les fournisseurs ou par l'opération de la loi — Préjudice allégué par les fournisseurs n'était pas grave dans le cadre de l'ensemble de la restructuration du Groupe B — Puisque le coeur des affaires du Groupe B incluait les cosmétiques et les parfums, les fournisseurs étaient visés par la restructuration et en profiteraient si elle réussissait — Groupe B n'a agi avec aucune mauvaise foi envers les fournisseurs — Rien ne justifiait la levée de la suspension ou un dépôt.

Faillite et insolvabilité — Proposition — Loi sur les arrangements avec les créanciers des compagnies — Questions diverses — Groupe B, qui était composé de trois chaînes de magasins, a obtenu la protection de la Loi sur les arrangements avec les créanciers des compagnies — Ordonnance initiale a suspendu les procédures contre le Groupe B — En date de l'ordonnance initiale, le Groupe B devait de l'argent à deux de ses fournisseurs en cosmétiques pour des biens qu'ils lui avaient livrés dans les 30 jours précédant l'ordonnance initiale — Fournisseurs ont chacun présenté une requête afin d'obtenir la levée de la suspension à l'égard de leur réclamation — Fournisseur L inc. a aussi demandé la remise des présentoirs fournis au Groupe B — Requêtes rejetées — Selon l'entente entre L inc. et le Groupe B, les parties devaient se partager également les coûts de la création, de la construction et de l'installation des présentoirs, et L inc. conserverait la propriété de ceux-ci — Entente ne constituait pas un bail traditionnel, mais comportait plusieurs des caractéristiques se trouvant généralement dans un contrat de location — Situation était très similaire à celle de l'usage d'un bien loué qui a été fourni après le prononcé de l'ordonnance initiale — Puisque le Groupe B utilisait toujours les présentoirs pour vendre des produits de L inc., rien ne justifiait un traitement différent de celui prévu par l'art. 11.3 LACC — Si le Groupe B voulait continuer à utiliser les présentoirs, il devait respecter les termes de l'obligation contractée, y compris faire le paiement de 28 000 $ dans les 90 jours de la livraison des présentoirs en plus du paiement de l'allocation de 28 000 $ à titre de « publicité à frais partagés » pour la période 2003-2004.

Cases considered by *Gascon J.S.C.*:

Agro Pacific Industries Ltd., Re (2000), 2000 BCSC 837, 2000 CarswellBC 1143, 76 B.C.L.R. (3d) 364, 5 B.L.R. (3d) 203, [2000] B.C.J. No. 1069 (B.C. S.C.) — considered

Bruce Agra Foods Inc. v. Everfresh Beverages Inc. (Receiver of) (1996), 45 C.B.R. (3d) 169, 1996 CarswellOnt 5053, 22 O.T.C. 247 (Ont. Gen. Div.) — considered

Canadian Airlines Corp., Re (2000), 2000 CarswellAlta 622, 19 C.B.R. (4th) 1 (Alta. Q.B.) — considered

Century Industries Inc. v. Enterprises Union Électrique Ltée (1992), 1992 CarswellQue 1869 (Que. S.C.) — distinguished

Détaillants Shirmax Ltée/Shirmax Retail Ltd. c. 170974 Canada Inc. (1994), 28 C.B.R. (3d) 177, 1994 CarswellQue 18 (Que. S.C.) — considered

Henry Birks & Sons Ltd., Re (1993), 22 C.B.R. (3d) 235, 1993 CarswellQue 38 (Que. S.C.) — considered

Hongkong Bank of Canada v. Chef Ready Foods Ltd. (1990), 51 B.C.L.R. (2d) 84, 4 C.B.R. (3d) 311, (sub nom. *Chef Ready Foods Ltd. v. Hongkong Bank of Canada)* [1991] 2 W.W.R. 136, 1990 CarswellBC 394, [1990] B.C.J. No. 2384 (B.C. C.A.) — considered

International Wallcoverings Ltd., Re (1999), 1999 CarswellOnt 4933, 28 C.B.R. (4th) 48 (Ont. Gen. Div. [Commercial List]) — referred to

Meridian Development Inc. v. Toronto Dominion Bank (1984), [1984] 5 W.W.R. 215, 52 C.B.R. (N.S.) 109, 32 Alta. L.R. (2d) 150, 53 A.R. 39, 11 D.L.R. (4th) 576, 1984 CarswellAlta 259 (Alta. Q.B.) — referred to

Mine Jeffrey inc., Re (2003), 2003 CarswellQue 90, 35 C.C.P.B. 71, [2003] R.J.D.T. 23, 40 C.B.R. (4th) 95, (sub nom. *Syndicat national de l'amiante d'Asbestos c. Mine Jeffrey inc.)* [2003] R.J.Q. 420, [2003] Q.J. No. 264 (Que. C.A.) — considered

Norcen Energy Resources Ltd. v. Oakwood Petroleums Ltd. (1988), 64 Alta. L.R. (2d) 139, [1989] 2 W.W.R. 566, 72 C.B.R. (N.S.) 20, 1988 CarswellAlta 319 (Alta. Q.B.) — considered

Olympia & York Developments Ltd., Re (March 14, 1994), Doc. B125/92, [1994] O.J. No. 1335 (Ont. Gen. Div. [Commercial List]) — considered

Packman Packaging Supplies Inc., Re (1995), 42 C.B.R. (3d) 143, 1995 CarswellQue 84 (Que. S.C.) — referred to

PCI Chemicals Canada Inc., Re (2002), 2002 CarswellQue 831, [2002] R.J.Q. 1093 (Que. S.C.) — considered

People's Department Stores Ltd. (1992) Inc., Re (1994), 37 C.B.R. (3d) 28, [1995] R.J.Q. 224, 1994 CarswellQue 151 (Que. S.C.) — referred to

Philip Services Corp., Re (1999), 1999 CarswellOnt 4495, 15 C.B.R. (4th) 107 (Ont. S.C.J. [Commercial List]) — referred to

Place Fleur de Lys c. Tag's Kiosque Inc. (1995), [1995] R.J.Q. 1659, 1995 CarswellQue 651 (Que. C.A.) — referred to

Quintette Coal Ltd. v. Nippon Steel Corp. (1990), 47 B.C.L.R. (2d) 193, 2 C.B.R. (3d) 291, 1990 CarswellBC 382 (B.C. S.C.) — referred to

Smith Brothers Contracting Ltd., Re (1998), 1998 CarswellBC 678, 53 B.C.L.R. (3d) 264, 13 P.P.S.A.C. (2d) 316, [1998] B.C.J. No. 728 (B.C. S.C.) — referred to

St-Lawrence Chemical Inc. v. A.R.C. Resins Corp. (May 16, 1997), Doc. 505-11-001681-977 (Que. S.C.) — considered

Steinberg Inc. c. Colgate-Palmolive Canada Inc. (1992), 13 C.B.R. (3d) 139, 1992 CarswellQue 22 (Que. S.C.) — considered

Steinberg Inc. c. Gillette Canada Inc. (1992), [1992] R.J.Q. 1602 (Que. S.C.) — considered

Woodward's Ltd., Re (1993), 17 C.B.R. (3d) 236, 79 B.C.L.R. (2d) 257, 1993 CarswellBC 530, [1993] B.C.J. No. 42 (B.C. S.C.) — considered

Woodward's Ltd., Re (1993), 77 B.C.L.R. (2d) 332, 100 D.L.R. (4th) 133, 1993 CarswellBC 75 (B.C. S.C.) — considered

Woodward's Ltd., Re (1993), 23 B.C.A.C. 224, 39 W.A.C. 224, 105 D.L.R. (4th) 517, 83 B.C.L.R. (2d) 31, 22 C.B.R. (3d) 25, 1993 CarswellBC 564 (B.C. C.A.) — referred to

166606 Canada inc. c. Bashtanik (1996), 1996 CarswellQue 1797 (Que. S.C.) — referred to

Statutes considered:

Bankruptcy and Insolvency Act, R.S.C. 1985, c. B-3
Generally — referred to
s. 50.4 [en. 1992, c. 27, s. 19] — referred to
s. 81.1 [en. 1992, c. 27, s. 38(1)] — referred to
s. 81.1(4) [en. 1992, c. 27, s. 38(1)] — referred to
s. 81.1(8) [en. 1992, c. 27, s. 38(1)] — referred to
Code civil du Bas-Canada, S. Prov. C. 1865, c. 41
art. 1543 — considered
Code civil du Québec, L.Q. 1991, c. 64
art. 1597 — considered
art. 1605 — considered
art. 1741 — considered
art. 1851 — referred to
Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36
Generally — referred to
s. 11 — considered
s. 11(3) — considered
s. 11(3)(a) — considered
s. 11(3)(b) — considered
s. 11(3)(c) — considered

MOTIONS by two suppliers for stay of proceedings against corporation protected by *Companies' Creditors Arrangement Act* to be lifted and declared inapplicable to suppliers or for deposit of proceeds of sale of unpaid goods in separate trust.

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

1) THE ISSUES

1 This judgment deals with the right of unpaid suppliers to repossess their goods still in the hands of a debtor company that availed itself of the protection of the *Companies' Creditors Arrangement Act*[1] (*CCAA*).

2 The facts giving rise to the dispute are simple and can be summarized as follows.

3 On December 17, 2003, Les Boutiques San Francisco incorporées, Les Ailes de la Mode incorporées and Les Éditions San Francisco incorporée (BSF Group) sought and obtained some of the protections available under the *CCAA*. The Initial Order issued on that day provided notably for a stay of the proceedings against the BSF Group.

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[1]R.S.C. 1985, c. C-36

4 A stay of proceedings is a standard conclusion in the initial orders made under the *CCAA* and section 11 (3) specifically provides for such a possibility:

> (3) A court may, on an initial application in respect of a company, make an order on such terms as it may impose, effective for such period as the court deems necessary not exceeding thirty days,
>
> (a) staying, until otherwise ordered by the court, all proceedings taken or that might be taken in respect of the company under an Act referred to in subsection (1);
>
> (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 or proceeding with any other action, suit or proceeding against the company.
>
> (Emphasis added)

5 On the date of the Initial Order issued here, one supplier, L'Oréal Canada Inc., was owed $413,557.08 by the BSF Group, $360,395,32 of which represented goods delivered within the 30 days prior to December 17, 2003[2]. After the application of some credits for services rendered, the amount owed was reduced to $299,840.09 on the day of hearing of L'Oréal's motion[3].

6 Similarly, another supplier, Make Up For Ever S.A., was also owed a sum of $67,420.97 on December 17, 2003, $30,015.58 of which represented goods delivered to the BSF Group within the 30 days preceding the date of the Initial Order[4].

7 In early January 2004, L'Oréal and Make Up For Ever each filed a motion by which they claimed that the stay of proceedings should be lifted and declared inapplicable inasmuch as they were concerned. The reason invoked: they each want to exercise their right to revendicate the goods sold and delivered still in the possession of the BSF Group, as any sale which took place is now resolved and resiliated automatically because of the BSF Group's failure to perform its obligations, namely to pay for the goods.

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[2]See "Requête de L'Oréal Canada inc. pour faire déclarer la suspension des procédures inapplicable ou, subsidiairement, pour ordonner le dépôt en fiducie de sommes et pour exiger le paiement de sommes relatives à l'utilisation de biens" dated January 13, 2004, paragraphs 2 and 3, and Exhibits R-1 to R-4.

[3]See "Liste d'admissions" dated January 29, 2004.

[4]See "Requête de Make Up For Ever S.A. pour faire déclarer la suspension des procédures inapplicable ou, subsidiairement, pour ordonner le dépôt en fiducie de sommes" dated January 19, 2004, paragraphs 2 and 3, and Exhibit R-1.

8 They rely upon article 1605 C.C.Q. which states:

> "**1605.** A contract may be resolved or resiliated without judicial proceedings where the debtor is in default by operation of law or where he has failed to perform his obligation within the time allowed in the writing putting him in default."
>
> (Emphasis added)

9 Subsidiarily, if the Court does not agree to lift the stay of proceedings against them, they ask that the proceeds of the sales of their goods be kept from now on in a separate trust account by the BSF Group, in order to protect their future rights and recourses.

10 Finally, in its own motion, L'Oréal asks that the BSF Group be ordered to either pay for the continued use of the display units ("agencements") it recently provided to them or return those immediately to L'Oréal in the absence of payment.

11 Not surprisingly, the BSF Group vigorously contests these requests. In that contestation, it also has the support of many: the Monitor, the Bank Syndicate and the Ad Hoc Committee of Unsecured Creditors.

12 Their position is clear and unanimous. There is no reason to treat these two suppliers any different than the other creditors of the BSF Group. To lift the stay of proceedings for these two suppliers would go against the specific objectives of the *CCAA* and the principles of the status quo that it should protect. Furthermore, the demands of these suppliers are not supported by any of the relevant precedents, be it from the Quebec or the Common Law provinces courts. Finally, they say that not only are the requests unjustified under the circumstances as these two suppliers, in particular, do not suffer any serious prejudice, but granting those would create an impact of such a nature as to put seriously in jeopardy the proposed arrangement of the BSF Group.

13 On the issue of the display units, they reply that nothing is owed at this stage since this debt preceded the Initial Order and should therefore be treated in the same manner as any others.

14 For sake of clarity and as the issues are very distinct from one another, the Court will deal, firstly, with the requests of L'Oréal and Make Up For Ever for the lift of the stay of proceedings and for the deposit of moneys in trust, and secondly, with the claim of L'Oréal pertaining to the display units.

2) THE LIFT OF THE STAY OF PROCEEDINGS AND, SUBSIDIARILY, THE DEPOSIT OF MONEYS IN TRUST

15 On the basis of the applicable statutes, the relevant case law and the evidence adduced, the Court is of the view that neither the lift of the stay of proceedings nor the deposit of moneys in trust should be ordered here, be it for the

benefit of L'Oréal or Make Up For Ever. In reaching this conclusion, the Court relies on the following considerations:

a) The purpose and objectives of the *CCAA*;

b) The precedents in Quebec and Canada; and

c) The absence of a serious and distinct prejudice to the two suppliers involved.

a) The purpose and objectives of the CCAA

16 It has been said often, and rightly so, that the *CCAA* is a remedial legislation. Its purpose is to allow companies in financial difficulties to reorganize themselves. As one judgment of the Quebec Superior Court recently reminded, it should be interpreted and applied as a flexible tool to assist in the restructuring of companies in financial difficulties[5].

17 One of the main goals of the *CCAA* is to allow the debtor company seeking its protection to stay in business as a going concern while attempting to solve its financial difficulties. The Courts indeed recognize that the Act should be given a large and generous interpretation to favour this objective[6].

18 As the Quebec Court of Appeal stated lately, contrary for instance to recourses under the *Bankruptcy and Insolvency Act*[7] (BIA), the objective of the *CCAA* is not to end the operation of a business and distribute its assets to its creditors, but rather to reach an arrangement between the debtor company and its creditors to allow for its survival[8].

19 One of the key elements to achieve these objectives is maintaining a status quo for the necessary time while the debtor company attempts to gain the approval of its creditors for a proposed arrangement[9]. Like the British Columbia Court of Appeal once said[10]:

> "[. . .] Equally obviously, if the attempt at compromise or arrangement is to have any prospect of success there must be a means of holding the creditors at bay, hence the powers vested in the court under s. 11."

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[5] *PCI Chemicals Canada Inc., Re* (2002), 2002 CarswellQue 831, [2002] R.J.Q. 1093 (Que. S.C.).

[6] *Olympia & York Developments Ltd., Re*, [1994] O.J. No. 1335 (Ont. Gen. Div. [Commercial List]); *Norcen Energy Resources Ltd. v. Oakwood Petroleums Ltd.* (1988), 72 C.B.R. (N.S.) 20 (Alta. Q.B.).

[7] R.S.C. 1985, c. B-3.

[8] *Mine Jeffrey inc., Re*, [2003] R.J.Q. 420 (Que. C.A.), par. 30.

[9] *Id.*, par. 31.

[10] *Hongkong Bank of Canada v. Chef Ready Foods Ltd.* (1990), 4 C.B.R. (3d) 311 (B.C. C.A.), 315; see also *Meridian Development Inc. v. Toronto Dominion Bank* (1984), 52 C.B.R. (N.S.) 109 (Alta. Q.B.), 114.

(Emphasis added)

20 In a judgment often cited on that subject, Mr. Justice Tysoe of the British Columbia Supreme Court summarized well what is meant by maintaining the status quo when a debtor company seeks the protection of the *CCAA*[11]:

> "It is my view that the maintenance of the status quo is intended to attempt to accomplish the following three objectives:
>
> 1. To suspend or freeze the rights of all creditors as they existed as at the date of the stay Order (which, in British Columbia, is normally the day on which the *CCAA* proceedings are commenced). This objective is intended to allow the insolvent company an opportunity to reorganize itself without any creditor having an advantage over the company or any other creditor.
>
> 2. To postpone litigation in which the insolvent company is involved so that the human and monetary resources of the company can be devoted to the reorganization process. The litigation may be resolved by way of the reorganization.
>
> 3. To permit the insolvent company to take certain action that is beneficial to its continuation during the period of reorganization or its attempt to reorganize or, conversely, to restrain a non-creditor or a creditor with rights arising after the stay from exercising rights that are detrimental to the continuation of the company during the period of reorganization or its attempt to reorganize. This is the objective recognized by *Quintette* and *Alberta-Pacific Terminals.* [. . .]"

(Emphasis added)

21 Therefore, as section 11 of the *CCAA* enacts and these precedents reiterate, in order to allow a debtor company to restructure itself and continue its operations, the stay of proceedings is a basic component of the maintenance of the status quo. Staying the proceedings means to suspend or freeze not only actual or potential litigation, but likewise any type of manoeuvres for positioning amongst creditors. This obviously includes the possibility of creditors seeking to repossess their goods in the hands of the debtor company who, to the contrary, should be allowed to continue operating as a going concern while protected under the *CCAA*.

22 From that standpoint, the motions of L'Oréal and Make Up For Ever are going directly against these objectives and the key element of maintaining the status quo during the course of the restructuring under the *CCAA*. The lift they are seeking is directly opposed to what the Act specifically provides for at sec-

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[11] *Woodward's Ltd., Re* (1993), 100 D.L.R. (4th) 133 (B.C. S.C.), 140.

tion 11 and would place both of them in a preferred position compared to that of the other unsecured creditors.

23 Surely, maintaining the status quo involves balancing the interests of all affected parties and avoiding advantages to some over the others. Under the *CCAA*, the restructuring process and the general interest of all the creditors should always be preferred over the particular interests of individual ones[12].

24 The Court does not believe that it is appropriate to set aside these objectives and principles in this case.

25 In its Initial Amended Order of January 15, 2004, the Court has already indicated that the contemplated arrangement of the BSF Group appeared practical, workable and realistic from an economic standpoint. At this stage, it has very strong support within the creditors of the BSF Group and no one has suggested that there exists a better solution to the problems now faced by the BSF Group.

26 In a situation where there exists a contemplated arrangement which is not doomed to fail but rather appears reasonable, which has the support of a vast majority of the creditors, and which is still being pursued diligently, it is the Court's opinion that the pursuit of the objectives of the *CCAA* should strongly be favoured, not countered.

27 As a result, with a contemplated arrangement such as the one involved here, the solutions should be pursued and the issues resolved within the context of this arrangement, not outside of it.

28 To that end, one must remember that the contemplated arrangement described by the BSF Group already gives consideration to the situation of suppliers such as L'Oréal and Make Up For Ever. One of its guiding principles is indeed expressed as follows by the BSF Group[13]:

> The participation of claims in the baskets could be adjusted so that the first dollars of each claim and sums due for merchandise sold and delivered within 30 days of the Initial Order, could be entitled to a greater participation in the basket than the remaining claims;

29 Since the proposed arrangement is not yet finalized, it is certainly too soon to comment on this potential treatment of the particular situation of the "30 days goods" suppliers. At this stage, it is sufficient to note that proper attention is being given to the situation of these suppliers who may otherwise have had other rights save for the protection afforded by the *CCAA*. Presently, there is no reason to believe that the arrangement that will eventually be submitted to the cred-

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[12]See, on these issues *Canadian Airlines Corp., Re* (2000), 19 C.B.R. (4th) 1 (Alta. Q.B.), 11; *Woodward's Ltd., Re* (1993), 17 C.B.R. (3d) 236 (B.C. S.C.); and *Quintette Coal Ltd. v. Nippon Steel Corp.* (1990), 2 C.B.R. (3d) 291 (B.C. S.C.), 297.

[13]See Motion for the Extension of the Initial Order dated January 14, 2004, paragraph 17 f).

itors for approval, and thereafter to the Court for sanction if fair and reasonable, will not be governed by similar considerations.

30 Still, L'Oréal and Make Up For Ever argued that the stay of proceedings will potentially deprive them of some of their alleged rights under the Civil Code of Quebec or the *BIA*, particularly if the arrangement fails and a bankruptcy is declared. Even though this possibility exists, when a proposed arrangement is characterized by qualifiers such as "not doomed to failure", "apparently reasonable", "strongly supported" and "diligently pursued", the Court considers that it should assess the situation with an assumption of success, not of failure, of the process.

31 Accordingly, even if these concerns of L'Oréal and Make Up For Ever should the arrangement fails are legitimate, they should not be the guiding criteria of the Court under the circumstances. Especially so when a proper arrangement can eventually alleviate, partially or totally, the loss of the alleged rights that the suppliers may now be denied.

32 To minimize the consequences of their requests, L'Oréal and Make Up For Ever have also argued that their claims represent less than $370,000, while the total accounts payable of the unsecured creditors, including the suppliers, represent more than $31,000,000[14]. The impact, if any, of their motions upon the restructuring of the BSF Group would therefore be, so they say, minimal.

33 Since no similar motions from other suppliers are presently pending, they are saying that the Court should not conclude that granting their requests will have the detrimental impact upon the restructuring process that the other parties are voicing.

34 With respect, the Court cannot agree with this argument.

35 Even though no other similar motions are now pending, the Court cannot simply close the eyes or look in the opposite direction and just pretend not to see the obvious. In a business such as that of the BSF Group, which is involved in the retail sale of men's, women's and children's apparels and accessories, it is clear that there are many other suppliers in a situation similar to that of L'Oréal and Make Up For Ever.

36 It is also clear that if the requests of L'Oréal and Make Up For Ever are granted, there will be many others presented to the Court. Opening this door would create a chaotic situation that will strike at the very heart of the going concern and continued operations objectives that the *CCAA* aims at protecting.

37 The Court does not need to have specific evidence from other suppliers confirming that they will proceed similarly to L'Oréal and Make Up For Ever should the motions be granted. This is self-evident and the Court cannot ignore

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[14]First Report of the Monitor, January 14, 2004, paragraphs 19 and 20.

it. This is exactly what Mr. Justice Lagacé from the Quebec Superior Court relied upon, amongst other things, in refusing to grant a similar request in the context of the restructuring of Steinberg Inc. under the *CCAA*[15]:

> "[. . .] Or le tribunal ne peut ignorer que plusieurs autres créanciers pourraientréclamer le même droit que désire exercer la débitrice-requérante. [. . .]"
>
> (Emphasis added)

38 All in all, when one considers the purpose and objectives of the *CCAA*,there are simply no justifications for the conclusions sought by L'Oréal and Make Up For Ever in their motions.

b) The precedents in Quebec and in Canada

39 That said, the Court notes further that there are no precedents, be it in Quebec or elsewhere in Canada, that support the requests made here by L'Oréal and Make Up for Ever. Indeed, all the judgments that bare any kind of similarity to the situation at hand go against the granting of what is being asked.

i. The Quebec Cases

40 To this date, the cases in Quebec have refused the claims of unpaid suppliers to repossess their goods in the context of a stay of proceedings pursuant to a reorganization or restructuring process, be it under the *CCAA* or the *BIA*.

41 For instance, in the context of the Steinberg Inc. restructuring under the *CCAA*, Mr. Justice Lagacé twice refused motions to authorize an unpaid supplier to seize before judgment the merchandises sold and delivered within the 30 days prior to the Initial Order[16].

42 In the two judgments he rendered, Mr. Justice Lagacé concluded that when faced with an arrangement that appeared serious, the individual interest of a creditor should not be preferred over the general interest of all the creditors. For Mr. Justice Lagacé, granting the requests would have most likely resulted in a number of similar motions by other suppliers and it would have basically led to the failure of the arrangement before it was even submitted to the creditors for approval. This would have been contrary to the objectives of the *CCAA*.

43 It is worth noting that in these two decisions, the suppliers were relying upon article 1543 C.C.B.C. and their corresponding right to revendicate the goods

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[15]*Steinberg Inc. c. Colgate-Palmolive Canada Inc.* (1992), 13 C.B.R. (3d) 139 (Que. S.C.), 141.

[16]*Steinberg Inc. c. Colgate-Palmolive Canada Inc., id.*; *Steinberg Inc. c. Gillette Canada Inc.*, [1992] R.J.Q. 1602 (Que. S.C.).

sold and delivered within the prior 30 days. Since 1994, article 1741 C.C.Q. has replaced article 1543 C.C.B.C. It now states the following:

> **1741.** Except in the case of a sale with a term, the seller of movable property may, within thirty days of delivery, consider the sale resolved and revendicate the property if the buyer, being in default, has failed to pay the price and if the property is still entire and in the same condition and has not passed into the hands of a third person who has paid the price thereof, or of a hypothecary creditor who has obtained surrender thereof.
>
> Where the buyer is in default to pay the price and the property meets the conditions prescribed for resolution of the sale, the seizure of the property by a third person is no hindrance to the rights of the seller.
>
> (Emphasis added)

44 Here, L'Oréal and Make Up For Ever are not relying upon this article which is specific to the situation of an unpaid vendor of movable property in the Quebec Civil Code. As their sales were with a term, they do not meet the conditions necessary for its application. Thus, to justify their requests, they are relying upon the general provisions of obligations applicable to all contracts found at article 1605 C.C.Q.

45 It is difficult to see why the reasoning applicable for a claim made under article 1543 C.C.B.C. (now 1741 C.C.Q.) in cases like the two *Steinberg* decisions would be any different inasmuch as the general provisions of article 1605 C.C.Q. are concerned. At the very least, L'Oréal and Make Up For Ever did not present any convincing argument to that end.

46 Likewise, in the context of the *BIA* this time, Mr. Justice Denis has reached a conclusion similar to that of Mr. Justice Lagacé on a demand by suppliers for the repossession of goods after the filing of a notice of intention to make a proposal[17].

47 In that matter, the suppliers were again invoking article 1543 C.C.B.C. Nonetheless, Mr. Justice Denis concluded that there was no reason not to apply the stay of proceedings to them. He emphasized that sections 81.1(4) and 50.4 of the *BIA* intended to temporarily deny certain rights to creditors in order to allow a company to make a proposal to solve its financial difficulties. The protection that the *BIA* afforded to suppliers of goods in section 81.1 was not applicable in a proposal context, hence the absence of any basis to provide them with a similar protection through article 1543 C.C.Q.

48 The same conclusion was reached by Mr. Justice Halperin in *Henry Birks & Sons Ltd., Re*[18]. On a petition for an order pursuant to section 81.1(8) of the *BIA*,

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[17] *Détaillants Shirmax Ltée/Shirmax Retail Ltd. c. 170974 Canada Inc.* (1994), 28 C.B.R. (3d) 177 (Que. S.C.).

[18] *Henry Birks & Sons Ltd., Re* (1993), 22 C.B.R. (3d) 235 (Que. S.C.).

he denied the request of unpaid suppliers to exercise their remedies as unpaid vendors, as such could have well placed in jeopardy the whole reorganization process of the debtor company. He noted that section 81.1 was clear and only suspended the running of the 30 days period upon the commencement of a proposal proceeding, even though any rights as unpaid vendors in the future would often be illusory if the goods were no longer in the possession of the debtor company once a bankruptcy was finally declared[19].

49 No Quebec courts decisions granting the requests sought by L'Oréal or Make Up For Ever could be found to support their position. The situation was no different in the Common Law provinces.

ii. The Common Law Provinces Cases

50 In proceedings taken under the *CCAA*, the British Columbia Supreme Court has twice denied requests similar to those presented by L'Oréal and Make Up For Ever.

51 In *Agro Pacific Industries Ltd., Re*[20], Mr. Justice Thackray denied an application by suppliers to set aside a stay of proceedings granted under the *CCAA*. He stated notably that ordering that the supplies made to the debtor company within 30 days of the Initial Order be traced and identified and their proceeds put in a trust account would be an attempt to improperly introduce into the *CCAA* proceedings requirements similar to those contained in section 81.1 of the *BIA*. In his reasons, Mr. Justice Thackray had these comments which are worth citing:

> "[52] An order establishing a trust fund in favour of the applicant suppliers would create a class of secured creditors after the fact. It would turn the Court into the author of a new class of creditor. Classes of creditors should be created by the parties on a contractual basis when entering into their business relationships.
>
> [. . .]
>
> [55] Mr. Justice Tysoe in *Re Woodward's* also alluded to the potential that the Court cannot lose sight of legislative intention. He pointed out that the *CCAA* is « silent as to the creation of a trust fund to be held for the benefit of the suppliers in the event that the reorganization is not successful. » Many of the challenges by the suppliers in the case at bar are legislative.
>
> [56] The *CCAA* must be accepted as Parliament's approval of the continued business activities of an insolvent company, to be carried out in as normal a manner as possible while reorganizing. The Court is not

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[19]See also *People's Department Stores Ltd. (1992) Inc., Re* (1994), 37 C.B.R. (3d) 28 (Que. S.C.).

[20][2000] B.C.J. No. 1069 (B.C. S.C.).

> allowed to suggest that the legislative intent is one designed, *per se*, to disadvantage the suppliers. It must, rather, be taken as giving hope that reorganization, rather than bankruptcy, will eventually benefit all interested parties."
>
> (Emphasis added)

52 In this judgment, Mr. Justice Thackray found no basis to justify the requests made by the suppliers under the *CCAA*.

53 In *Woodward's Ltd., Re*[21], Mr. Justice Tysoe reached a similar conclusion. In that case, applications by suppliers of goods for relief under the *CCAA* were also denied. Applications for leave to appeal of that decision were furthermore dismissed[22].

54 For Mr. Justice Tysoe, in addition to the fact that section 81.1 of the *BIA* could not be of any use to the suppliers as the *CCAA* did not contain any similar provision, the creation of any trust fund was not justified as it would not serve to maintain the status quo. He wrote this on the issue[23]:

> "Apart from consideration of s. 81.1 of the *B. & I. Act*, there is no justification for the creation of the trust fund. It would not serve to maintain the status quo. To the contrary, it would give the suppliers an advantage over other creditors of Woodward's. It would not be beneficial to the continuation of Woodward's business during the reorganization period or Woodward's attempt to reorganize. Indeed, it was the position of Woodward's on these applications that the creation of a trust fund in the amount of $30 million would make any reorganization impossible."
>
> (Emphasis added)

55 Finally, and similarly to what the Quebec courts did conclude, in *Bruce Agra Foods Inc.*, Mr. Justice Farley denied a motion made by unpaid suppliers this time within the context of a notice of intention to file a proposal under the *BIA*. In that case, Mr. Justice Farley concluded that in a reorganization scenario, unpaid suppliers could not avail themselves of a protection similar to that of section 81.1 of the *BIA*. He mentioned[24]:

> "2. If Parliament had intended that unpaid suppliers have direct *immediate* rights in a reorganization scenario as envisaged by a Notice of Intention to File a Proposal, then it would seem to me that it would have provided for same to take place in s. 81.1(b) but rather Parliament addressed the Notice of Intention situation by having a suspension during the relevant time period: see s. 81.1(4). Unfortunately for those affected, in order to promote reorgani-

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[21] *Woodward's Ltd., Re*, *supra*, note 11.

[22] *Woodward's Ltd., Re* (1993), 105 D.L.R. (4th) 517 (B.C. C.A.).

[23] *Woodward's Ltd., Re*, *supra*, note 11, p. 141.

[24] *Bruce Agra Foods Inc. v. Everfresh Beverages Inc. (Receiver of)* (1996), 45 C.B.R. (3d) 169 (Ont. Gen. Div.), 171-173.

> zations (which is an underlying fundamental of the BIA including the 1992 amendments which puts some teeth or perhaps « life blood » into that part of the BIA), there will be some prejudice to creditors (who may be unpaid sellers). If the rights of unpaid suppliers were to override, then there would have to be an amendment to section 69.1 (a) to that effect. [. . .]
>
> [. . .]
>
> 6. It would seem to me that unpaid supplier rights are truly intended to protect against the unfair consequences in liquidation as seen by Parliament and are not intended to affect or disrupt reorganizations proposed pursuant to Part IV of the BIA. [. . .]"
>
> (Emphasis added)

56 Again, L'Oréal and Make Up For Ever could not refer the Court to any decision from the Common Law provinces which had granted a motion similar to theirs.

iii) L'Oréal and Make Up For Ever reply to the precedents

57 Notwithstanding, to distinguish these decisions, L'Oréal and Make Up For Ever first argued that in the Quebec decisions in *Steinberg* or in *Shirmax*[25], no claims for the deposit of moneys in a trust account similar to what is requested here were apparently made.

58 While it is true that this issue was not specifically dealt with in these three judgments, the Court fails to see on what basis their conclusions would have been any different with respect to the deposit of moneys in a trust account.

59 The protection given to an unpaid supplier under article 1543 C.C.B.C. (now 1741 C.C.Q.) discussed in these decisions was limited to the right to repossess its goods. If the exercise of that right was considered by the Courts as inappropriate in the context of proceedings under the *CCAA* or the *BIA*, it follows that, logically, the exercise of the same right "by equivalent", namely by having the proceeds of the sale of the goods deposited in a trust account, would normally trigger the same answer.

60 Second, L'Oréal and Make Up For Ever further argued that the judgment in *Shirmax*[26] should be distinguished because in that case, the impact upon the restructuring would have been very significant considering the extent of the debt owed to the suppliers involved when compared to the whole debt of the company. This argument cannot be retained because it would require the Court to ignore the obvious consequences of a judgment granting the requests made, namely that it will in all likelihood trigger an avalanche of similar type of requests by the numerous suppliers of the BSF Group.

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[25] *Supra*, note 17.

[26] *Supra*, note 17.

61 Third, L'Oréal and Make Up For Ever argued that the decisions of the Common Law provinces should be distinguished and ignored as there are no recourses similar to that of article 1605 C.C.Q. in those jurisdictions.

62 While that is true, it remains that the decisions rendered in the Common Law provinces are quite relevant and useful to the issues to be decided here.

63 On the one hand, these judgments have correctly emphasized that the *CCAA*, while providing for a stay of proceedings in the context of a restructuring, has made no exceptions for the rights of suppliers as, for instance, the *BIA* has done in some limited circumstances, albeit not for proposals.

64 On the other hand, in denying the requests made, these judgments have also emphasized, again rightfully, that the issues raised by the suppliers were more legislative than judicial in nature, since Parliament had decided to protect specifically the unpaid suppliers rights only in limited circumstances in the *BIA*.

65 These decisions have correctly noted that in situations of reorganizations or restructurings, neither the *CCAA* nor the *BIA* contain provisions addressing these rights, except for the suspension of the running of the 30 day delay of section 81.1 in the case of a proposal under the *BIA*. On that issue, and as it was decided for example in *Woodward's Ltd., Re*, the terms of the Court's Initial Order already include a similar suspension for the benefit of the suppliers.

66 In addition, and again similarly to what this Court did here, these judgments of the other provinces have considered and given weight to the detrimental impact the granting of the motions involved would have had upon the key objectives of the protections offered by the *CCAA*.

67 On the whole, even though provisions similar to article 1605 C.C.Q. do not exist in these other jurisdictions, these decisions can be relied on since their conclusions are based upon reasons that do apply in this case.

68 As a fourth and final point, L'Oréal and Make Up For Ever argue that, notwithstanding all these precedents, in two cases decided in the context of restructurings conducted under the *CCAA* and the *BIA*, the Quebec courts have granted requests to put in a trust account the proceeds of merchandise sold pending the outcome of the reorganization process.

69 In this respect, they refer to the Superior Court judgment of Mr. Justice Archambault in *Century Industries Inc. v. Enterprises Union Électrique Ltée*[27] and to the Court of Appeal decision in *Gestion Max Boutin inc. v. Brasserie Molson O'Keefe*[28].

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[27]C.S. Montreal, nº 500-05-005804-925, 1992-04-29, j. Archambault, 1992 CarswellQue 1869 (Que. S.C.).

[28]J.E. 94-804 (C.A.).

70 However, as it was indicated at the hearing, these decisions can be distinguished easily as the creditors involved had specifically retained by contract their rights of ownership in the goods at issue, which is not the case for L'Oréal or Make Up For Ever.

71 In short, the review of these precedents in Quebec and in Canada confirms the absence of justification for the remedies sought here by these two suppliers.

c) The absence of a serious and distinct prejudice to the two suppliers involved

72 But that is not all. In addition to the fact that the conclusions sought by L'Oréal and Make Up For Ever would be contrary to the applicable case law as well as the purpose and objectives of the *CCAA*, the Court is satisfied that under the circumstances, neither L'Oréal nor Make Up For Ever would suffer a prejudice sufficiently serious as to justify lifting the stay of proceedings.

73 In summary, L'Oréal and Make Up For Ever are alleging that they are suffering a serious and distinct prejudice because the stay of proceedings will result in them losing a right to repossess goods that they have under article 1605 C.C.Q., hence their justification to lift the stay.

74 To emphasize their prejudice, they are also asserting that an arrangement under the *CCAA* must give creditors something more than what they would otherwise receive in the context of a bankruptcy. Since they will end up, in all likelihood, receiving less in the context of an arrangement under the *CCAA* than in a bankruptcy process under the *BIA*, they consider that their motions should be granted.

75 The Court disagrees with these arguments.

76 On the first of these arguments, in *Canadian Airlines Corp., Re*, it was stated that under the *CCAA*, there are simply no statutory tests to guide a court in lifting a stay against a certain creditor. In that case, to give some indications of what could be considered to that end, Madam Justice Paperny referred to the following[29]:

> "20 At pages 342 and 343 of this text, Canadian Commercial Reorganization: Preventing Bankruptcy (Aurora: Canada Law Book, looseleaf), R.H. McLaren describes situations in which the court will lift a stay:
>
> 1. When the plan is likely to fail;
> 2. The applicant shows hardship (the hardship must be caused by the stay itself and be independent of any pre-existing condition of the applicant creditor);
> 3. The applicant shows necessity for payment (where the creditors financial problems are created by the order of where the

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[29] *Supra*, note 12, p. 7-8.

failure to pay the creditor would cause it to close and thus jeopardize the debtor's company's existence);

4. The applicant would be severely prejudiced by refusal to lift the stay and there would be no resulting prejudice to the debtor company or the positions of creditors;

5. It is necessary to permit the applicant to take steps to protect a right which could be lost by the passage of time;

6. After the lapse of a significant time period, the insolvent is no closer to a proposal than at the commencement of the stay period."

(Emphasis added)

77 When one considers these situations, none apply here, except potentially the fifth one. However, even in such a situation, the only alleged prejudice suffered by L'Oréal and Make Up For Ever would be one directly caused by the mere application of the Act, namely by the stay of proceedings which the *CCAA* authorizes.

78 On that specific issue, in the decision of *St-Lawrence Chemical Inc. v. A.R.C. Resins Corp.*, Madam Justice Lemelin of the Quebec Superior Court concluded this[30]:

"Le préjudice de la requérante ne peut être que celui causé par l'application normale de la loi qui suspend les recours de tous les créanciers et fournisseurs. Le juge Trudeau qualifie même ce préjudice "de sérieux" dans l'affaire de faillite Goineau.

La requérante ne peut demander au Tribunal de mettre de côté l'application d'une loi qui dans le vœu du législateur doit favoriser la réorganisation d'entreprises en difficultés en les mettant à l'abri des procédures temporairement. Permettre aux fournisseurs de reprendre les marchandises vendues compromet les opérations de la personne insolvable. La requérante doit satisfaire le Tribunal de ce préjudice sérieux, ce qu'elle ne fait pas."

(Emphasis added)

79 The Court agrees with these comments. Simply stated, the application of the *CCAA* cannot of itself constitute a sufficiently serious and distinct prejudice to justify the lift of a stay of proceedings.

80 Consequently, even though much time was spent in argument by the attorneys for both sides on the right of an unpaid supplier to even invoke the application of article 1605 C.C.Q. in a situation similar to that of L'Oréal and Make Up For Ever, the Court considers that it is not necessary to decide this question.

81 There are sufficient reasons here to deny the motions of L'Oréal and Make Up For Ever without having to decide whether or not an unpaid supplier who

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[30](May 16, 1997), Doc. 505-11-001681-977 (Que. S.C.), J. Lemelin, AZ-97026278, p. 5.

does not meet the conditions of article 1741 C.C.Q. can nevertheless invoke the benefit of the general provision of article 1605 C.C.Q. This question appears to be far from settled in the civil law doctrine or in the case law[31].

82 In any event, on that issue of the alleged right to repossess of these suppliers, the Court notes that the resolution or resiliation of a contract without judicial proceedings as invoked by L'Oréal and Make Up For Ever only applies where the debtor, namely the BSF Group, is in default by writing or by operation of law.

83 The BSF Group was apparently not put in default in writing by these suppliers and article 1597 C.C.Q. describes the situations where a debtor is in default by operation of law:

> "**1597.** A debtor is in default by the sole operation of law where the performance of the obligation would have been useful only within a certain time which he allowed to expire or where he failed to perform the obligation immediately despite the urgency that he do so.
>
> A debtor is also in default by operation of law where he has violated an obligation not to do, or where specific performance of the obligation has become impossible through his fault, and also where he has made clear to the creditor his intention not to perform the obligation or where, in the case of an obligation of successive performance, he has repeatedly refused or neglected to perform it."
>
> (Emphasis added)

84 Here, there is only one instance where the BSF Group would potentially be in default by operation of law towards these two suppliers: because it would have "*made clear to* (these) *creditors* (its) *intention not to perform* (its) *obligations*".

85 However, it does not appear that this is the case yet.

86 When a creditor avails itself of the protection that the law offers, and as result is afforded it with a corresponding stay of proceedings, one cannot conclude that this debtor then makes it clear to its creditors that it intends not to perform its obligations. As a matter of fact, under the *CCAA*, the objective of this debtor is rather to propose an arrangement to these creditors for the compromise of these obligations and this may include a partial and even a total performance of these obligations in some cases.

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[31] See on this issue Jean-Louis BAUDOUIN et Pierre-Gabriel JOBIN, *Les obligations*, 5e édition, Cowansville, Éditions Yvon Blais, 1998, p. 592-593; Pierre-Gabriel JOBIN, *La vente*, 2e édition, Cowansville, Éditions Yvon Blais, 2001, p. 262-264; Denys-Claude LAMONTAGNE, *Droit de la vente*, Cowansville, Éditions Yvon Blais, 1995, p. 146-147; *Place Fleur de Lys c. Tag's Kiosque Inc.*, [1995] R.J.Q. 1659 (Que. C.A.); *Packman Packaging Supplies Inc., Re* (1995), 42 C.B.R. (3d) 143 (Que. S.C.); *166606 Canada inc. c. Bashtanik* (1996), 1997 CarswellQue 1797 (Que. S.C.), J.E. 96-1556.

87 Therefore, it is far from obvious that L'Oréal and Make Up For Ever even qualify here for the application of article 1605 C.C.Q. If this were so, then their position would be even less justified under the circumstances.

88 Concerning now the second argument that in proceedings conducted under the *CCAA*, L'Oréal and Make Up For Ever should not be put in a situation worst than the one they would be in under the *BIA*, the Court considers that if anything, it is the situation of all the creditors collectively that must be looked at.

89 While it is true that one of the objectives of the *CCAA* is to provide a better solution than what a bankruptcy would offer, this is so from the standpoint of the benefit to all the creditors, not to individual ones. L'Oréal and Make Up For Ever are looking at the situation only from their own viewpoint, while in the context of proceedings under the *CCAA*, the prejudice and interest of the parties must in every respect be looked at collectively.

90 Indeed, under the circumstances, the prejudice alleged by L'Oréal and Make Up For Ever, even from an individual standpoint, is far from being serious in the overall picture of the restructuring of the BSF Group.

91 Both companies are involved in the cosmetics and perfumes business and they supply mostly, if not exclusively, Les Ailes de la Mode. In the restructuring business plan submitted to the Court[32], one of the key elements of the repositioning of the BSF Group is to focus upon what it calls its core business, notably with its banner Les Ailes de la Mode. This core business includes for one thing the cosmetics and perfumes.

92 Therefore, these two suppliers, perhaps much more so than many others, are well within the specific business and banner upon which the BSF Group intends to focus for its restructuring. As a result, they appear to be creditors who would definitely benefit, not suffer, from a successful restructuring of the BSF Group.

93 It is in fact striking to note this from the admissions filed in the record[33]. The sales of L'Oréal to the BSF Group totalled $3,609,000 in 2002 and $3,155,000 in 2003, for an average of $281,833 per month over these 24 months. In comparison, the sales of L'Oréal to the BSF Group for the first month immediately following the Initial Order totalled more than $335,000, namely a higher monthly average, even in the context of the restructuring process.

94 Finally, on this issue of the prejudice, it must be remembered that, in this case, there is no evidence of bad faith in the BSF Group's behaviour towards these two suppliers. Notwithstanding what is alleged in their motions, the Court is of the view that the circumstances surrounding the discussions and exchanges

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[32]Exhibit R-5 in support of the Motion for the Extension of the Initial Order dated January 14, 2004.

[33]"Liste d'admissions" dated January 29, 2004.

of cheques in December 2003 indicate that they were carried on in good faith, in the normal course of business of the BSF Group.

95 To sum up, be it from the angles of the lack of serious and distinct prejudice to L'Oréal and Make Up For Ever, of the applicable precedents and their reasoning, or of the purpose and objectives of the *CCAA*, nothing warrants the Court to lift the stay of proceedings or to order the deposit of moneys in trust in the actual situation of these two suppliers.

3) THE CLAIM OF L'ORÉAL CONCERNING THE DISPLAY UNITS

96 Turning now to the claim of L'Oréal concerning the display units it provided to the BSF Group in November 2003, this is what the evidence indicates.

97 Even if the written contract presented by L'Oréal in that month was never signed by the BSF Group, the exchanges of e-mails[34] that were filed in the record nevertheless suggest that the parties had agreed as follows.

98 L'Oréal accepted to provide to the BSF Group some display units that were to be used by the BSF Group to exhibit the products and facilitate their sales. The parties were to share equally in the cost of creating, constructing and installing these display units but at all times, L'Oréal was to remain the owner. For its share, it was agreed that a first amount of $28,000 would be paid by the BSF Group within 90 days of delivery and another amount of $28,000 would be spent by them as « coop-advertising » during 2003-2004.

99 L'Oréal considers that this is covered by section 11.3 of the *CCAA* which indicates in part that:

> "**11.3** No order made under section 11 shall have the effect of
>
> (*a*) prohibiting a person from requiring immediate payment for goods, services, use of leased or licensed property or other valuable consideration provided after the order is made; [. . .]"
>
> (Emphasis added)

100 The BSF Group replies that the agreement at issue is not per se a contract of lease but rather a *sui generis* agreement and that section 11.3 does not apply.

101 Even though this agreement is not a traditional lease, it remains that it shares a lot of the characteristics that one would normally find in a contract of lease (article 1851 C.C.Q.). More specifically, we definitely have here a person, L'Oréal, who provides another, the BSF Group, with the use and enjoyment of display units for a certain period, in exchange for payments that are detailed in the e-mails filed. The display units are also not to be kept by the BSF Group but returned to L'Oréal after their use.

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[34]Exhibit R-10 in support of the motion of L'Oréal.

102 This is certainly closer to a traditional lease for use than, for instance, to some sort of financing agreement[35].

103 With respect to these display units, it is the Court's opinion that we have a situation which is quite analogous to the use of leased property provided after the initial order is made. The BSF Group continues to this day to make use of those display units for the purpose of selling the products of L'Oréal. Similarly to the use of leased premises, these are still being enjoyed and benefited from by the BSF Group in order to help the sale of the products of L'Oréal. It is a continuing benefit that the BSF Group still wants to make use of and the Court fails to see why it should be treated differently than the other situations covered by section 11.3 of the *CCAA*.

104 As a result, with respect to these conclusions of the motion of L'Oréal, the Court considers that if it is indeed the intent of the BSF Group to continue to use these display units, it should abide by the terms of the obligations it agreed to. These include the payment of an amount of $28,000 within 90 days of delivery of the display units and an allowance of $28,000 as "coop-advertising" for the period 2003-2004.

105 Since there has been no indication or evidence suggesting that the BSF Group has yet defaulted on these obligations, the Court will simply issue in this respect a declaration confirming this conclusion.

106 **FOR THESE REASONS, THE COURT:**

WITH RESPECT TO L'ORÉAL CANADA INC.:

107 DISMISSES the motion for the lift of the stay of proceedings and for the deposit of moneys in trust;

108 DECLARES that with respect to the display units provided by L'Oréal Canada Inc. to Les Ailes de la Mode pursuant to the terms of the e-mails filed as Exhibit R-10, Les Ailes de la Mode must comply with the obligations agreed upon between the parties, namely to:

- Pay an amount of $28,000 to L'Oréal Canada Inc. within 90 days following the delivery of the display units; and
- Provide for an allowance of $28,000 as "coop-advertising" for the period 2003-2004;

109 WITH COSTS.

WITH RESPECT TO MAKE UP FOR EVER S.A.:

110 DISMISSES the motion for the lift of the stay of proceedings and for the deposit of moneys in trust;

111 WITH COSTS.

Motions dismissed.

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[35]See on that issue *Smith Brothers Contracting Ltd., Re* (1998), 53 B.C.L.R. (3d) 264 (B.C. S.C.); *Philip Services Corp., Re* (1999), 15 C.B.R. (4th) 107 (Ont. S.C.J. [Commercial List]); *International Wallcoverings Ltd., Re* (1999), 28 C.B.R. (4th) 48 (Ont. Gen. Div. [Commercial List]).

TAB 7

CANADIAN BANKRUPTCY REPORTS

Fourth Series/Quatrième série

Recueil de jurisprudence canadienne
en droit de la faillite

[Indexed as: **Canadian Airlines Corp., Re**]

In the Matter of Canadian Airlines Corporation and Canadian Airlines International Ltd.

The Bank of Nova Scotia Trust Company of New York, As Trustee for the Holders of Senior Secured Notes and Montreal Trust Company of Canada, As Collateral Agent for the Holders of Senior Secured Notes, Plaintiffs and Canadian Airlines Corporation, Canadian Airlines International Ltd., Canadian Regional Airlines Ltd., Canadian Regional Airlines (1998) Ltd. and Canadian Airlines Fuel Corporation Inc., Defendants

Alberta Court of Queen's Bench

Paperny J.

Judgment: May 4, 2000

Docket: Calgary 0001-05071, 0001-05044

G. Morawetz, A.J. McConnell and *R.N. Billington*, for Bank of Nova Scotia Trust Co. of New York and Montreal Trust Co. of Canada.

A.L. Friend, Q.C., and *H.M. Kay, Q.C.*, for Canadian Airlines.

S. Dunphy, for Air Canada and 853350 Alberta Ltd.

R. Anderson, Q.C., for Loyalty Group.

H. Gorman, for ABN AMRO Bank N.V.

P. McCarthy, for Monitor - Price Waterhouse Cooper.

D. Haigh, Q.C., and *D. Nishimura*, for Unsecured noteholders - Resurgence Asset Management.

C.J. Shaw, for Airline Pilots Association International.

G. Wells, for NavCanada.

D. Hardy, for Royal Bank of Canada.

Corporations — Arrangements and compromises — Under Companies' Creditors Arrangement Act — Arrangements — Effect of arrangement — Stay of proceedings — Senior secured noteholders brought application for appointment of receiver over collateral on same day that airline was granted CCAA protection — Noteholders

constituted separate class that intended to vote against plan and had voted to realize on security — Noteholders brought application for order lifting stay of proceedings against them to allow for appointment of receiver and manager over assets and property charged in their favour, and for order appointing court officer with exclusive right to negotiate sale of assets or shares of airline's subsidiary — Application dismissed — In determining whether stay should be lifted, court had to balance interests of all parties who stood to be affected — This would include general public, which would be affected by collapse of airline — Evidence indicated that liquidation would be inevitable were noteholders to realize on collateral — Objective of stay was not to maintain literal status quo but to maintain situation that was not prejudicial to creditors while allowing airline "breathing room" — It was premature to conclude that plan would be rejected or that proposal acceptable to noteholders could not be reached — Evidence indicated that airline was moving to effect compromises swiftly and in good faith — Appointment of receiver to manage collateral would negate effect of stay and thwart purposes of Act — Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36.

Corporations — Arrangements and compromises — Under Companies' Creditors Arrangement Act — Miscellaneous issues — Senior secured noteholders brought application for appointment of receiver over collateral on same day that airline was granted CCAA protection — Noteholders constituted separate class that intended to vote against plan and voted to realize on security — Noteholders brought application for order lifting stay of proceedings against them to allow for appointment of receiver and manager over assets and property charged in their favour, and for order appointing court officer with exclusive right to negotiate sale of assets or shares of airline's subsidiary — Application dismissed — Proposal that airline make interim payments for use of security was not viable — Suggestion that other airline financially supporting plan should pay out airline's debts to noteholders was without legal foundation — Existence of solvent entity financially supporting plan with view to obtaining economic benefit for itself did not create obligation on that entity to pay airline's creditors — Noteholders could not require sale of assets or shares of airline's subsidiary — Subsidiary was not debtor company but was itself property of airline — Marketing of subsidiary's assets would constitute "proceeding in respect of petitioners' property" within meaning of s. 11 of Act — Even if marketing of subsidiary's assets did not so qualify, court has inherent jurisdiction to grant stays in relation to proceedings against third parties where exercise of jurisdiction is important to reorganization process — In deciding whether to exercise inherent jurisdiction, court weighs interests of insolvent corporation against interests of parties who would be affected by stay — Threshold of prejudice required to persuade court not to exercise inherent jurisdiction to grant stay is lower than threshold required to persuade court not to exercise discretion under s. 11 of Act — Noteholders failed to meet either threshold — Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36, s. 11.

Cases considered by *Paperny J.*:

Alberta-Pacific Terminals Ltd., Re (1991), 8 C.B.R. (3d) 99 (B.C. S.C.) — considered

Campeau v. Olympia & York Developments Ltd. (1992), 14 C.B.R. (3d) 303, 14 C.P.C. (3d) 339 (Ont. Gen. Div.) — considered

Citibank Canada v. Chase Manhattan Bank of Canada (1991), 5 C.B.R. (3d) 165, 2 P.P.S.A.C. (2d) 21, 4 B.L.R. (2d) 147 (Ont. Gen. Div.) — referred to

Hongkong Bank of Canada v. Chef Ready Foods Ltd. (1990), 51 B.C.L.R. (2d) 84, 4 C.B.R. (3d) 311, (sub nom. *Chef Ready Foods Ltd. v. Hongkong Bank of Canada)* [1991] 2 W.W.R. 136 (B.C. C.A.) — referred to

Meridian Development Inc. v. Toronto Dominion Bank, [1984] 5 W.W.R. 215, 52 C.B.R. (N.S.) 109, 32 Alta. L.R. (2d) 150, 53 A.R. 39, 11 D.L.R. (4th) 576 (Alta. Q.B.) — referred to

Norcen Energy Resources Ltd. v. Oakwood Petroleums Ltd. (1988), 64 Alta. L.R. (2d) 139, [1989] 2 W.W.R. 566, 72 C.B.R. (N.S.) 20, 72 C.R. (N.S.) 20 (Alta. Q.B.) — referred to

Nova Metal Products Inc. v. Comiskey (Trustee of) (1990), 1 C.B.R. (3d) 101, (sub nom. *Elan Corp. v. Comiskey)* 1 O.R. (3d) 289, (sub nom. *Elan Corp. v. Comiskey)* 41 O.A.C. 282 (Ont. C.A.) — referred to

Pacific National Lease Holding Corp., Re (1992), 72 B.C.L.R. (2d) 368, 19 B.C.A.C. 134, 34 W.A.C. 134, 15 C.B.R. (3d) 265 (B.C. C.A. [In Chambers]) — considered

Philip's Manufacturing Ltd., Re (1992), 9 C.B.R. (3d) 25, 67 B.C.L.R. (2d) 84, 4 B.L.R. (2d) 142 (B.C. C.A.) — considered

Philip's Manufacturing Ltd., Re (1992), 15 C.B.R. (3d) 57 (note), 143 N.R. 286 (note), 70 B.C.L.R. (2d) xxxiii (note), 15 B.C.A.C. 240 (note), 27 W.A.C. 240 (note), 6 B.L.R. (2d) 149 (note) (S.C.C.) — referred to

Quintette Coal Ltd. v. Nippon Steel Corp. (1990), 80 C.B.R. (N.S.) 98 (B.C. S.C.) — considered

Woodward's Ltd., Re (1993), 17 C.B.R. (3d) 236, 79 B.C.L.R. (2d) 257 (B.C. S.C.) — considered

Statutes considered:

Bankruptcy and Insolvency Act, R.S.C. 1985, c. B-3
Generally — referred to

Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36
Generally — considered
s. 11 — considered
s. 11(4) — considered

APPLICATION by holders of senior secured notes in corporation for order lifting stay of proceedings against them in *Companies' Creditors Arrangement Act* proceeding to allow for appointment of receiver and manager over assets and property charged in their favour and for order appointing court officer with exclusive right to negotiate sale of assets or shares of corporation's subsidiary.

***Paperny J.* (orally):**

1 Montreal Trust Company of Canada, Collateral Agent for the holders of the Senior Secured Notes, and the Bank of Nova Scotia Trust Company of New York, Trustee for the holders of the Senior Secured Notes, apply for the following relief:

> 1. In the CCAA proceeding (Action No. 0001-05071) an order lifting the stay of proceedings against them contained in the orders of this court

dated March 24, 2000 and April 19, 2000 to allow for the court-ordered appointment of Ernst & Young Inc. as receiver and manager over the assets and property charged in favour of the Senior Secured Noteholders; and

2. In Action No. 0001-05044, an order appointing Ernst & Young Inc. as a court officer with the exclusive right to negotiate the sale of the assets or shares of Canadian Regional Airlines (1998) Ltd.

2 Canadian Airlines Corporation ("CAC") is a Canadian based holding company which, through its majority owned subsidiary Canadian Airlines International Ltd. ("CAIL") provides domestic, U.S.-Canada transborder and international jet air transportation services. CAC also provides regional transportation through its subsidiary Canadian Regional Airlines (1998) Ltd. ("Canadian Regional"). Canadian Regional is not an applicant under the CCAA proceedings.

3 The Senior Secured Notes were issued under an Indenture dated April 24, 1998 between CAC and the Trustee. The principal face amount is $175 million U.S. As well, there is interest outstanding. The Senior Secured Notes are directly and indirectly secured by a diverse package of assets and property of the CCAA applicants, including spare engines, rotables, repairables, hangar leases and ground equipment. The security comprises the key operational assets of CAC and CAIL. The security also includes the outstanding shares of Canadian Regional and the $56 million intercompany indebtedness owed by Canadian Regional to CAIL.

4 Under the terms of the Indenture, CAC is required to make an offer to purchase the Senior Secured Notes where there is a "change of control" of CAC. It is submitted by the Senior Secured Noteholders that Air Canada indirectly acquired control of CAC on January 4, 2000 resulting in a change of control. Under the Indenture, CAC is then required to purchase the notes at 101 percent of the outstanding principal, interest and costs. CAC did not do so. According to the Trustee, an Event of Default occurred, and on March 6, 2000 the Trustee delivered Notices of Intention to Enforce Security under the Bankruptcy and Insolvency Act.

5 On March 24, 2000, the Senior Secured Noteholders commenced Action No. 0001-05044 and brought an application for the appointment of a receiver over their collateral. On the same day, CAC and CAIL were granted CCAA protection and the Senior Secured Noteholders adjourned their application for a receiver. However, the Senior Secured Noteholders made further application that day for orders that Ernst & Young be appointed monitor over their security and for weekly payments from CAC and CAIL of $500,000 U.S. These applications were dismissed.

6 The CCAA Plan filed on April 25, 2000, proposes that the Senior Secured Noteholders constitute a separate class and offers them two alternatives:

1. To accept repayment of less than the outstanding amount; or
2. To be unaffected by the CCAA Plan and realize on their security.

7 On April 26th, 2000, the Senior Secured Noteholders met and unanimously rejected the first option. They passed a resolution to take steps to realize on the security.

8 The Senior Secured Noteholders argue that the time has come to permit them to realize on their security. They have already rejected the Plan and see no utility in waiting to vote in this regard on May 26th, 2000, the date set by this court.

9 The Senior Secured Noteholders submit that since the CCAA proceedings began five weeks ago, the following has occurred:

-interest has continued to accrue at approximately $2 million U.S. per month;

-the security has decreased in value by approximately $6 million Canadian;

-the Collateral Agent and the Trustee have incurred substantial costs;

-no amounts have been paid for the continued use of the collateral, which is key to the operations of CAIL;

-no outstanding accrued interest has been paid; and- they are the only secured creditor not getting paid.

10 The Senior Secured Noteholders emphasize that one of the end results of the Plan is a transfer of CAIL's assets to Air Canada. The Senior Secured Noteholders assert that the Plan is sponsored by this very solvent proponent, who is in a position to pay them in full. They are argue that Air Canada has made an economic decision not to do so and instead is using the CCAA to achieve its own objectives at their expense, an inappropriate use of the Act.

11 The Senior Secured Noteholders suggest that the Plan will not be impacted if they are permitted to realize on their security now instead of after a formal rejection of the Plan at the court-scheduled vote on May 26, 2000. The Senior Secured Noteholders argue that for all of the preceding reasons lifting the stay would be in accordance with the spirit and intent of the CCAA.

12 The CCAA is remedial legislation which should be given a large and liberal interpretation: See, for example, *Citibank Canada v. Chase Manhattan Bank of Canada* (1991), 5 C.B.R. (3d) 165 (Ont. Gen. Div.). It is intended to permit the court to make orders which will effectively maintain the status quo for a period while the struggling company attempts to develop a plan to compromise its debts and ultimately continue operations for the benefit of both the company and its creditors: See for example, *Meridian Development Inc. v. Toronto Dominion*

Bank (1984), 52 C.B.R. (N.S.) 109 (Alta. Q.B.), and *Hongkong Bank of Canada v. Chef Ready Foods Ltd.* (1990), 4 C.B.R. (3d) 311 (B.C. C.A.).

13 This aim is facilitated by the power to stay proceedings provided by Section 11 of the Act. The stay power is the key element of the CCAA process.

14 The granting of a stay under Section 11 is discretionary. On the debtor's initial application, the court may order a stay at its discretion for a period not to exceed 30 days. The burden of proof to obtain a stay extension under Section 11(4) is on the debtor. The debtor must satisfy the court that circumstances exist that make the request for a stay extension appropriate and that the debtor has acted, and is acting, in good faith and with due diligence. CAC and CAIL discharged this burden on April 19, 2000. However, unlike under the Bankruptcy and Insolvency Act, there is no statutory test under the CCAA to guide the court in lifting a stay against a certain creditor.

15 In determining whether a stay should be lifted, the court must always have regard to the particular facts. However, in every order in a CCAA proceeding the court is required to balance a number of interests. McFarlane J.A. states in his closing remarks of his reasons in *Re Pacific National Lease Holding Corp.* (1992), 15 C.B.R. (3d) 265 (B.C. C.A. [In Chambers]):

> In supervising a proceeding under the C.C.A.A. orders are made, and orders are varied as changing circumstances require. Orders depend upon a careful and delicate balancing of a variety of interests and problems.

16 Also see Blair J.'s decision in *Campeau v. Olympia & York Developments Ltd.* (1992), 14 C.P.C. (3d) 339 (Ont. Gen. Div.), for another example of the balancing approach.

17 As noted above, the stay power is to be used to preserve the status quo among the creditors of the insolvent company. Huddart J., as she then was, commented on the status quo in *Re Alberta-Pacific Terminals Ltd.* (1991), 8 C.B.R. (3d) 99 (B.C. S.C.). She stated:

> The status quo is not always easy to find... Nor is it always easy to define. The preservation of the status quo cannot mean merely the preservation of the relative pre-stay debt status of each creditor. Other interests are served by the CCAA. Those of investors, employees, and landlords among them, and in the case of the Fraser Surrey terminal, the public too, not only of British Columbia, but also of the prairie provinces. The status quo is to be preserved in the sense that manoeuvres by creditors that would impair the financial position of the company while it attempts to reorganize are to be prevented, not in the sense that all creditors are to be treated equally or to be maintained at the same relative level. It is the company and all the interests its demise would affect that must be considered.

18 Further commentary on the status quo is contained in *Quintette Coal Ltd. v. Nippon Steel Corp.* (1990), 80 C.B.R. (N.S.) 98 (B.C. S.C.). Thackray J. comments that the maintenance of the status quo does not mean that every detail of

the status quo must survive. Rather, it means that the debtor will be able to stay in business and will have breathing space to develop a proposal to remain viable.

19 Finally, in making orders under the CCAA, the court must never lose sight of the objectives of the legislation. These were concisely summarized by the chambers judge and adopted by the British Columbia Court of Appeal in *Re Pacific National Lease Holding Corp.* (1992), 15 C.B.R. (3d) 265 (B.C. C.A. [In Chambers]):

> (1) The purpose of the CCAA is to allow an insolvent company a reasonable period of time to reorganize its affairs and prepare and file a plan for its continued operation subject to the requisite approval of the creditors and court.
>
> (2) The CCAA is intended to serve not only the company's creditors but also a broad constituency which includes the shareholders and employees.
>
> (3) During the stay period, the Act is intended to prevent manoeuvres for positioning amongst the creditors of the company.
>
> (4) The function of the court during the stay period is to play a supervisory role to preserve the status quo and to move the process along to the point where a compromise or arrangement is approved or it is evident that the attempt is doomed to failure.
>
> (5) The status quo does not mean preservation of the relative pre-stay debt status of each creditor. Since the companies under CCAA orders continue to operate and having regard to the broad constituency of interests the Act is intended to serve, the preservation of the status quo is not intended to create a rigid freeze of relative pre-stay positions.
>
> (6) The court has a broad discretion to apply these principles to the facts of th particular case.

20 At pages 342 and 343 of this text, Canadian Commercial Reorganization: Preventing Bankruptcy (Aurora: Canada Law Book, looseleaf), R.H. McLaren describes situations in which the court will lift a stay:

> 1. When the plan is likely to fail;
>
> 2. The applicant shows hardship (the hardship must be caused by the stay itself and be independent of any pre-existing condition of the applicant creditor);
>
> 3. The applicant shows necessity for payment (where the creditors' financial problems are created by the order or where the failure to pay the creditor would cause it to close and thus jeopardize the debtor's company's existence);
>
> 4. The applicant would be severely prejudiced by refusal to lift the stay and there would be no resulting prejudice to the debtor company or the positions of creditors;
>
> 5. It is necessary to permit the applicant to take steps to protect a right which could be lost by the passage of time;

6. After the lapse of a significant time period, the insolvent is no closer to a proposal than at the commencement of the stay period.

21 I now turn to the particular circumstances of the applications before me.

22 I would firstly address the matter of the Senior Secured Noteholders' current rejection of the compromise put forward under the Plan. Although they are in a separate class under CAC's Plan and can control the vote as it affects their interest, they are not in a position to vote down the Plan in its entirety. However, the Senior Secured Noteholders submit that where a plan offers two options to a class of creditors and the class has selected which option it wants, there is no purpose to be served in delaying that class from proceeding with its chosen course of action. They rely on the *Nova Metal Products Inc. v. Comiskey (Trustee of)* (1990), 1 C.B.R. (3d) 101 (Ont. C.A.) at 115, as just one of several cases supporting this proposition. *Re Philip's Manufacturing Ltd.* (1992), 9 C.B.R. (3d) 25 (B.C. C.A.) at pp. 27-28, leave to appeal to S.C.C. refused (1992), 15 C.B.R. (3d) 57 (note) (S.C.C.), would suggest that the burden is on the Senior Secured Noteholders to establish that the Plan is "doomed to fail". To the extent that Nova Metal and Philip's Manufacturing articulate different tests to meet in this context, the application of either would not favour the Senior Secured Noteholders.

23 The evidence before me suggests that progress may still be made in the negotiations with the representatives of the Senior Secured Noteholders and that it would be premature to conclude that any further discussions would be unsuccessful. The parties are continuing to explore revisions and alternative proposals which would satisfy the Senior Secured Noteholders.

24 Mr. Carty's affidavit sworn May 1, 2000, in response to these applications states his belief that these efforts are being made in good faith and that, if allowed to continue, there is a real prospect for an acceptable proposal to be made at or before the creditors' meeting on May 26, 2000. Ms. Allen's affidavit does not contain any assertion that negotiations will cease. Despite the emphatic suggestion of the Senior Secured Noteholders' counsel that negotiations would be "one way", realistically I do not believe that there is no hope of the Senior Secured Noteholders coming to an acceptable compromise.

25 Further, there is no evidence before me that would indicate the Plan is "doomed to fail". The evidence does disclose that CAC and CAIL have already achieved significant compromises with creditors and continue to work swiftly and diligently to achieve further progress in this regard. This is reflected in the affidavits of Mr. Carty and the reports from the Monitor.

26 In any case, there is a fundamental problem in the application of the Senior Secured Noteholders to have a receiver appointed in respect of their security which the certainty of a "no" vote at this time does not vitiate: It disregards the interests of the other stakeholders involved in the process. These include other secured creditors, unsecured creditors, employees, shareholders and the flying

public. It is not insignificant that the debtor companies serve an important national need in the operation of a national and international airline which employs tens of thousands of employees. As previously noted, these are all constituents the court must consider in making orders under the CCAA proceeding.

27 Paragraph 11 of Mr. Carty's May 1, 2000 affidavit states as follows:

> In my opinion, the continuation of the stay of proceedings to allow the restructuring process to continue will be of benefit to all stakeholders including the holders of the Senior Secured Notes. A termination of the stay proceedings as regards the security of the holders of the Senior Secured Notes would immediately deprive CAIL of assets which are critical to its operational integrity and would result in grave disruption of CAIL's operations and could lead to the cessation of operations. This would result in the destruction of value for all stakeholders, including the holders of the Senior Secured Notes. Furthermore, if CAIL ceased to operate, it is doubtful that Canadian Regional Airlines (1998) Ltd. ("CRAL98"), whose shares form a significant part of the security package of the holders of the Senior Secured Notes, would be in a position to continue operating and there would be a very real possibility that the equity of CAIL and CRAL, valued at approximately $115 million for the purposes of the issuance of the Senior Secured Notes in 1998, would be largely lost. Further, if such seizure caused CAIL to cease operations, the market for the assets and equipment which are subject to the security of the holders of the Senior Secured Notes could well be adversely affected, in that it could either lengthen the time necessary to realize on these assets or reduce realization values.

28 The alternative to this Plan proceeding is addressed in the Monitor's reports to the court. For example, in Paragraph 8 of the Monitor's third report to the court states:

> The Monitor believes the if the Plan is not approved and implemented, CAIL will not be able to continue as a going concern. In that case, the only foreseeable alternative would be a liquidation of CAIL's assets by a receiver and manager and/or by a trustee. Under the Plan, CAIL's obligations to parties it considers to be essential in order to continue operations, including employees, customers, travel agents, fuel, maintenance, catering and equipment suppliers, and airport authorities, are in most cases to be treated as unaffected and paid in full. In the event of a liquidation, those parties would not, in most cases, be paid in full and, except for specific lien rights, statutory priorities or other legal protection, would rank as ordinary unsecured creditors. The Monitor estimates that the additional unsecured claims which would arise if CAIL were to cease operation as a going concern and be forced into liquidation would be in excess of $1.1 billion.

29 This evidence is uncontradicted and flies in the face of the Senior Secured Noteholders' assertion that realizing on their collateral at this point in time will not affect the Plan. Although, as the Senior Secured Noteholders heavily empha-

sized the Plan does contemplate a "no" vote by the Senior Secured Noteholders, the removal of their security will follow that vote. 9.8(c) of the Plan states that:

> If the Required Majority of Affected Secured Noteholders fails to approve the Plan, arrangements in form and substance satisfactory to the Applicants will have been made with the Affected Secured Noteholders or with a receiver appointed over the assets comprising the Senior Notes Security, which arrangements provide for the transitional use by [CAIL], and subsequent sale, of the assets comprising the Senior Notes Security.

30 On the other side of the scale, the evidence of the Senior Secured Noteholders is that the value of their security is well in excess of what they are owed. Paragraph 15(a) of the Monitor's third report to the court values the collateral at $445 million. The evidence suggests that they are not the only secured creditor going unpaid. CAIL is asking that they be permitted to continue the restructuring process and their good faith efforts to attempt to reach an acceptable proposal with the Senior Secured Noteholders until the date of the creditors meeting, which is in three weeks. The Senior Secured Noteholders have not established that they will suffer any material prejudice in the intervening period.

31 The appointment of a receiver at this time would negate the effect of the order staying proceedings and thwart the purposes of the CCAA.

32 Accordingly, I am dismissing the application, with leave to reapply in the event that the Senior Secured Noteholders vote to reject the Plan on May 26, 2000.

33 An alternative to receivership raised by the Senior Secured Noteholders was interim payment for use of the security. The Monitor's third report makes it clear that the debtor's cash flow forecasts would not permit such payments.

34 The Senior Secured Noteholders suggested Air Canada could make the payments and, indeed, that Air Canada should pay out the debt owed to them by CAC. It is my view that, in the absence of abuse of the CCAA process, simply having a solvent entity financially supporting a plan with a view to ultimately obtaining an economic benefit for itself does not dictate that that entity should be required to pay creditors in full as requested. In my view, the evidence before me at this time does not suggest that the CCAA process is being improperly used. Rather, the evidence demonstrates these proceedings to be in furtherance of the objectives of the CCAA.

35 With respect to the application to sell shares or assets of Canadian Regional, this application raises a distinct issue in that Canadian Regional is not one of the debtor companies. In my view, Paragraph 5(a) of Chief Justice Moore's March 24, 2000 order encompasses marketing the shares or assets of Canadian Regional. That paragraph stays, inter alia:

> ...any and all proceedings ... against or in respect of ... any of the Petitioners' property ... whether held by the Petitioners directly or indirectly, as principal or nominee, beneficially or otherwise...

36 As noted above, Canadian Regional is CAC's subsidiary, and its shares and assets are the "property" of CAC and marketing of these would constitute a "proceeding ... in respect of ... the Petitioners' property" within the meaning of Paragraph 5(a) and Section 11 of the CCAA.

37 If I am incorrect in my interpretation of Paragraph 5(a), I rely on the inherent jurisdiction of the court in these proceedings.

38 As noted above, the CCAA is to be afforded a large and liberal interpretation. Two of the landmark decisions in this regard hail from Alberta: *Meridian Development Inc. v. Toronto Dominion Bank*, supra, and *Norcen Energy Resources Ltd. v. Oakwood Petroleums Ltd.* (1988), 72 C.B.R. (N.S.) 20 (Alta. Q.B.). At least one court has also recognized an inherent jurisdiction in relation to the CCAA in order to grant stays in relation to proceedings against third parties: *Re Woodward's Ltd.* (1993), 17 C.B.R. (3d) 236 (B.C. S.C.). Tysoe J. urged that although this power should be used cautiously, a prerequisite to its use should not be an inability to otherwise complete the reorganization. Rather, what must be shown is that the exercise of the inherent jurisdiction is important to the reorganization process. The test described by Tysoe J. is consistent with the critical balancing that must occur in CCAA proceedings. He states:

> In deciding whether to exercise its inherent jurisdiction, the court should weigh the interests of the insolvent company against the interests of parties who will be affected by the exercise of the inherent jurisdiction. If, in relative terms, the prejudice to the affected party is greater than the benefit that will be achieved by the insolvent company, the court should decline to its inherent jurisdiction. The threshold of prejudice will be much lower than the threshold required to persuade the court that it should not exercise its discretion under Section 11 of the CCAA to grant or continue a stay that is prejudicial to a creditor of the insolvent company (or other party affected by the stay).

39 The balancing that I have described above in the context of the receivership application equally applies to this application. While the threshold of prejudice is lower, the Senior Secured Noteholders still fail to meet it. I cannot see that it is important to the CCAA proceedings that the Senior Secured Noteholders get started on marketing Canadian Regional. Instead, it would be disruptive and endanger the CCAA proceedings which, on the evidence before me, have progressed swiftly and in good faith.

40 The application in Action No. 0001-05044 is dismissed, also with leave to reapply after the vote on May 26, 2000.

41 I appreciate that the Senior Secured Noteholders will be disappointed and likely frustrated with the outcome of these applications. I would emphasize that on the evidence before me their rights are being postponed and not eradicated. Any hardship they experience at this time must yield to the greater hardship that the debtor companies and the other constituents would suffer were the stay to be lifted at this time.

Application dismissed.

TAB 8

[Indexed as: **Lehndorff General Partner Ltd., Re**]

Re Companies' Creditors Arrangement Act,
R.S.C. 1985, c. C-36;
Re Courts of Justice Act, R.S.O. 1990, c. C-43;
Re plan of compromise in respect of LEHNDORFF GENERAL PARTNER LTD. (in its own capacity and in its capacity as general partner of LEHNDORFF UNITED PROPERTIES (CANADA), LEHNDORFF PROPERTIES (CANADA) and LEHNDORFF PROPERTIES (CANADA) II) and in respect of certain of their nominees LEHNDORFF UNITED PROPERTIES (CANADA) LTD., LEHNDORFF CANADIAN HOLDINGS LTD., LEHNDORFF CANADIAN HOLDINGS II LTD., BAYTEMP PROPERTIES LIMITED and 102 BLOOR STREET WEST LIMITED and in respect of THG LEHNDORFF VERMÖGENSVERWALTUNG GMBH (in its capacity as limited partner of LEHNDORFF UNITED PROPERTIES (CANADA))

Ontario Court of Justice (General Division – Commercial List)
Farley J.

Heard – December 24, 1992.
Judgment – January 6, 1993.

Corporations – Arrangements and compromises – Companies' Creditors Arrangement Act – Stay of proceedings – Stay being granted even where it would affect non-applicants that were not companies within meaning of Act – Business operations of applicants and non-applicants being so intertwined as to make stay appropriate.

The applicant companies were involved in property development and management and sought the protection of the *Companies' Creditors Arrangement Act* ("CCAA") in order that they could present a plan of compromise. They also sought a stay of all proceedings against the individual company applicants either in their own capacities or because of their interest in a larger group of companies. Each of the applicant companies was insolvent and had outstanding debentures issued under trust deeds. They proposed a plan of compromise among themselves and the holders of the debentures as well as those others of their secured and unsecured creditors deemed appropriate in the circumstances.

A question arose as to whether the court had the power to grant a stay of proceedings against non-applicants that were not companies and, therefore, not within the express provisions of the CCAA.

Held – The application was allowed.

It was appropriate, given the significant financial intertwining of the applicant companies, that a consolidated plan be approved. Further, each of the applicant

companies had a realistic possibility of being able to continue operating even though each was currently unable to meet all of its expenses. This was precisely the sort of situation in which all of the creditors would likely benefit from the application of the CCAA and in which it was appropriate to grant an order staying proceedings.

The inherent power of the court to grant stays can be used to supplement s. 11 of the CCAA when it is just and reasonable to do so. Clearly, the court had the jurisdiction to grant a stay in respect of any of the applicants that were companies fitting the criteria in the CCAA. However, the stay requested also involved limited partnerships where (1) the applicant companies acted on behalf of the limited partnerships, or (2) the stay would be effective against any proceedings taken by any party against the property assets and undertakings of the limited partnerships in which they held a direct interest. The business operations of the applicant companies were so intertwined with the limited partnerships that it would be impossible for a stay to be granted to the applicant companies that would affect their business without affecting the undivided interest of the limited partnerships in the business. As a result, it was just and reasonable to supplement s. 11 and grant the stay.

While the provisions of the CCAA allow for a cramdown of a creditor's claim, as well as the interest of any other person, anyone wishing to start or continue proceedings against the applicant companies could use the comeback clause in the order to persuade the court that it would not be just and reasonable to maintain the stay. In such a motion, the onus would be on the applicant companies to show that it was appropriate in the circumstances to continue the stay.

Cases considered

Amirault Fish Co., Re, 32 C.B.R. 186, [1951] 4 D.L.R. 203 (N.S. T.D.) – referred to.

Associated Investors of Canada Ltd., Re, 67 C.B.R. (N.S.) 237, 56 Alta. L.R. (2d) 259, [1988] 2 W.W.R. 211, 38 B.L.R. 148, (sub nom. *Re First Investors Corp.*) 46 D.L.R. (4th) 669 (Q.B.), reversed (1988), 71 C.B.R. 71, 60 Alta. L.R. (2d) 242, 89 A.R. 344 (C.A.) – referred to.

Campeau v. Olympia & York Developments Ltd. (1992), 14 C.B.R. (3d) 303 (Ont. Gen. Div.) – referred to.

Canada Systems Group (EST) v. Allen-Dale Mutual Insurance Co. (1982), 29 C.P.C. 60, 137 D.L.R. (3d) 287 (Ont. H.C.) [affirmed (1983), 41 O.R. (2d) 135, 33 C.P.C. 210, 145 D.L.R. (3d) 266 (C.A.)] – referred to.

Empire-Universal Films Ltd. v. Rank, [1947] O.R. 775 (H.C.) – referred to.

Feifer v. Frame Manufacturing Corp., Re, 28 C.B.R. 124, [1947] Que. K.B. 348 (C.A.) – referred to.

Fine's Flowers Ltd. v. Fine's Flowers (Creditors of) (1992), 10 C.B.R. (3d) 87, 4 B.L.R. (2d) 293, 87 D.L.R. (4th) 391, 7 O.R. (3d) 193 (Gen. Div.) – referred to.

Gaz Métropolitain v. Wynden Canada Inc. (1982), 44 C.B.R. (N.S.) 285 (Que. S.C.) [affirmed (1982), 45 C.B.R. (N.S.) 11 (Que. C.A.)] – referred to.

Hongkong Bank of Canada v. Chef Ready Foods Ltd. (1990), 4 C.B.R. (3d) 311, 51 B.C.L.R. (2d) 84, [1991] 2 W.W.R. 136 (C.A.) – referred to.

Inducon Development Corp. Re (1992), 8 C.B.R. (3d) 306 (Ont. Gen. Div.) – referred to.

International Donut Corp. v. 050863 N.B. Ltd. (1992), 127 N.B.R. (2d) 290, 319 A.P.R. 290 (Q.B.) – considered.

Keppoch Development Ltd., Re (1991), 8 C.B.R. (3d) 95 (N.S. T.D.) – referred to.

Langley's Ltd., Re, [1938] O.R. 123, [1938] 3 D.L.R. 230 (C.A.) – referred to.

McCordic v. Bosanquet (1974), 5 O.R. (2d) 53 (H.C.) – referred to.

Meridian Developments Inc. v. Toronto Dominion Bank, 52 C.B.R. (N.S.) 109, [1984] 5 W.W.R. 215, 32 Alta. L.R. (2d) 150, 53 A.R. 39, 11 D.L.R. (4th) 576 (Q.B.) – referred to.

Norcen Energy Resources Ltd. v. Oakwood Petroleums Ltd. (1988), 72 C.B.R. (N.S.) 1, 63 Alta. L.R. (2d) 361, 92 A.R. 1 (Q.B.) – referred to.

Northland Properties Ltd., Re (1988), 73 C.B.R. (N.S.) 141 (B.C. S.C.) – referred to.

Nova Metal Products Inc. v. Comiskey (Trustee of) (1990), 1 C.B.R. (3d) 101, (sub nom. *Elan Corp. v. Comiskey*) 41 O.A.C. 282, 1 O.R. (3d) 289 (C.A.) – referred to.

Quintette Coal Ltd. v. Nippon Steel Corp. (1990), 2 C.B.R. (3d) 303, 51 B.C.L.R. (2d) 105 (C.A.), affirming (1990), 2 C.B.R. (3d) 291, 47 B.C.L.R. (2d) 193 (S.C.), leave to appeal to S.C.C. refused (1991), 7 C.B.R. (3d) 164 (note), 55 B.C.L.R. (2d) xxxiii (note), 135 N.R. 317 (note) – referred to.

Reference re Companies' Creditors Arrangement Act (Canada), [1934] S.C.R. 659, 16 C.B.R. 1, [1934] 4 D.L.R. 75 – referred to.

Seven Mile Dam Contractors v. R. (1979), 13 B.C.L.R. 137, 104 D.L.R. (3d) 274 (S.C.), affirmed (1980), 25 B.C.L.R. 183 (C.A.) – referred to.

Sklar-Peppler Furniture Corp. v. Bank of Nova Scotia (1991), 8 C.B.R. (3d) 312, 86 D.L.R. (4th) 621 (Ont. Gen. Div.) – referred to.

Slavik, Re (1992), 12 C.B.R. (3d) 157 (B.C. S.C.) – considered.

Stephanie's Fashions Ltd., Re (1990), 1 C.B.R. (3d) 248 (B.C. S.C.) – referred to.

Ultracare Management Inc. v. Zevenberger (Trustee of) (1990), 3 C.B.R. (3d) 151, (sub nom. *Ultracare Management Inc. v. Gammon*) 1 O.R. (3d) 321 (Gen. Div.) – referred to.

United Maritime Fishermen Co-operative, Re (1988), 67 C.B.R. (N.S.) 44, 84 N.B.R. (2d) 415, 214 A.P.R. 415 (Q.B.), varied on reconsideration (1988), 68 C.B.R. (N.S.) 170, 87 N.B.R. (2d) 333, 221 A.P.R. 333 (Q.B.), reversed (1988), 69 C.B.R. (N.S.) 161, 88 N.B.R. (2d) 253, 224 A.P.R. 253, (sub nom. *Cdn. Co-op. Leasing Services v. United Maritime Fishermen Co-op.*) 51 D.L.R. (4th) 618 (C.A.) – referred to.

Statutes considered

Bankruptcy Act, R.S.C. 1985, c. B-3 –
- s. 85
- s. 142

Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36 –
- preamble
- s. 2
- s. 3
- s. 4
- s. 5
- s. 6
- s. 7
- s. 8
- s. 11

Courts of Justice Act, R.S.O. 1990, c. C.43.

Judicature Act, The, R.S.O. 1937, c. 100.

Limited Partnerships Act, R.S.O. 1990, c. L.16 –
- s. 2(2)
- s. 3(1)
- s. 8
- s. 9

s. 11
s. 12(1)
s. 13
s. 15(2)
s. 24
Partnership Act, R.S.A. 1980, c. P-2 –
Pt. 2
s. 75

Rules considered
Ontario, Rules of Civil Procedure –
r. 8.01
r. 8.02

APPLICATION under *Companies' Creditors Arrangement Act* to file consolidated plan of compromise and for stay of proceedings.

Alfred Apps, Robert Harrison and *Melissa J. Kennedy*, for applicants.

L. Crozier, for Royal Bank of Canada.

R.C. Heintzman, for Bank of Montreal.

J. Hodgson, Susan Lundy and *James Hilton*, for Canada Trustco Mortgage Corporation.

Jay Schwartz, for Citibank Canada.

Stephen Golick, for Peat Marwick Thorne* Inc., proposed monitor.

John Teolis, for Fuji Bank Canada.

Robert Thorton, for certain of the advisory boards.

(Doc. B366/92)

1 January 6, 1993. FARLEY J.: – These are my written reasons relating to the relief granted the applicants on December 24, 1992 pursuant to their application under the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36 ("CCAA") and the *Courts of Justice Act*, R.S.O. 1990, c. C.43 ("CJA"). The relief sought was as follows:

(a) short service of the notice of application;

(b) a declaration that the applicants were companies to which the CCAA applies;

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*As amended by the court.

(c) authorization for the applicants to file a consolidated plan of compromise;

(d) authorization for the applicants to call meetings of their secured and unsecured creditors to approve the consolidated plan of compromise;

(e) a stay of all proceedings taken or that might be taken either in respect of the applicants in their own capacity or on account of their interest in Lehndorff United Properties (Canada) ("LUPC"), Lehndorff Properties (Canada) ("LPC") and Lehndorff Properties (Canada) II ("LPC II") and collectively (the "Limited Partnerships") whether as limited partner, as general partner or as registered titleholder to certain of their assets as bare trustee and nominee; and

(f) certain other ancillary relief.

2 The applicants are a number of companies within the larger Lehndorff group ("Group") which operates in Canada and elsewhere. The group appears to have suffered in the same way that a number of other property developers and managers which have also sought protection under the CCAA in recent years. The applicants are insolvent; they each have outstanding debentures issues under trust deeds; and they propose a plan of compromise among themselves and the holders of these debentures as well as those others of their secured and unsecured creditors as they deemed appropriate in the circumstances. Each applicant except THG Lehndorff Vermögensverwaltung GmbH ("GmbH") is an Ontario corporation. GmbH is a company incorporated under the laws of Germany. Each of the applicants has assets or does business in Canada. Therefore each is a "company" within the definition of s. 2 of the CCAA. The applicant Lehndorff General Partner Ltd. ("General Partner Company") is the sole general partner of the Limited Partnerships. The General Partner Company has sole control over the property and businesses of the Limited Partnerships. All major decisions concerning the applicants (and the Limited Partnerships) are made by management operating out of the Lehndorff Toronto Office. The applicants aside from the General Partner Company have as their sole purpose the holding of title to properties as bare trustee or nominee on behalf of the Limited Partnerships. LUPC is a limited partnership registered under the *Limited Partnership Act*, R.S.O. 1990, c. L.16 ("Ontario LPA"). LPC and LPC II are limited partnerships registered under Part 2 of the *Partnership Act*, R.S.A. 1980, c. P-2 ("Alberta PA") and each is registered in Ontario as an extra provincial limited partnership. LUPC has

over 2,000 beneficial limited partners, LPC over 500 and LPC II over 250, most of whom are residents of Germany. As at March 31, 1992 LUPC had outstanding indebtedness of approximately $370 million, LPC $45 million and LPC II $7 million. Not all of the members of the Group are making an application under the CCAA. Taken together the Group's indebtedness as to Canadian matters (including that of the applicants) was approximately $543 million. In the summer of 1992 various creditors (Canada Trustco Mortgage Company, Bank of Montreal, Royal Bank of Canada, Canadian Imperial Bank of Commerce and the Bank of Tokyo Canada) made demands for repayment of their loans. On November 6, 1992 Funtanua Investments Limited, a minor secured lendor also made a demand. An interim standstill agreement was worked out following a meeting of July 7, 1992. In conjunction with Peat Marwick Thorne Inc. which has been acting as an informal monitor to date and Fasken Campbell Godfrey the applicants have held multiple meetings with their senior secured creditors over the past half year and worked on a restructuring plan. The business affairs of the applicants (and the Limited Partnerships) are significantly intertwined as there are multiple instances of inter-corporate debt, cross-default provisions and guarantees and they operated a centralized cash management system.

3 This process has now evolved to a point where management has developed a consolidated restructuring plan which plan addresses the following issues:

(a) The compromise of existing conventional, term and operating indebtedness, both secured and unsecured.

(b) The restructuring of existing project financing commitments.

(c) New financing, by way of equity or subordinated debt.

(d) Elimination or reduction of certain overhead.

(e) Viability of existing businesses of entities in the Lehndorff Group.

(f) Restructuring of income flows from the limited partnerships.

(g) Disposition of further real property assets aside from those disposed of earlier in the process.

(h) Consolidation of entities in the Group; and

(i) Rationalization of the existing debt and security structure in the continuing entities in the Group.

Formal meetings of the beneficial limited partners of the Limited Partnerships are scheduled for January 20 and 21, 1993 in Germany and an information circular has been prepared and at the time of hearing was being translated into German. This application was brought on for hearing at this time for two general reasons: (a) it had now ripened to the stage of proceeding with what had been distilled out of the strategic and consultative meetings; and (b) there were creditors other than senior secured lenders who were in a position to enforce their rights against assets of some of the applicants (and Limited Partnerships) which if such enforcement did take place would result in an undermining of the overall plan. Notice of this hearing was given to various creditors: Barclays Bank of Canada, Barclays Bank PLC, Bank of Montreal, Citibank Canada, Canada Trustco Mortgage Corporation, Royal Trust Corporation of Canada, Royal Bank of Canada, the Bank of Tokyo Canada, Funtauna Investments Limited, Canadian Imperial Bank of Commerce, Fuji Bank Canada and First City Trust Company. In this respect the applicants have recognized that although the initial application under the CCAA may be made on an ex parte basis (s. 11 of the CCAA; *Re Langley's Ltd.*, [1938] O.R. 123, [1938] 3 D.L.R. 230 (C.A.); *Re Keppoch Development Ltd.* (1991), 8 C.B.R. (3d) 95 (N.S. T.D.). The court will be concerned when major creditors have not been alerted even in the most minimal fashion (*Re Inducon Development Corp.* (1992), 8 C.B.R. (3d) 306 (Ont. Gen. Div.) at p. 310). The application was either supported or not opposed.

4 "Instant" debentures are now well recognized and respected by the courts: see *Re United Maritime Fishermen Co-operative* (1988), 67 C.B.R. (N.S.) 44 (N.B. Q.B.), at pp. 55-56, varied on reconsideration (1988), 68 C.B.R. (N.S.) 170 (N.B. Q.B.), reversed on different grounds (1988), 69 C.B.R. (N.S.) 161 (N.B. C.A.), at pp. 165-166; *Re Stephanie's Fashions Ltd.* (1990), 1 C.B.R. (3d) 248 (B.C. S.C.) at pp. 250-251; *Nova Metal Products Inc. v. Comiskey (Trustee of)* (sub nom. *Elan Corp. v. Comiskey*) (1990), 1 O.R. (3d) 289, 1 C.B.R. (3d) 101 (C.A.) per Doherty J.A., dissenting on another point, at pp. 306-310 (O.R.); *Ultracare Management Inc. v. Zevenberger (Trustee of)* (sub nom. *Ultracare Management Inc. v. Gammon*) (1990), 1 O.R. (3d) 321 (Gen. Div.) at p. 327. The applicants would appear to me to have met the technical hurdle of s. 3 and as defined s. 2) of the CCAA in that they are debtor companies since they are insolvent, they have outstanding an issue of debentures under a trust deed and the compromise or arrangement that is proposed includes that compromise between the applicants and the holders of those trust

deed debentures. I am also satisfied that because of the significant intertwining of the applicants it would be appropriate to have a consolidated plan. I would also understand that this court (Ontario Court of Justice (General Division)) is the appropriate court to hear this application since all the applicants except GmbH have their head office or their chief place of business in Ontario and GmbH, although it does not have a place of business within Canada, does have assets located within Ontario.

5 The CCAA is intended to facilitate compromises and arrangements between companies and their creditors as an alternative to bankruptcy and, as such, is remedial legislation entitled to a liberal interpretation. It seems to me that the purpose of the statute is to enable insolvent companies to carry on business in the ordinary course or otherwise deal with their assets so as to enable plan of compromise or arrangement to be prepared, filed and considered by their creditors and the court. In the interim, a judge has great discretion under the CCAA to make order so as to effectively maintain the status quo in respect of an insolvent company while it attempts to gain the approval of its creditors for the proposed compromise or arrangement which will be to the benefit of both the company and its creditors. See the preamble to and sections 4, 5, 6, 7, 8 and 11 of the CCAA; *Reference re Companies' Creditors Arrangement Act*, [1934] S.C.R. 659 at p. 661, 16 C.B.R. 1, [1934] 4 D.L.R. 75; *Meridian Developments Inc. v. Toronto Dominion Bank*, [1984] 5 W.W.R. 215 (Alta. Q.B.) at pp. 219-220; *Norcen Energy Resources Ltd. v. Oakwood Petroleums Ltd.* (1988), 72 C.B.R. (N.S.) 1, 63 Alta. L.R. (2d) 361 (Q.B.), at pp. 12-13 (C.B.R.); *Quintette Coal Ltd. v. Nippon Steel Corp.* (1990), 2 C.B.R. (3d) 303 (B.C. C.A.), at pp. 310-311, affirming (1990), 2 C.B.R. (3d) 291, 47 B.C.L.R. (2d) 193 (S.C.), leave to appeal to S.C.C. dismissed (1991), 7 C.B.R. (3d) 164 (S.C.C.).; *Nova Metal Products Inc. v. Comiskey (Trustee of)*, supra, at p. 307 (O.R.); *Fine's Flowers v. Fine's Flowers (Creditors of)* (1992), 7 O.R. (3d) 193 (Gen. Div.), at p. 199 and "Reorganizations Under The Companies' Creditors Arrangement Act", Stanley E. Edwards (1947) 25 Can. Bar Rev. 587 at p. 592.

6 The CCAA is intended to provide a structured environment for the negotiation of compromises between a debtor company and its creditors for the benefit of both. Where a debtor company realistically plans to continue operating or to otherwise deal with its assets but it requires the protection of the court in order to do so and it is otherwise too early for the court to determine whether the debtor company will succeed, relief should be granted under the CCAA. see *Nova Metal Products Inc. v. Comiskey (Trustee of)*, supra at pp. 297 and 316; *Re Stephanie's Fashions Ltd.*, supra, at pp. 251-252 and *Ultracare Management Inc. v. Zevenberger (Trustee of)*, supra, at p. 328 and

p. 330. It has been held that the intention of the CCAA is to prevent any manoeuvres for positioning among the creditors during the period required to develop a plan and obtain approval of creditors. Such manoeuvres could give an aggressive creditor an advantage to the prejudice of others who are less aggressive and would undermine the company's financial position making it even less likely that the plan will succeed: see *Meridian Developments Inc. v. Toronto Dominion Bank*, supra, at p. 220 (W.W.R.). The possibility that one or more creditors may be prejudiced should not affect the court's exercise of its authority to grant a stay of proceedings under the CCAA because this affect is offset by the benefit to all creditors and to the company of facilitating a reorganization. The court's primary concerns under the CCAA must be for the debtor and *all* of the creditors: see *Quintette Coal Ltd. v. Nippon Steel Corp.*, supra, at pp. 108-110; *Hongkong Bank of Canada v. Chef Ready Foods Ltd.* (1990), 4 C.B.R. (3d) 311, 51 B.C.L.R. (2d) 84 (C.A.), at pp. 315-318 (C.B.R.) and *Re Stephanie's Fashions Ltd.*, supra, at pp. 251-252.

7 One of the purposes of the CCAA is to facilitate ongoing operations of a business where its assets have a greater value as part of an integrated system than individually. The CCAA facilitates reorganization of a company where the alternative, sale of the property piecemeal, is likely to yield far less satisfaction to the creditors. Unlike the *Bankruptcy Act*, R.S.C. 1985, c. B-3, before the amendments effective November 30, 1992 to transform it into the *Bankruptcy and Insolvency Act* ("BIA"), it is possible under the CCAA to bind secured creditors it has been generally speculated that the CCAA will be resorted to by companies that are generally larger and have a more complicated capital structure and that those companies which make an application under the BIA will be generally smaller and have a less complicated structure. Reorganization may include partial liquidation where it is intended as part of the process of a return to long term viability and profitability. See *Hongkong Bank of Canada v. Chef Ready Foods Ltd.*, supra, at p. 318 and *Re Associated Investors of Canada Ltd.* (1987), 67 C.B.R. (N.S.) 237 (Alta. Q.B.) at pp. 245, reversed on other grounds at (1988), 71 C.B.R. (N.S.) 71 (Alta. C.A.). It appears to me that the purpose of the CCAA is also to protect the interests of creditors and to enable an orderly distribution of the debtor company's affairs. This may involve a winding-up or liquidation of a company or simply a substantial downsizing of its business operations, provided the same is proposed in the best interests of the creditors generally. See *Re Associated Investors of Canada Ltd.*, supra, at p. 318; *Re Amirault Fish Co.*, 32 C.B.R. 186, [1951] 4 D.L.R. 203 (N.S. T.D.) at pp. 187-188 (C.B.R.).

8 It strikes me that each of the applicants in this case has a realistic possibility of being able to continue operating, although each is

currently unable to meet all of its expenses albeit on a reduced scale. This is precisely the sort of circumstance in which all of the creditors are likely to benefit from the application of the CCAA and in which it is appropriate to grant an order staying proceedings so as to allow the applicant to finalize preparation of and file a plan of compromise and arrangement.

9 Let me now review the aspect of the stay of proceedings. Section 11 of the CCAA provides as follows:

> 11. Notwithstanding anything in the *Bankruptcy Act* or the *Winding-up Act*, whenever an application has been made under this Act in respect of any company, the court, on the application of any person interested in the matter, may, on notice to any other person or without notice as it may see fit,
>
> (*a*) make an order staying, until such time as the court may prescribe or until any further order, all proceedings taken or that might be taken in respect of the company under the *Bankruptcy Act* and the *Winding-up Act* or either of them;
>
> (*b*) restrain further proceedings in any action, suit or proceeding against the company on such terms as the court sees fit; and
>
> (*c*) make an order that no suit, action or other proceeding shall be proceeded with or commenced against the company except with the leave of the court and subject to such terms as the court imposes.

10 The power to grant a stay of proceeding should be construed broadly in order to permit the CCAA to accomplish its legislative purpose and in particular to enable continuance of the company seeking CCAA protection. The power to grant a stay therefore extends to a stay which affected the position not only of the company's secured and unsecured creditors, but also all non-creditors and other parties who could potentially jeopardize the success of the plan and thereby the continuance of the company. See *Norcen Energy Resources Ltd. v. Oakwood Petroleums Ltd.*, supra, at pp. 12-17 (C.B.R.) and *Quintette Coal Ltd. v. Nippon Steel Corp.*, supra, at pp. 296-298 (B.C. S.C.) and pp. 312-314 (B.C. C.A.) and *Meridian Developments Inc. v. Toronto Dominion Bank*, supra, at pp. 219 ff. Further the court has the power to order a stay that is effective in respect of the rights arising in favour of secured creditors under all forms of commercial security: see *Hongkong Bank of Canada v. Chef Ready Foods Ltd.*, supra, at p. 320 where Gibbs J.A. for the court stated:

> The trend which emerges from this sampling will be given effect here by holding that where the word "security" occurs in the C.C.A.A., it includes s. 178 security and, where the word creditor occurs, it includes a bank holding s. 178 security. To the extent that there may be conflict between the two statutes, therefore, the broad

scope of the C.C.A.A. prevails.

11 The power to grant a stay may also extend to preventing persons seeking to terminate or cancel executory contracts, including, without limitation agreements with the applying companies for the supply of goods or services, from doing so: see *Gaz Métropolitain v. Wynden Canada Inc.* (1982), 44 C.B.R. (N.S.) 285 (Que. S.C.) at pp. 290-291 and *Quintette Coal Ltd. v. Nippon Steel Corp.*, supra, at pp. 311-312 (B.C. C.A.). The stay may also extend to prevent a mortgagee from proceeding with foreclosure proceedings (see *Re Northland Properties Ltd.* (1988), 73 C.B.R. (N.S.) 141 (B.C. S.C.) or to prevent landlords from terminating leases, or otherwise enforcing their rights thereunder (see *Feifer v. Frame Manufacturing Corp.* (1947), 28 C.B.R. 124 (Que. C.A.)). Amounts owing to landlords in respect of arrears of rent or unpaid rent for the unexpired portion of lease terms are properly dealt with in a plan of compromise or arrangement: see *Sklar-Peppler Furniture Corp. v. Bank of Nova Scotia* (1991), 8 C.B.R. (3d) 312 (Ont. Gen. Div.) especially at p. 318. The jurisdiction of the court to make orders under the CCAA in the interest of protecting the debtor company so as to enable it to prepare and file a plan is effective notwithstanding the terms of any contract or instrument to which the debtor company is a party. Section 8 of the CCAA provides:

> 8. This Act extends and does not limit the provisions of any instrument now or hereafter existing that governs the rights of creditors or any class of them and has full force and effect notwithstanding anything to the contrary contained in that instrument.

The power to grant a stay may also extend to prevent persons from exercising any right of set off in respect of the amounts owed by such a person to the debtor company, irrespective of whether the debtor company has commenced any action in respect of which the defense of set off might be formally asserted: see *Quintette Coal Ltd. v. Nippon Steel Corp.*, supra, at pp. 312-314 (B.C.C.A.).

12 It was submitted by the applicants that the power to grant a stay of proceedings may also extend to a stay of proceedings against non-applicants who are not companies and accordingly do not come within the express provisions of the CCAA. In support thereof they cited a CCAA order which was granted staying proceedings against individuals who guaranteed the obligations of a debtor-applicant which was a qualifying company under the terms of the CCAA: see *Re Slavik*, unreported, [1992] B.C.J. No. 341 [now reported at 12 C.B.R. (3d) 157 (B.C. S.C.)]. However in the *Slavik* situation the individual guarantors were officers and shareholders of two companies which had sought and obtained CCAA protection. Vickers J. in that case indicated that the facts of that case included the following unexplained and unamplified fact [at p. 159]:

> 5. The order provided further that all creditors of Norvik Timber Inc. be enjoined from making demand for payment upon that firm or upon any guarantor of an obligation of the firm until further order of the court.

The CCAA reorganization plan involved an assignment of the claims of the creditors to "Newco" in exchange for cash and shares. However the basis of the stay order originally granted was not set forth in this decision.

13 It appears to me that Dickson J. in *International Donut Corp. v. 050863 N.D. Ltd.*, unreported, [1992] N.B.J. No. 339 (N.B. Q.B.) [now reported at 127 N.B.R. (2d) 290, 319 A.P.R. 290] was focusing only on the stay arrangements of the CCAA when concerning a limited partnership situation he indicated [at p. 295 N.B.R.]:

> In August 1991 the limited partnership, through its general partner the plaintiff, applied to the Court under the *Companies' Creditors Arrangement Act*, R.S.C., c. C-36 for an order delaying the assertion of claims by creditors until an opportunity could be gained to work out with the numerous and sizable creditors a compromise of their claims. An order was obtained but it in due course expired without success having been achieved in arranging with creditors a compromise. *That effort may have been wasted, because it seems questionable that the federal Act could have any application to a limited partnership in circumstances such as these.* (Emphasis added.)

14 I am not persuaded that the words of s. 11 which are quite specific as relating as to a *company* can be enlarged to encompass something other than that. However it appears to me that Blair J. was clearly in the right channel in his analysis in *Campeau v. Olympia & York Developments Ltd.* unreported, [1992] O.J. No. 1946 [now reported at 14 C.B.R. (3d) 303 (Ont. Gen. Div.)] at pp. 4-7 [at pp. 308-310 C.B.R.].

> *The Power to Stay*
>
> The court has always had an inherent jurisdiction to grant a stay of proceedings whenever it is just and convenient to do so, in order to control its process or prevent an abuse of that process: see *Canada Systems Group (EST) Ltd. v. Allendale Mutual Insurance Co.* (1982), 29 C.P.C. 60, 137 D.L.R. (3d) 287 (Ont. H.C.), and cases referred to therein. In the civil context, this general power is also embodied in the very broad terms of s. 106 of the *Courts of Justice Act*, R.S.O. 1990, c. C.43, which provides as follows:
>
> "106. A court, on its own initiative or on motion by any person, whether or not a party, may stay any proceeding in the court on such terms as are considered just."
>
> Recently, Mr. Justice O'Connell has observed that this discre-

tionary power is "highly dependent on the facts of each particular case": *Arab Monetary Fund v. Hashim* (unreported) [(June 25, 1992), Doc. 24127/88 (Ont. Gen. Div.)], [1992] O.J. No. 1330.

Apart from this inherent and general jurisdiction to stay proceedings, there are many instances where the court is specifically granted the power to stay in a particular context, by virtue of statute or under the *Rules of Civil Procedure*. The authority to prevent multiplicity of proceedings in the same court, under r. 6.01(1), is an example of the latter. The power to stay judicial and extra-judicial proceedings under s. 11 of the C.C.A.A., is an example of the former. Section 11 of the C.C.A.A. provides as follows.

The Power to Stay in the Context of C.C.A.A. Proceedings

By its formal title the C.C.A.A. is known as "An Act to facilitate compromises and arrangements between companies and their creditors". To ensure the effective nature of such a "facilitative" process it is essential that the debtor company be afforded a respite from the litigious and other rights being exercised by creditors, while it attempts to carry on as a going concern and to negotiate an acceptable corporate restructuring arrangement with such creditors.

In this respect it has been observed that the C.C.A.A. is "to be used as a practical and effective way of restructuring corporate indebtedness.": see the case comment following the report of *Norcen Energy Resources Ltd. v. Oakwood Petroleums Ltd.* (1988), 72 C.B.R. (N.S.) 1, 63 Alta. L.R. (2d) 361, 92 A.R. 81 (Q.B.), and the approval of that remark as "a perceptive observation about the attitude of the courts" by Gibbs J.A. in *Quintette Coal Ltd. v. Nippon Steel Corp.* (1990), 51 B.C.L.R. (2d) 105 (C.A.) at p. 113 [B.C.L.R.].

Gibbs J.A. continued with this comment:

"To the extent that a general principle can be extracted from the few cases directly on point, and the others in which there is persuasive obiter, it would appear to be that the courts have concluded that under s. 11 there is *a discretionary power to restrain judicial or extra-judicial conduct* against the debtor company *the effect of which is, or would be, seriously to impair the ability of the debtor company to continue in business during the compromise or arrangement negotiating period.*" (emphasis added)

I agree with those sentiments and would simply add that, in my view, the restraining power extends as well to conduct which could seriously impair the debtor's ability to focus and concentrate its efforts on the business purpose of negotiating the compromise or arrangement. [In this respect, see also *Sairex GmbH v. Prudential Steel Ltd.* (1991), 8 C.B.R. (3d) 62 (Ont. Gen. Div.) at p. 77.]

I must have regard to these foregoing factors while I consider, as well, the general principles which have historically governed the court's exercise of its power to stay proceedings. These principles

> were reviewed by Mr. Justice Montgomery in *Canada Systems Group (EST) Ltd. v. Allendale Mutual Insurance*, supra (a "Mississauga Derailment" case), at pp. 65-66 [C.P.C.]. The balance of convenience must weigh significantly in favour of granting the stay, as a party's right to have access to the courts must not be lightly interfered with. The court must be satisfied that a continuance of the proceeding would serve as an injustice to the party seeking the stay, in the sense that it would be oppressive or vexatious or an abuse of the process of the court in some other way. The stay must not cause an injustice to the plaintiff.

It is quite clear from *Empire-Universal Films Limited v. Rank*, [1947] O.R. 775 (H.C.) that McRuer C.J.H.C. considered that *The Judicature Act* [R.S.O. 1937, c. 100] then [and now the CJA] merely confirmed a statutory right that previously had been considered inherent in the jurisdiction of the court with respect to its authority to grant a stay of proceedings. See also *McCordic v. Bosanquet* (1974), 5 O.R. (2d) 53 (H.C.) and *Canada Systems Group (EST) Ltd. v. Allen-Dale Mutual Insurance Co.* (1982), 29 C.P.C. 60 (H.C.) at pp. 65-66.

15 Montgomery J. in *Canada Systems*, supra, at pp. 65-66 indicated:

> Goodman J. (as he then was) in *McCordic v. Bosanquet* (1974), 5 O.R. (2d) 53 in granting a stay reviewed the authorities and concluded that the inherent jurisdiction of the Court to grant a stay of proceedings may be made whenever it is just and reasonable to do so. "This court has ample jurisdiction to grant a stay whenever it is just and reasonable to do so." (Per Lord Denning M.R. in *Edmeades v. Thames Board Mills Ltd.*, [1969] 2 Q.B. 67 at 71, [1969] 2 All E.R. 127 (C.A.)). Lord Denning's decision in *Edmeades* was approved by Lord Justice Davies in *Lane v. Willis; Lane v. Beach (Executor of Estate of George William Willis)*, [1972] 1 All E.R. 430, [1972] 1 W.L.R. 326 (*sub nom. Lane v. Willis; Lane v. Beach*) (C.A.).
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> . . .
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> In *Weight Watchers Int. Inc. v. Weight Watchers of Ont. Ltd.* (1972), 25 D.L.R. (3d) 419, 5 C.P.R. (2d) 122, appeal allowed by consent without costs (*sub nom. Weight Watchers of Ont. Ltd. v. Weight Watchers Inc. Inc.*) 42 D.L.R. (3d) 320n, 10 C.P.R. (2d) 96n (Fed. C.A.), Mr. Justice Heald on an application for stay said at p. 426 [25 D.L.R.]:
>
> "The principles which must govern in these matters are clearly stated in the case of *Empire Universal Films Ltd. et al. v. Rank et al.*, [1947] O.R. 775 at p. 779, as follows [quoting *St. Pierre et al. v. South American Stores (Gath & Chaves), Ltd. et al.*, [1936] 1 K.B. 382 at p. 398]:
>
> '(1.) A mere balance of convenience is not a sufficient ground for depriving a plaintiff of the advantages of prosecuting his action in an English Court if it is otherwise properly brought. The right of access

> to the King's Court must not be lightly refused. (2.) In order to justify a stay two conditions must be satisfied, one positive and the other negative: (a) the defendant must satisfy the Court that the continuance of the action would work an injustice because it would be oppressive or vexatious to him or would be an abuse of the process of the Court in some other way; and (b) the stay must not cause an injustice to the plaintiff. On both the burden of proof is on the defendant.' "

16 Thus it appears to me that the inherent power of this court to grant stays can be used to supplement s. 11 of the CCAA when it is just and reasonable to do so. Is it appropriate to do so in the circumstances? Clearly there is jurisdiction under s. 11 of the CCAA to grant a stay in respect of any of the applicants which are all companies which fit the criteria of the CCAA. However the stay requested also involved the limited partnerships to some degree either (i) with respect to the applicants acting on behalf of the Limited Partnerships or (ii) the stays being effective vis-à-vis any proceedings taken by any party against the property assets and undertaking of the Limited Partnerships in respect of which they hold a direct interest (collectively the "Property") as set out in the terms of the stay provisions of the order paragraphs 4 through 18 inclusive attached as an appendix to these reasons. [Appendix omitted.] I believe that an analysis of the operations of a limited partnership in this context would be beneficial to an understanding of how there is a close inter-relationship to the applicants involved in this CCAA proceedings and how the Limited Partnerships and their Property are an integral part of the operations previously conducted and the proposed restructuring.

17 A limited partnership is a creation of statute, consisting of one or more general partners and one or more limited partners. The limited partnership is an investment vehicle for passive investment by limited partners. It in essence combines the flow through concept of tax depreciation or credits available to "ordinary" partners under general partnership law with limited liability available to shareholders under corporate law. See Ontario LPA sections 2(2) and 3(1) and Lyle R. Hepburn, *Limited Partnerships*, (Toronto: De Boo, 1991), at p. 1-2 and p. 1-12. I would note here that the limited partnership provisions of the Alberta PA are roughly equivalent to those found in the Ontario LPA with the interesting side aspect that the Alberta legislation in s. 75 does allow for judgment against a limited partner to be charged against the limited partner's interest in the limited partnership. A general partner has all the rights and powers and is subject to all the restrictions and liabilities of a partner in a partnership. In particular a general partner is fully liable to each creditor of the business of the limited partnership. The general partner has sole control over the property and business of the limited partnership: see Ontario LPA

ss. 8 and 13. Limited partners have no liability to the creditors of the limited partnership's business; the limited partners' financial exposure is limited to their contribution. The limited partners do not have any "independent" ownership rights in the property of the limited partnership. The entitlement of the limited partners is limited to their contribution plus any profits thereon, after satisfaction of claims of the creditors. See Ontario LPA sections 9, 11, 12(1), 13, 15(2) and 24. The process of debtor and creditor relationships associated with the limited partnership's business are between the general partner and the creditors of the business. In the event of the creditors collecting on debt and enforcing security, the creditors can only look to the assets of the limited partnership together with the assets of the general partner including the general partner's interest in the limited partnership. This relationship is recognized under the *Bankruptcy Act* (now the BIA) sections 85 and 142.

18 A general partner is responsible to defend proceedings against the limited partnership in the firm name, so in procedural law and in practical effect, a proceeding against a limited partnership is a proceeding against the general partner. See Ontario *Rules of Civil Procedure*, O. Reg. 560/84, Rules 8.01 and 8.02.

19 It appears that the preponderance of case law supports the contention that contention that a partnership including a limited partnership is not a separate legal entity. See *Lindley on Partnership*, 15th ed. (London: Sweet & Maxwell, 1984), at pp. 33-35; *Seven Mile Dam Contractors v. R.* (1979), 13 B.C.L.R. 137 (S.C.), affirmed (1980), 25 B.C.L.R. 183 (C.A.) and "Extra-Provincial Liability of the Limited Partner", Brad A. Milne, (1985) 23 Alta. L. Rev. 345, at pp. 350-351. Milne in that article made the following observations:

> The preponderance of case law therefore supports the contention that a limited partnership is not a separate legal entity. It appears, nevertheless, that the distinction made in *Re Thorne* between partnerships and trade unions could not be applied to limited partnerships which, like trade unions, must rely on statute for their validity. The mere fact that limited partnerships owe their existence to the statutory provision is probably not sufficient to endow the limited partnership with the attribute of legal personality as suggested in *Ruzicks* unless it appeared that the Legislature clearly intended that the limited partnership should have a separate legal existence. A review of the various provincial statutes does not reveal any procedural advantages, rights or powers that are fundamentally different from those advantages enjoyed by ordinary partnerships. The legislation does not contain any provision resembling section 15 of the *Canada Business Corporation Act* [S.C. 1974-75, c. 33, as am.] which expressly states that a corporation has the capacity, both in and outside of Canada, of a natural person. It is therefore difficult to imagine that the Legislature intended to create a new category of legal entity.

20 It appears to me that the operations of a limited partnership in the ordinary course are that the limited partners take a completely passive role (they must or they will otherwise lose their limited liability protection which would have been their sole reason for choosing a limited partnership vehicle as opposed to an "ordinary" partnership vehicle). For a lively discussion of the question of "control" in a limited partnership as contrasted with shareholders in a corporation, see R. Flannigan, "The Control Test of Investor Liability in Limited Partnerships" (1983) 21 Alta. L. Rev. 303; E. Apps, "Limited Partnerships and the 'Control' Prohibition: Assessing the Liability of Limited Partners" (1991) 70 Can. Bar Rev. 611; R. Flannigan, "Limited Partner Liability: A Response" (1992) 71 Can. Bar Rev. 552. The limited partners leave the running of the business to the general partner and in that respect the care, custody and the maintenance of the property, assets and undertaking of the limited partnership in which the limited partners and the general partner hold an interest. The ownership of this limited partnership property, assets and undertaking is an undivided interest which cannot be segregated for the purpose of legal process. It seems to me that there must be afforded a protection of the whole since the applicants' individual interest therein cannot be segregated without in effect dissolving the partnership arrangement. The limited partners have two courses of action to take if they are dissatisfied with the general partner or the operation of the limited partnership as carried on by the general partner – the limited partners can vote to (a) remove the general partner and replace it with another or (b) dissolve the limited partnership. However Flannigan strongly argues that an unfettered right to remove the general partner would attach general liability for the limited partners (and especially as to the question of continued enjoyment of favourable tax deductions) so that it is prudent to provide this as a conditional right: *Control Test*, (1992), supra, at pp. 524-525. Since the applicants are being afforded the protection of a stay of proceedings in respect to allowing them time to advance a reorganization plan and complete it if the plan finds favour, there should be a stay of proceedings (vis-à-vis any action which the limited partners may wish to take as to replacement or dissolution) through the period of allowing the limited partners to vote on the reorganization plan itself.

21 It seems to me that using the inherent jurisdiction of this court to supplement the statutory stay provisions of s. 11 of the CCAA would be appropriate in the circumstances; it would be just and reasonable to do so. The business operations of the applicants are so intertwined with the limited partnerships that it would be impossible for relief as to a stay to be granted to the applicants which would affect their business without at the same time extending that stay to the

undivided interests of the limited partners in such. It also appears that the applicants are well on their way to presenting a reorganization plan for consideration and a vote; this is scheduled to happen within the month so there would not appear to be any significant time inconvenience to any person interested in pursuing proceedings. While it is true that the provisions of the CCAA allow for a cramdown of a creditor's claim (as well as an interest of any other person), those who wish to be able to initiate or continue proceedings against the applicants may utilize the comeback clause in the order to persuade the court that it would not be just and reasonable to maintain that particular stay. It seems to me that in such a comeback motion the onus would be upon the applicants to show that in the circumstances it was appropriate to continue the stay.

22 The order is therefore granted as to the relief requested including the proposed stay provisions.

Application allowed.

TAB 9

Therefore, in my opinion the obligation did not arise until after bankruptcy and the Commission's penalty is not a provable claim in this bankruptcy.

47 Given my conclusion that the penalty imposed by the Securities Commission after the date of bankruptcy is not a claim provable in this bankruptcy, I do not have to go on to decide the next issue, that is, if it was a provable claim, whether it would survive any discharge from bankruptcy.

48 The application of the Securities Commission for a declaration that the Penalty is not a claim provable in Mr. Thow's bankruptcy is allowed.

Application granted.

[Indexed as: **Nortel Networks Corp., Re [ERISA Lift Stay Motion]**]

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

AND IN THE MATTER OF A PLAN OF COMPROMISE OR ARRANGEMENT OF NORTEL NETWORKS CORPORATION, NORTEL NETWORKS LIMITED, NORTEL NETWORKS GLOBAL CORPORATION, NORTEL NETWORKS INTERNATIONAL CORPORATION AND NORTEL NETWORKS TECHNOLOGY CORPORATION (Applicants)

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

Ontario Superior Court of Justice [Commercial List]

Morawetz J.

Heard: June 16, 2009

Judgment: August 18, 2009

Docket: 09-CL-7950

Alan Merskey for Nortel Networks Corp. et al

Lyndon Barnes, Adam Hirsch for Board of Directors of Nortel Networks Corporation, Nortel Networks Limited

Leanne Williams for Flextronics Inc.

J. Pasquariello for Monitor, Ernst & Young Inc.

B. Wadsworth for CAW-Canada

Thomas McRae for Recently Severed Calgary Employees

A. McKinnon for Former Employees

Mary Arzoymanidis for Bell Canada

Alex MacFarlane for Unsecured Creditors' Committee

Gavin Finlayson for Noteholders
Tina Lie for Superintendent of Financial Services of Ontario
Steven Graff, Ian Aversa for Current and Former Employees

Civil practice and procedure — Disposition without trial — Stay or dismissal of action — Removal of stay — Action was commenced in United States which involved alleged breach by named defendants of their statutory duties under Employee Retirement Income Security Act, 1974 (ERISA) — ERISA litigation was at discovery stage, which entailed review and production of millions of pages of electronic documents and numerous depositions — Stay was contained in Amended and Restated Initial Order (initial order) — Applicants brought motion for order extending stay — Current and former employees of N Inc. who were participants in long-term investment plan sponsored by N Inc. (moving parties) brought motion for order lifting stay of proceedings — Motion by applicants granted — Motion by moving parties dismissed — D&O stay under initial order did cover D&O defendants in ERISA litigation and it was not appropriate to lift stay at this time — Effect of stay would be merely to postpone ERISA litigation — Allegations against named defendants were not restricted to defendants acting in their capacity as fiduciaries — In expanding scope of litigation to include broad allegations as against directors, moving parties had brought ERISA litigation within terms of D&O stay — Restructuring was at critical stage and energies and activities of board should be directed towards restructuring — To permit ERISA litigation to continue at that time would result in significant distraction and diversion of resources at time when that could be least afforded — Further postponement of claim for relatively short period of time would not be unduly prejudicial to moving parties.

Cases considered by *Morawetz J.*:

Campeau v. Olympia & York Developments Ltd. (1992), 14 C.B.R. (3d) 303, 14 C.P.C. (3d) 339, 1992 CarswellOnt 185, [1992] O.J. No. 1946 (Ont. Gen. Div.) — referred to

Morneau Sobeco Ltd. Partnership v. Aon Consulting Inc. (2008), 2008 CarswellOnt 1427, (sub nom. *Morneau Sobeco Ltd. Partnership v. AON Consulting Inc.)* 237 O.A.C. 267, 65 C.C.L.I. (4th) 159, 2008 ONCA 196, 40 C.B.R. (5th) 172, 65 C.C.P.B. 293, (sub nom. *Slater Steel Inc. (Re))* 2008 C.E.B. & P.G.R. 8285, 291 D.L.R. (4th) 314 (Ont. C.A.) — distinguished

SNV Group Ltd., Re (2001), 95 B.C.L.R. (3d) 116, 2001 BCSC 1644, 2001 CarswellBC 2662, [2001] B.C.J. No. 2497 (B.C. S.C.) — referred to

Woodward's Ltd., Re (1993), 17 C.B.R. (3d) 236, 79 B.C.L.R. (2d) 257, 1993 CarswellBC 530, [1993] B.C.J. No. 42 (B.C. S.C.) — referred to

Statutes considered:

Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36
Generally — referred to
s. 11.5 [en. 1997, c. 12, s. 124] — considered
s. 11.5(1) [en. 1997, c. 12, s. 124] — considered
s. 11.5(2) [en. 1997, c. 12, s. 124] — referred to

Employee Retirement Income Security Act, 1974, 29 U.S.C.
Generally — referred to

Rules considered:

Rules of Civil Procedure, R.R.O. 1990, Reg. 194
R. 21 — referred to

MOTION by applicants for order extending stay in action; MOTION by moving parties for order lifting stay of proceedings.

***Morawetz J.*:**

1 This endorsement relates to two motions.

2 The first is brought by the Applicants for an order extending the stay contained at paragraphs 14 – 15 and 19 of the Amended and Restated Initial Order (the "Initial Order") to the individual defendants (the "Named Defendants") in the action commenced in the United States District Court, Middle District of Tennessee, Nashville District (the "ERISA Litigation").

3 The second is brought by the current and former employees of Nortel Networks Inc. ("NNI") who are or were participants in the long-term investment plan sponsored by NNI (the "Moving Parties") for an order, if necessary, lifting the stay of proceedings provided for in the Initial Order for the purpose of allowing the Moving Parties to continue with the ERISA Litigation.

4 For the following reasons, the motion of the Applicants is granted and the motion of the Moving Parties is dismissed.

Background

5 The motion of the Applicants is supported by the Board of Directors of Nortel Networks Corp. ("NNC") and Nortel Networks Ltd. ("NNL"), the Monitor, the Unsecured Creditors' Committee and the Bondholders.

6 The ERISA Litigation involves the alleged breach by the Named Defendants of their statutory duties under the *Employee Retirement Income Security Act, 1974* ("ERISA") regarding the management of NNI's defined contribution retirement plan (the "Plan"). It is alleged that, among others, the Named Defendants breached their duty by imprudently offering NNC stock for investment in the Plan.

7 The ERISA Litigation is currently at the discovery stage, which entails a review and production of millions of pages of electronic documents and numerous depositions. The ERISA Litigation plaintiffs are entitled to conduct up to 60 depositions.

8 Counsel to the Moving Parties explained that the defendants in ERISA cases are typically the individuals who managed the plan, being the "fiduciaries" in the language of ERISA. The fiduciaries may include the corporate entity itself, senior management employees, human resources employees and/or other personnel, entities or persons outside the company, or any combination of same.

Counsel submits that under ERISA, the status of an individual as a fiduciary depends on the plan documents and the actual management and practice relating to the plan, not an individual's official corporate status as an officer and/or director of the plan's sponsor.

9 Although the intent of the ERISA action may be aimed at the individuals in their capacity as independent ERISA fiduciaries, it seems to me that the Second Amended Complaint ("SAC") as filed in the action has a much broader impact.

10 At paragraph 15 of his factum, Mr. Barnes makes the following submission:

> It is simply untenable to suggest that the D&O Defendants [referred to herein as the "Named Defendants"] are only being sued in their capacity as independent ERISA fiduciaries. This claim is belied by the Plaintiff's own pleadings. The Second Amended Consolidated Class Action Complaint ("SAC") repeatedly asserts claims against the Named Defendants that specifically relate to the obligations of the company, where the defendants are alleged to be liable in their capacities as directors or officers. For example, the Plaintiffs allege that Nortel "necessarily acts through its Board of Directors, officers and employees", and assert that the "directors-fiduciaries act on behalf of [Nortel]". The SAC further claims that the Named Defendants are liable as "co-fiduciaries" alongside the company. It is inescapable that some of the claims for which the plaintiffs seek to recover against the individual Named Defendants relate to obligations of Nortel, because, as is evident from multiple allegations in the SAC, Nortel can only act derivatively through its directors and officers.

11 Mr. Barnes cites references to the SAC at page 5, paragraph 14; page 6, paragraph 19; pages 24, 52, 54 and paragraphs 50 – 109, 114; and pages 26 and 35 and paragraphs 58 and 66.

12 Mr. Barnes goes on to submit that as a result, the allegations in the ERISA Litigation against the Named Defendants and the allegations against the corporate defendants are invariably intertwined, raising several identical questions of fact and law.

13 Mr. Barnes also made reference to paragraph 147 of the SAC which sets out the additional theory of liability against some of the Defendants and alleges in the alternative that the said defendants are liable as non-fiduciaries who knowingly participated in the fiduciary breaches of the other Plan fiduciaries described herein, for which said Defendants are liable pursuant to ERISA.

14 Although the ERISA Litigation may be aimed at the Named Defendants in their capacities as "fiduciaries" it seems to me that this distinction is somewhat blurred such that it is arguable that the Named Defendants only have fiduciary status under ERISA as a consequence of their position as directors or officers of the company.

15 The Moving Parties concede that the ERISA Litigation against NNI, NNC and NNL is stayed as a result of the Chapter 11 proceeding, the Initial Order,

and the Chapter 15 proceedings. The Moving Parties seek to continue the action as against the Named Defendants and carry on with the discovery process.

16 The Moving Parties stated intention in continuing with the ERISA Litigation is to pursue insurance proceeds. The Moving Parties have filed evidence of an offer to settle made within the limits of the applicable policies but the offer has not been accepted.

17 The Moving Parties take the position that the ERISA Litigation is not stayed as against the Named Defendants pursuant to the stay because the Named Defendants are "not being sued in their capacity as officers and directors of the two Canadian corporations, but in their capacities as fiduciaries of an American 401(k) Plan". The Applicants take the position that it is, however, as a result of their employment by the Applicants that the Named Defendants had any capacity as fiduciaries for an American 401(k) Plan.

18 The Moving Parties take the position that a continuation of the ERISA Litigation will have a minimal effect on the Applicants because, among other things:

(a) the documentary discovery can be managed by the lawyers without the extensive involvement of any Nortel personnel;

(b) the bulk of documentary discovery issues have been worked out;

(c) they will accommodate individual defendants involved in the restructuring efforts by scheduling the remaining steps in the ERISA Litigation so that they are not distracted from the restructuring efforts; and

(d) they will agree that any determination or adjudication shall be without prejudice to the Canadian applicants in the claims process.

19 The Applicants take the position that they do not wish to be drawn into the conflict over the insurance proceeds as this would result in prejudice to their restructuring efforts. At this time, the Applicants are at a critical stage of their restructuring and submit that their efforts should be directed towards the restructuring.

20 Mr. Barnes submits that, if the ERISA Litigation is allowed to continue, it will detract significant attention and resources from Nortel's restructuring. The Moving Parties are seeking continued discovery of millions of pages of electronic documents in the company's possession and are expected to conduct dozens depositions. Mr. Barnes further submits it is simply not the case that continued litigation has a minimal effect on the company as negotiating a discovery agreement and collecting and providing the documents in question requires considerable time and resources in preparing past and current directors and officers for the depositions which will necessitate significant attention and focus for management and the board. In addition, he submits that addressing the strategic issues raised by the litigation, including the prospect of settlement, requires the attention of management and the board. Further, as the questions of fact and law

at issue in the ERISA Litigation are practically identical as between the corporate defendants and the D&O Defendants, he submits there is a serious risk of the record being tainted if the action proceeds without the Applicants' participation, which could have corresponding effects on any claims process.

21 It is also necessary to take into account the effect of a stay of the ERISA Litigation on the Moving Parties.

22 As counsel to the Applicants points out, the Moving Parties have also stated that their primary interest in continuing the ERISA Litigation is to pursue an insurance policy issued by Chubb. The Moving Parties have noted that the insurance proceeds are a "wasting policy", starting at U.S. $30 million and declining for defence costs.

23 Counsel to the Applicants submits that in the event that the stay continues, few defence costs will be incurred against the insurance proceeds and the Moving Parties will maintain the value of their within limits offer.

24 Further, as Mr. Barnes points out, staying the entire ERISA Litigation would not significantly harm the Moving Parties as it does not preclude their action, but merely postpones it.

Analysis

25 Section 11.5 of the CCAA authorizes the court to make an order under the CCAA to provide for a stay of proceedings against directors. Section 11.5(1) states:

> 11.5(1) An order made under section 11 may provide that no person may commence or continue any action against a director of the debtor company on any claim against directors that arose before the commencement of proceedings under this Act and that relates to obligations of the company where directors are under any law liable within their capacity as directors for the payment of such obligations, unless a compromise or arrangement in respect of the company, if one is filed, is sanctioned by the court or is refused by the creditors or the court.

26 Section 19 of the Initial Order provides as follows:

> THIS COURT ORDERS that during the Stay Period, and except as permitted by subsection 11.5(2) of the CCAA, no Proceeding may be commenced or continued against any of the former, current or future directors or officers of the Applicants with respect to any claim against the directors or officers that arose before the date hereof and that relates to any obligations of the Applicants whereby the directors or officers are alleged under any law to be liable in their capacity as directors or officers for the payment or performance of such obligations, unless a compromise or arrangement in respect of the Applicants, if one is filed, is sanctioned by this Court or is refused by the creditors of the applicant or this Court (the "D&O" stay).

27 It is also argued by both counsel to the Applicants and the Board that this statutory power is augmented by the court's inherent jurisdiction to grant a stay

in appropriate circumstances. (See: *SNV Group Ltd., Re*, [2001] B.C.J. No. 2497 (B.C. S.C.).) Counsel to the Applicants and the Board also submit that the CCAA is remedial legislation to be construed liberally and in these circumstances, it should be recognized that the purpose of the stay is to provide a debtor with its opportunity to negotiate with its creditors without having to devote time and scarce resources to defending legal actions against it. It is further submitted that given that a company can only act through its management and board, by extension, the purpose of the stay provision is to provide management and the board with the opportunity to negotiate with creditors and other stakeholders without having to devote precious time, resources and energy to defending against legal actions.

28 Mr. Barnes submits that the ERISA Litigation falls squarely within the terms of the D&O Stay as it is a claim against former and current directors and officers under a U.S. statute that arose prior to the date of filing. Further, the Named Defendants are only exposed to this liability as a consequence of their position with the company.

29 It is on this last point that Mr. Graff, on behalf of the Moving Parties, takes issue. He submits that the litigation is not stayed against the individual defendants because they are not being sued in their capacities as officers and directors of two Canadian corporations, but in their capacities as fiduciaries of an American 401(k) Plan. As such, he submits that the stay ought not to extend to the ERISA Litigation. He submits that the named defendants' liability is not a derivative of the Applicants' liability, if any, as a fiduciary. He further submits that the corporate defendants have claimed in the ERISA Litigation that the corporate entities are not fiduciaries at all and need not even have been named in the ERISA Litigation.

30 Mr. Graff further submits that the Applicants' submission and the Board's submission is flawed and that following the reasoning of the Court of Appeal in *Morneau Sobeco Ltd. Partnership v. Aon Consulting Inc.* (2008), 40 C.B.R. (5th) 172 (Ont. C.A.), the fact that the management of the Plan has always been performed by the Applicants' employees, officers and directors is moot. Mr. Graff submits that the *Morneau* case is on "all fours" with this case.

31 With respect, I do not find that the *Morneau* case is on "all fours" with this case. Mr. Graff submits that in *Morneau*, the Court of Appeal opined on the applicable legal questions: When are directors and officers not directors and officers?

32 In my view, while the Court of Appeal may have commented on the issue referenced by Mr. Graff, it was not in a context which is similar to that being faced on this motion. In *Morneau*, the Court of Appeal was faced with an interpretation issue arising out of the scope and terms of a release. The consequences of an interpretation against Morneau would have resulted in a bar of the claim. This distinction between *Morneau* and the case at bar is, in my view, significant.

33 The *Morneau* case can also be distinguished on the basis that Gillese J.A. was examining a release and, in particular, how far that release went. That is not an issue that is before me. There is no determination that is being made on this motion that will affect the ultimate outcome of the ERISA Litigation. There is no issue that a denial of the stay will result in the action being barred. Rather, the effect of the stay would be merely to postpone the ERISA Litigation.

34 This is not a Rule 21 motion and accordingly, the pleadings do not have to be reviewed on the basis as to whether it is "plain, obvious and beyond doubt" that the claim could not succeed. In this case, there is no "bright line" in the pleadings. As I have noted above, the allegations against the Named Defendants are not restricted to the defendants acting in their capacity as fiduciaries. In expanding the scope of the litigation to include broad allegations as against the directors, the Moving Parties have brought the ERISA Litigation, in my view, within the terms of the D&O Stay.

35 Having determined that the ERISA Litigation falls within the terms of the D&O Stay, the second issue to consider is whether the stay should be lifted so as to permit the ERISA Litigation to continue at this time.

36 In my view, the Nortel restructuring is at a critical stage and the energies and activities of the Board should be directed towards the restructuring. I accept the argument of Mr. Barnes on this point. To permit the ERISA Litigation to continue at that time would, in my view, result in a significant distraction and diversion of resources at a time when that can be least afforded. It is necessary in considering whether to lift the stay, to weigh the interests of the Applicants against the interests of those who will be affected by the stay. Where the benefits to be achieved by the applicant outweighs the prejudice to affected parties, a stay will be granted. (See: *Woodward's Ltd., Re* (1993), 17 C.B.R. (3d) 236 (B.C. S.C.).)

37 I also note the comments of Blair J. (as he then was) in *Campeau v. Olympia & York Developments Ltd.* (1992), 14 C.B.R. (3d) 303 (Ont. Gen. Div.) at paragraph 24 where he stated:

> In making these orders, I see no prejudice to the Campeau plaintiffs. The processing of their action is not being precluded, but merely postponed. Their claims may, indeed, be addressed more expeditiously than might have otherwise been the case, as they may be dealt with - at least for the purposes of that proceeding in the CCAA proceeding itself.

38 The prejudice to be suffered by the Moving Parties in the ERISA Litigation is a postponement of the claim. In view of the fact that the ERISA Litigation was commenced in 2001, I have not been persuaded that a further postponement for a relatively short period of time will be unduly prejudicial to the Moving Parties.

Disposition

39 Under the circumstances, I have concluded that the D&O Stay under the Initial Order does cover the D&O Defendants in the ERISA Litigation and that it is not appropriate to lift the stay at this time.

40 It is recognized that the ERISA Litigation will proceed at some point. The plaintiffs in the ERISA Litigation are at liberty to have this matter reviewed in 120 days.

41 To the extend that I have erred in determining that the ERISA Litigation is not the type of action directly contemplated by the D&O Stay, I would exercise this Court's inherent power to stay the proceedings against non-parties to achieve the same result.

Motion by applicants granted; motion by moving parties dismissed.