Court File No.: CV-17-11846-00CL

ONTARIO
SUPERIOR COURT OF JUSTICE
(COMMERCIAL LIST)

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 SEARS CANADA INC., CORBEIL ÉLECTRIQUE INC., S.L.H. TRANSPORT INC., THE CUT INC., SEARS CONTACT SERVICES INC., INITIUM LOGISTICS SERVICES INC., INITIUM COMMERCE LABS INC., INITIUM TRADING AND SOURCING CORP., SEARS FLOOR COVERING CENTRES INC., 173470 CANADA INC., 2497089 ONTARIO INC., 6988741 CANADA INC., 10011711 CANADA INC., 1592580 ONTARIO LIMITED, 955041 ALBERTA LTD., 4201531 CANADA INC., 168886 CANADA INC., AND 3339611 CANADA INC.

(each, an "**Applicant**", and collectively, the "**Applicants**")

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(Motions Returnable August 18, 2017)

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TO: **SERVICE LIST**

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TAB 1

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** Preliminary Version **

Case Name:

Century Services Inc. v. Canada (Attorney General)

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

[2010] S.C.J. No. 60

[2010] A.C.S. no 60

2010 SCC 60

[2010] 3 S.C.R. 379

[2010] 3 R.C.S. 379

2011 D.T.C. 5006

409 N.R. 201

296 B.C.A.C. 1

12 B.C.L.R. (5th) 1

2010 CarswellBC 3419

326 D.L.R. (4th) 577

EYB 2010-183759

2011EXP-9

J.E. 2011-5

2011 G.T.C. 2006

[2011] 2 W.W.R. 383

72 C.B.R. (5th) 170

[2010] G.S.T.C. 186

196 A.C.W.S. (3d) 27

File No.: 33239.

Supreme Court of Canada

Heard: May 11, 2010;
Judgment: December 16, 2010.

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

(136 paras.)

Appeal From:

ON APPEAL FROM THE COURT OF APPEAL FOR BRITISH COLUMBIA

Bankruptcy and insolvency law -- Companies' Creditors Arrangement Act (CCAA) matters -- Application of Act -- Compromises and arrangements -- Where Crown affected -- Effect of related legislation -- Bankruptcy and Insolvency Act -- Appeal by Century Services Inc. from judgment of British Columbia Court of Appeal reversing a judgment dismissing a Crown application for payment of unremitted GST monies allowed -- Section 222(3) of the Excise Tax Act evinced no explicit intention of Parliament to repeal s. 18.3 of CCAA -- Parliament's intent with respect to GST deemed trusts was to be found in the CCAA -- Judge had the discretion under the CCAA to continue the stay of the Crown's claim for enforcement of the GST deemed trust while otherwise lifting it to permit debtor company to make an assignment in bankruptcy.

Appeal by Century Services Inc. from a judgment of the British Columbia Court of Appeal reversing a judgment dismissing a Crown application for payment of unremitted GST monies. The debtor company commenced proceedings under the Companies' Creditors Arrangement Act (CCAA), obtaining a stay of proceedings with a view to reorganizing its financial affairs. Among the debts owed by the debtor company at the commencement of the reorganization was an amount of GST collected but unremitted to the Crown. The Excise Tax Act (ETA) created a deemed trust in favour of the Crown for amounts collected in respect of GST. The ETA provided that the deemed trust operated despite any other enactment of Canada except the Bankruptcy and Insolvency Act (BIA). However, the CCAA also provided that subject to certain exceptions, none of which mentioned GST, deemed trusts in favour of the Crown did not operate under the CCAA. In the context of the

CCAA proceedings, a chambers judge approved a payment not exceeding $5 million to the debtor company's major secured creditor, Century Services. The judge agreed to the debtor company's proposal to hold back an amount equal to the GST monies collected but unremitted to the Crown and place it in the Monitor's trust account until the outcome of the reorganization was known. After concluding that reorganization was not possible, the debtor company sought leave to partially lift the stay of proceedings so it could make an assignment in bankruptcy under the Bankruptcy and Insolvency Act (BIA). The Crown sought an order that the GST monies held by the Monitor be paid to the Receiver General of Canada. The judge denied the Crown's motion, and allowed the assignment in bankruptcy. The Court of Appeal found two independent bases for allowing the Crown's appeal. First, the court's authority under s. 11 of the CCAA was held not to extend to staying the Crown's application for immediate payment of the GST funds subject to the deemed trust after it was clear that reorganization efforts had failed and that bankruptcy was inevitable. As restructuring was no longer a possibility, staying the Crown's claim to the GST funds no longer served a purpose under the CCAA and the court was bound under the priority scheme provided by the ETA to allow payment to the Crown. Second, the Court of Appeal concluded that by ordering the GST funds segregated in the Monitor's trust account, the judge had created an express trust in favour of the Crown from which the monies in question could not be diverted for any other purposes.

HELD: Appeal allowed. Section 222(3) of the ETA evinced no explicit intention of Parliament to repeal CCAA s. 18.3. Had Parliament sought to give the Crown a priority for GST claims, it could have done so explicitly, as it did for source deductions. There was no express statutory basis for concluding that GST claims enjoyed a preferred treatment under the CCAA or the BIA. Parliament's intent with respect to GST deemed trusts was to be found in the CCAA. With respect to the scope of a court's discretion when supervising reorganization, the broad discretionary jurisdiction conferred on the supervising judge had to be interpreted having regard to the remedial nature of the CCAA and insolvency legislation generally. The question was whether the order advanced the underlying purpose of the CCAA. The judge's order staying Crown enforcement of the GST claim ensured that creditors would not be disadvantaged by the attempted reorganization under the CCAA. The effect of his order was to blunt any impulse of creditors to interfere in an orderly liquidation. His order was thus in furtherance of the CCAA's objectives to the extent that it allowed a bridge between the CCAA and BIA proceedings. The order fostered a harmonious transition between reorganization and liquidation while meeting the objective of a single collective proceeding that was common to both statutes. The breadth of the court's discretion under the CCAA was sufficient to lift the stay to allow entry into liquidation. No express trust was created by the judge's order because there was no certainty of object inferrable from his order. Further, no deemed trust was created.

Statutes, Regulations and Rules Cited:

An Act to establish the Wage Earner Protection Program Act, to amend the Bankruptcy and Insolvency Act and the Companies' Creditors Arrangement Act and to make consequential amendments to other Acts, S.C. 2005, c. 47, s. 69, s. 128, s. 131

Bank Act, S.C. 1991, c. 46,

Bankruptcy and Insolvency Act, R.S.C. 1985, c. B-, s. 67, s. 86

Canada Pension Plan, R.S.C. 1985, c. C-8, s. 23

Cities and Towns Act, R.S.Q., c. C-19,

Civil Code of QuÚbec, S.Q. 1991, c. 64, art. 2930

Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36, s. 11, s. 11.4, s. 18.3, s. 18.4, s. 20, s. 21

Companies' Creditors Arrangement Act, 1933, S.C. 1932-33, c. 36,

Employment Insurance Act, S.C. 1996, c. 23, s. 86(2), s. 86(2.1)

Excise Tax Act, R.S.C. 1985, c. E-15, s. 222

Income Tax Act, R.S.C. 1985, c. 1 (5th Supp.), s. 227(4), s. 227(4.1)

Interpretation Act, R.S.C. 1985, c. I-21, s. 2, s. 44(f)

Personal Property Security Act, S.A. 1988, c. P-4.05,

Winding-up and Restructuring Act, R.S.C. 1985, c. W-11,

Subsequent History:

NOTE: This document is subject to editorial revision before its reproduction in final form in the Canada Supreme Court Reports.

Court Catchwords:

Bankruptcy and Insolvency -- Priorities -- Crown applying on eve of bankruptcy of debtor company to have GST monies held in trust paid to Receiver General of Canada -- Whether deemed trust in favour of Crown under Excise Tax Act prevails over provisions of Companies' Creditors Arrangement Act purporting to nullify deemed trusts in favour of Crown -- Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36, s. 18.3(1) -- Excise Tax Act, R.S.C. 1985, c. E-15, s. 222(3).

Bankruptcy and insolvency -- Procedure -- Whether chambers judge had authority to make order partially lifting stay of proceedings to allow debtor company to make assignment in bankruptcy and to stay Crown's right to enforce GST deemed trust -- Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36, s. 11.

Trusts -- Express trusts -- GST collected but unremitted to Crown -- Judge ordering that GST be held by Monitor in trust account -- Whether segregation of Crown's GST claim in Monitor's account created an express trust in favour of Crown.

Court Summary:

The debtor company commenced proceedings under the *Companies' Creditors Arrangement Act* ("*CCAA*"), obtaining a stay of proceedings to allow it time to reorganize its financial affairs. One of the debtor company's outstanding debts at the commencement of the reorganization was an amount of unremitted Goods and Services Tax ("GST") payable to the Crown. Section 222(3) of the *Excise Tax Act* ("*ETA*") created a deemed trust over unremitted GST, which operated despite any other enactment of Canada except the *Bankruptcy and Insolvency Act* ("*BIA*"). However, s. 18.3(1) of the *CCAA* provided that any statutory deemed trusts in favour of the Crown did not operate under the *CCAA*, subjcct to certain exceptions, none of which mentioned GST.

Pursuant to an order of the *CCAA* chambers judge, a payment not exceeding $5 million was approved to the debtor company's major secured creditor, Century Services. However, the chambers judge also ordered the debtor company to hold back and segregate in the Monitor's trust account an

amount equal to the unremitted GST pending the outcome of the reorganization. On concluding that reorganization was not possible, the debtor company sought leave of the court to partially lift the stay of proceedings so it could make an assignment in bankruptcy under the *BIA*. The Crown moved for immediate payment of unremitted GST to the Receiver General. The chambers judge denied the Crown's motion, and allowed the assignment in bankruptcy. The Court of Appeal allowed the appeal on two grounds. First, it reasoned that once reorganization efforts had failed, the chambers judge was bound under the priority scheme provided by the *ETA* to allow payment of unremitted GST to the Crown and had no discretion under s. 11 of the *CCAA* to continue the stay against the Crown's claim. Second, the Court of Appeal concluded that by ordering the GST funds segregated in the Monitor's trust account, the chambers judge had created an express trust in favour of the Crown.

Held (Abella J. dissenting): The appeal should be allowed.

Per McLachlin C.J., Binnie, LeBel, **Deschamps**, Charron, Rothstein and Cromwell JJ.: The apparent conflict between s. 222(3) of the *ETA* and s. 18.3(1) of the *CCAA* can be resolved through an interpretation that properly recognizes the history of the *CCAA*, its function amidst the body of insolvency legislation enacted by Parliament and the principles for interpreting the *CCAA* that have been recognized in the jurisprudence. The history of the *CCAA* distinguishes it from the *BIA* because although these statutes share the same remedial purpose of avoiding the social and economic costs of liquidating a debtor's assets, the *CCAA* offers more flexibility and greater judicial discretion than the rules-based mechanism under the *BIA*, making the former more responsive to complex reorganizations. Because the *CCAA* is silent on what happens if reorganization fails, the *BIA* scheme of liquidation and distribution necessarily provides the backdrop against which creditors assess their priority in the event of bankruptcy. The contemporary thrust of legislative reform has been towards harmonizing aspects of insolvency law common to the *CCAA* and the *BIA*, and one of its important features has been a cutback in Crown priorities. Accordingly, the *CCAA* and the *BIA* both contain provisions nullifying statutory deemed trusts in favour of the Crown, and both contain explicit exceptions exempting source deductions deemed trusts from this general rule. Meanwhile, both Acts are harmonious in treating other Crown claims as unsecured. No such clear and express language exists in those Acts carving out an exception for GST claims.

When faced with the apparent conflict between s. 222(3) of the *ETA* and s. 18.3(1) of the *CCAA*, courts have been inclined to follow *Ottawa Senators Hockey Club Corp.(Re)* and resolve the conflict in favour of the *ETA*. *Ottawa Senators* should not be followed. Rather, the *CCAA* provides the rule. Section 222(3) of the *ETA* evinces no explicit intention of Parliament to repeal *CCAA* s. 18.3. Where Parliament has sought to protect certain Crown claims through statutory deemed trusts and intended that these deemed trusts continue in insolvency, it has legislated so expressly and elaborately. Meanwhile, there is no express statutory basis for concluding that GST claims enjoy a preferred treatment under the *CCAA* or the *BIA*. The internal logic of the *CCAA* appears to subject a GST deemed trust to the waiver by Parliament of its priority. A strange asymmetry would result if differing treatments of GST deemed trusts under the *CCAA* and the *BIA* were found to exist, as this would encourage statute shopping, undermine the *CCAA*'s remedial purpose and invite the very social ills that the statute was enacted to avert. The later in time enactment of the more general s. 222(3) of the *ETA* does not require application of the doctrine of implied repeal to the earlier and more specific s. 18.3(1) of the *CCAA* in the circumstances of this case. In any event, recent amendments to the *CCAA* in 2005 resulted in s. 18.3 of the Act being renumbered and reformulated, making it the later in time provision. This confirms that Parliament's intent with respect to GST deemed

trusts is to be found in the *CCAA*. The conflict between the *ETA* and the *CCAA* is more apparent than real.

The exercise of judicial discretion has allowed the *CCAA* to adapt and evolve to meet contemporary business and social needs. As reorganizations become increasingly complex, *CCAA* courts have been called upon to innovate. In determining their jurisdiction to sanction measures in a *CCAA* proceeding, courts should first interpret the provisions of the *CCAA* before turning to their inherent or equitable jurisdiction. Noteworthy in this regard is the expansive interpretation the language of the *CCAA* is capable of supporting. The general language of the *CCAA* should not be read as being restricted by the availability of more specific orders. The requirements of appropriateness, good faith and due diligence are baseline considerations that a court should always bear in mind when exercising *CCAA* authority. The question is whether the order will usefully further efforts to avoid the social and economic losses resulting from liquidation of an insolvent company, which extends to both the purpose of the order and the means it employs. Here, the chambers judge's order staying the Crown's GST claim was in furtherance of the *CCAA*'s objectives because it blunted the impulse of creditors to interfere in an orderly liquidation and fostered a harmonious transition from the *CCAA* to the *BIA*, meeting the objective of a single proceeding that is common to both statutes. The transition from the *CCAA* to the *BIA* may require the partial lifting of a stay of proceedings under the *CCAA* to allow commencement of *BIA* proceedings, but no gap exists between the two statutes because they operate in tandem and creditors in both cases look to the *BIA* scheme of distribution to foreshadow how they will fare if the reorganization is unsuccessful. The breadth of the court's discretion under the *CCAA* is sufficient to construct a bridge to liquidation under the *BIA*. Hence, the chambers judge's order was authorized.

No express trust was created by the chambers judge's order in this case because there is no certainty of object inferrable from his order. Creation of an express trust requires certainty of intention, subject matter and object. At the time the chambers judge accepted the proposal to segregate the monies in the Monitor's trust account there was no certainty that the Crown would be the beneficiary, or object, of the trust because exactly who might take the money in the final result was in doubt. In any event, no dispute over the money would even arise under the interpretation of s. 18.3(1) of the *CCAA* established above, because the Crown's deemed trust priority over GST claims would be lost under the *CCAA* and the Crown would rank as an unsecured creditor for this amount.

Per Fish J.: The GST monies collected by the debtor are not subject to a deemed trust or priority in favour of the Crown. In recent years, Parliament has given detailed consideration to the Canadian insolvency scheme but has declined to amend the provisions at issue in this case, a deliberate exercise of legislative discretion. On the other hand, in upholding deemed trusts created by the *ETA* notwithstanding insolvency proceedings, courts have been unduly protective of Crown interests which Parliament itself has chosen to subordinate to competing prioritized claims. In the context of the Canadian insolvency regime, deemed trusts exist only where there is a statutory provision *creating* the trust and a *CCAA* or *BIA* provision explicitly *confirming* its effective operation. The *Income Tax Act*, the *Canada Pension Plan Act* and the *Employment Insurance Act* all contain deemed trust provisions that are strikingly similar to that in s. 222 of the *ETA* but they are all also confirmed in s. 37 of the *CCAA* and in s. 67(3) of the *BIA* in clear and unmistakeable terms. The same is not true of the deemed trust created under the *ETA*. Although Parliament created a deemed trust in favour of the Crown to hold unremitted GST monies, and although it purports to maintain this trust notwithstanding any contrary federal or provincial legislation, it did not *confirm* the continued op-

eration of the trust in either the *BIA* or the *CCAA*, reflecting Parliament's intention to allow the deemed trust to lapse with the commencement of insolvency proceedings.

Per Abella J (dissenting): Section 222(3) of the *ETA* gives priority during *CCAA* proceedings to the Crown's deemed trust in unremitted GST. This provision unequivocally defines its boundaries in the clearest possible terms and excludes only the *BIA* from its legislative grasp. The language used reflects a clear legislative intention that s. 222(3) would prevail if in conflict with any other law except the *BIA*. This is borne out by the fact that following the enactment of s. 222(3), amendments to the *CCAA* were introduced, and despite requests from various constituencies, s. 18.3(1) was not amended to make the priorities in the *CCAA* consistent with those in the *BIA*. This indicates a deliberate legislative choice to protect the deemed trust in s. 222(3) from the reach of s. 18.3(1) of the *CCAA*.

The application of other principles of interpretation reinforces this conclusion. An earlier, specific provision may be overruled by a subsequent general statute if the legislature indicates, through its language, an intention that the general provision prevails. Section 222(3) achieves this through the use of language stating that it prevails despite any law of Canada, of a province, or "any other law" *other than the BIA*. Section 18.3(1) of the *CCAA* is thereby rendered inoperative for purposes of s. 222(3). By operation of s. 44(f) of the *Interpretation Act*, the transformation of s. 18(3) into s. 37(1) after the enactment of s. 222(3) of the *ETA* has no effect on the interpretive queue, and s. 222(3) of the *ETA* remains the "later in time" provision. This means that the deemed trust provision in s. 222(3) of the *ETA* takes precedence over s. 18.3(1) during *CCAA* proceedings. While s. 11 gives a court discretion to make orders notwithstanding the *BIA* and the *Winding-up Act,* that discretion is not liberated from the operation of any other federal statute. Any exercise of discretion is therefore circumscribed by whatever limits are imposed by statutes *other* than the *BIA* and the *Winding-up Act*. That includes the *ETA*. The chambers judge in this case was, therefore, required to respect the priority regime set out in s. 222(3) of the *ETA*. Neither s. 18.3(1) nor s. 11 of the *CCAA* gave him the authority to ignore it. He could not, as a result, deny the Crown's request for payment of the GST funds during the *CCAA* proceedings.

Cases Cited

By Deschamps J.

Overruled: *Ottawa Senators Hockey Club Corp. (Re)* (2005), 73 O.R. (3d) 737; **distinguished:** *Doré v. Verdun (City)*, [1997] 2 S.C.R. 862; **referred to**: *Reference re Companies' Creditors Arrangement Act*, [1934] S.C.R. 659; *Quebec (Revenue) v. Caisse populaire Desjardins de Montmagny*, 2009 SCC 49, [2009] 3 S.C.R. 286; *Deputy Minister of Revenue v. Rainville*, [1980] 1 S.C.R. 35; *Gauntlet Energy Corp., Re*, 2003 ABQB 894, 30 Alta. L.R. (4) 192; *Komunik Corp. (Arrangement relatif à)*, 2009 QCCS 6332 (CanLII), leave to appeal granted, 2010 QCCA 183 (CanLII); *Royal Bank of Canada v. Sparrow Electric Corp.*, [1997] 1 S.C.R. 411; *First Vancouver Finance v. M.N.R.*, 2002 SCC 49, [2002] 2 S.C.R. 720; *Solid Resources Ltd., Re* (2002), 40 C.B.R. (4) 219; *Metcalfe & Mansfield Alternative Investments II Corp. (Re)*, 2008 ONCA 587, 92 O.R. (3d) 513; *Dylex Ltd., Re* (1995), 31 C.B.R. (3d) 106; *Elan Corp. v. Comiskey* (1990), 41 O.A.C. 282; *Chef Ready Foods Ltd. v. Hongkong Bank of Can.* (1990), 51 B.C.L.R. (2d) 84; *Pacific National Lease Holding Corp, Re* (1992), 19 B.C.AC. 134; *Canadian Airlines Corp., Re*, 2000 ABQB 442, 84 Alta. L.R. (3d) 9; *Air Canada, Re* (2003), 42 C.B.R. (4) 173; *Air Canada, Re*, 2003 CanLII 49366; *Canadian Red Cross Society/Société Canadienne de la Croix Rouge, Re* (2000), 19 C.B.R.

(4) 158; *Skydome Corp., Re* (1998), 16 C.B.R. (4) 118; *United Used Auto & Truck Parts Ltd., Re*, 2000 BCCA 146, 135 B.C.A.C. 96, aff'g (1999), 12 C.B.R. (4) 144; *Skeena Cellulose Inc., Re*, 2003 BCCA 344, 13 B.C.L.R. (4) 236; *Stelco Inc. (Re)* (2005), 75 O.R. (3d) 5; *Philip's Manufacturing Ltd., Re* (1992), 9 C.B.R. (3d) 25; *Ivaco Inc. (Re)* (2006), 83 O.R. (3d) 108.

By Fish J.

Referred to: *Ottawa Senators Hockey Club Corp. (Re)* (2005), 73 O.R. (3d) 737.

By Abella J. (dissenting)

Ottawa Senators Hockey Club Corp. (Re) (2005), 73 O.R. (3d) 737; *Tele-Mobile Co. v. Ontario*, 2008 SCC 12, [2008] 1 S.C.R. 305; *Doré v. Verdun (City)*, [1997] 2 S.C.R. 862; *Attorney General of Canada v. Public Service Staff Relations Board*, [1977] 2 F.C. 663.

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Civil Code of Québec, S.Q. 1991, c. 64.

Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36, ss. 11, 11.4, 18.3, 18.4, 20 [am. 2005, c. 47, ss. 128, 131], 21 [am. 1997, c. 12, s. 126].

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History and Disposition:

APPEAL from a judgment of the British Columbia Court of Appeal (Newbury, Tysoe and Smith JJ.A.), 2009 BCCA 205, 98 B.C.L.R. (4) 242, 270 B.C.A.C. 167, 454 W.A.C. 167, [2009] 12 W.W.R. 684, [2009] G.S.T.C. 79, [2009] B.C.J. No. 918 (QL), 2009 CarswellBC 1195, reversing a judgment of Brenner C.J.S.C., 2008 BCSC 1805, [2008] G.S.T.C. 221, [2008] B.C.J. No. 2611 (QL), 2008 CarswellBC 2895, dismissing a Crown application for payment of GST monies. Appeal allowed, Abella J. dissenting.

Counsel:

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

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

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

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

1. Facts and Decisions of the Courts Below

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

3 Amongst the debts owed by LeRoy Trucking was an amount for Goods and Services Tax ("GST") collected but unremitted to the Crown. The *ETA* creates a deemed trust in favour of the Crown for amounts collected in respect of GST. The deemed trust extends to any property or proceeds held by the person collecting GST and any property of that person held by a secured creditor, requiring that property to be paid to the Crown in priority to all security interests. The *ETA* provides

that the deemed trust operates despite any other enactment of Canada except the *BIA*. However, the *CCAA* also provides that subject to certain exceptions, none of which mentions GST, deemed trusts in favour of the Crown do not operate under the *CCAA*. Accordingly, under the *CCAA* the Crown ranks as an unsecured creditor in respect of GST. Nonetheless, at the time LeRoy Trucking commenced *CCAA* proceedings the leading line of jurisprudence held that the *ETA* took precedence over the *CCAA* such that the Crown enjoyed priority for GST claims under the *CCAA*, even though it would have lost that same priority under the *BIA*. The *CCAA* underwent substantial amendments in 2005 in which some of the provisions at issue in this appeal were renumbered and reformulated (S.C. 2005, c. 47). However, these amendments only came into force on September 18, 2009. I will refer to the amended provisions only where relevant.

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

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

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

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

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

2. Issues

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

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

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

(3) Did the court's order of April 29, 2008 requiring segregation of the Crown's GST claim in the Monitor's trust account create an express trust in favour of the Crown in respect of those funds?

3. Analysis

10 The first issue concerns Crown priorities in the context of insolvency. As will be seen, the *ETA* provides for a deemed trust in favour of the Crown in respect of GST owed by a debtor "[d]espite ... any other enactment of Canada (except the *Bankruptcy and Insolvency Act*)" (s. 222(3)), while the *CCAA* stated at the relevant time that "notwithstanding any provision in federal or provincial legislation that has the effect of deeming property to be held in trust for Her Majesty, property of a debtor company shall not be [so] regarded" (s. 18.3(1)). It is difficult to imagine two statutory provisions more apparently in conflict. However, as is often the case, the apparent conflict can be resolved through interpretation.

11 In order to properly interpret the provisions, it is necessary to examine the history of the *CCAA*, its function amidst the body of insolvency legislation enacted by Parliament, and the principles that have been recognized in the jurisprudence. It will be seen that Crown priorities in the insolvency context have been significantly pared down. The resolution of the second issue is also rooted in the context of the *CCAA*, but its purpose and the manner in which it has been interpreted in the case law are also key. After examining the first two issues in this case, I will address Tysoe J.A.'s conclusion that an express trust in favour of the Crown was created by the court's order of April 29, 2008.

3.1 *Purpose and Scope of Insolvency Law*

12 Insolvency is the factual situation that arises when a debtor is unable to pay creditors (see generally, R. J. Wood, *Bankruptcy and Insolvency Law* (2009), at p. 16). Certain legal proceedings become available upon insolvency, which typically allow a debtor to obtain a court order staying its creditors' enforcement actions and attempt to obtain a binding compromise with creditors to adjust the payment conditions to something more realistic. Alternatively, the debtor's assets may be liquidated and debts paid from the proceeds according to statutory priority rules. The former is usually referred to as reorganization or restructuring while the latter is termed liquidation.

13 Canadian commercial insolvency law is not codified in one exhaustive statute. Instead, Parliament has enacted multiple insolvency statutes, the main one being the *BIA*. The *BIA* offers a self-contained legal regime providing for both reorganization and liquidation. Although bankruptcy legislation has a long history, the *BIA* itself is a fairly recent statute -- it was enacted in 1992. It is characterized by a rules-based approach to proceedings. The *BIA* is available to insolvent debtors owing $1000 or more, regardless of whether they are natural or legal persons. It contains mechanisms for debtors to make proposals to their creditors for the adjustment of debts. If a proposal fails, the *BIA* contains a bridge to bankruptcy whereby the debtor's assets are liquidated and the proceeds paid to creditors in accordance with the statutory scheme of distribution.

14 Access to the *CCAA* is more restrictive. A debtor must be a company with liabilities in excess of $5 million. Unlike the *BIA*, the *CCAA* contains no provisions for liquidation of a debtor's assets if reorganization fails. There are three ways of exiting *CCAA* proceedings. The best outcome is achieved when the stay of proceedings provides the debtor with some breathing space during which solvency is restored and the *CCAA* process terminates without reorganization being needed. The second most desirable outcome occurs when the debtor's compromise or arrangement is accepted by its creditors and the reorganized company emerges from the *CCAA* proceedings as a going concern. Lastly, if the compromise or arrangement fails, either the company or its creditors usually seek to have the debtor's assets liquidated under the applicable provisions of the *BIA* or to place the debtor into receivership. As discussed in greater detail below, the key difference between the reorganization regimes under the *BIA* and the *CCAA* is that the latter offers a more flexible mechanism with greater judicial discretion, making it more responsive to complex reorganizations.

15 As I will discuss at greater length below, the purpose of the *CCAA* -- Canada's first reorganization statute -- is to permit the debtor to continue to carry on business and, where possible, avoid the social and economic costs of liquidating its assets. Proposals to creditors under the *BIA* serve the same remedial purpose, though this is achieved through a rules-based mechanism that offers less flexibility. Where reorganization is impossible, the *BIA* may be employed to provide an orderly mechanism for the distribution of a debtor's assets to satisfy creditor claims according to predetermined priority rules.

16 Prior to the enactment of the *CCAA* in 1933 (S.C. 1932-33, c. 36), practice under existing commercial insolvency legislation tended heavily towards the liquidation of a debtor company (J. Sarra, *Creditor Rights and the Public Interest: Restructuring Insolvent Corporations* (2003), at p. 12). The battering visited upon Canadian businesses by the Great Depression and the absence of an effective mechanism for reaching a compromise between debtors and creditors to avoid liquidation required a legislative response. The *CCAA* was innovative as it allowed the insolvent debtor to attempt reorganization under judicial supervision outside the existing insolvency legislation which, once engaged, almost invariably resulted in liquidation (*Reference re Companies' Creditors Arrangement Act*, [1934] S.C.R. 659, at pp. 660-61; Sarra, *Creditor Rights*, at pp. 12-13).

17 Parliament understood when adopting the *CCAA* that liquidation of an insolvent company was harmful for most of those it affected -- notably creditors and employees -- and that a workout which allowed the company to survive was optimal (Sarra, *Creditor Rights*, at pp. 13-15).

18 Early commentary and jurisprudence also endorsed the *CCAA*'s remedial objectives. It recognized that companies retain more value as going concerns while underscoring that intangible losses, such as the evaporation of the companies' goodwill, result from liquidation (S. E. Edwards, "Reorganizations Under the Companies' Creditors Arrangement Act" (1947), 25 *Can. Bar Rev.* 587, at p. 592). Reorganization serves the public interest by facilitating the survival of companies supplying goods or services crucial to the health of the economy or saving large numbers of jobs (*ibid.*, at p. 593). Insolvency could be so widely felt as to impact stakeholders other than creditors and employees. Variants of these views resonate today, with reorganization justified in terms of rehabilitating companies that are key elements in a complex web of interdependent economic relationships in order to avoid the negative consequences of liquidation.

19 The *CCAA* fell into disuse during the next several decades, likely because amendments to the Act in 1953 restricted its use to companies issuing bonds (S.C. 1952-53, c. 3). During the economic downturn of the early 1980s, insolvency lawyers and courts adapting to the resulting wave of

insolvencies resurrected the statute and deployed it in response to new economic challenges. Participants in insolvency proceedings grew to recognize and appreciate the statute's distinguishing feature: a grant of broad and flexible authority to the supervising court to make the orders necessary to facilitate the reorganization of the debtor and achieve the *CCAA*'s objectives. The manner in which courts have used *CCAA* jurisdiction in increasingly creative and flexible ways is explored in greater detail below.

20 Efforts to evolve insolvency law were not restricted to the courts during this period. In 1970, a government-commissioned panel produced an extensive study recommending sweeping reform but Parliament failed to act (see *Bankruptcy and Insolvency: Report of the Study Committee on Bankruptcy and Insolvency Legislation* (1970)). Another panel of experts produced more limited recommendations in 1986 which eventually resulted in enactment of the *Bankruptcy and Insolvency Act* of 1992 (S.C. 1992, c. 27) (see *Proposed Bankruptcy Act Amendments: Report of the Advisory Committee on Bankruptcy and Insolvency* (1986)). Broader provisions for reorganizing insolvent debtors were then included in Canada's bankruptcy statute. Although the 1970 and 1986 reports made no specific recommendations with respect to the *CCAA*, the House of Commons committee studying the *BIA*'s predecessor bill, C-22, seemed to accept expert testimony that the *BIA*'s new reorganization scheme would shortly supplant the *CCAA*, which could then be repealed, with commercial insolvency and bankruptcy being governed by a single statute (*Minutes of Proceedings and Evidence of the Standing Committee on Consumer and Corporate Affairs and Government Operations*, Issue No. 15, October 3, 1991, at pp. 15:15-15:16).

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

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

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

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

23 Another point of convergence of the *CCAA* and the *BIA* relates to priorities. Because the *CCAA* is silent about what happens if reorganization fails, the *BIA* scheme of liquidation and distribution necessarily supplies the backdrop for what will happen if a *CCAA* reorganization is ultimately unsuccessful. In addition, one of the important features of legislative reform of both statutes since the enactment of the *BIA* in 1992 has been a cutback in Crown priorities (S.C. 1992, c. 27, s. 39; S.C. 1997, c. 12, ss. 73 and 125; S.C. 2000, c. 30, s. 148; S.C. 2005, c. 47, ss. 69 and 131; S.C. 2009, c. 33, ss. 25 and 29; see also *Quebec (Revenue) v. Caisse populaire Desjardins de Montmagny*, 2009 SCC 49, [2009] 3 S.C.R. 286; *Deputy Minister of Revenue v. Rainville*, [1980] 1 S.C.R. 35; *Proposed Bankruptcy Act Amendments: Report of the Advisory Committee on Bankruptcy and Insolvency* (1986)).

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

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

3.2 *GST Deemed Trust Under the CCAA*

26 The Court of Appeal proceeded on the basis that the *ETA* precluded the court from staying the Crown's enforcement of the GST deemed trust when partially lifting the stay to allow the debtor to enter bankruptcy. In so doing, it adopted the reasoning in a line of cases culminating in *Ottawa Senators*, which held that an *ETA* deemed trust remains enforceable during *CCAA* reorganization despite language in the *CCAA* that suggests otherwise.

27 The Crown relies heavily on the decision of the Ontario Court of Appeal in *Ottawa Senators* and argues that the later in time provision of the *ETA* creating the GST deemed trust trumps the provision of the *CCAA* purporting to nullify most statutory deemed trusts. The Court of Appeal in this case accepted this reasoning but not all provincial courts follow it (see, e.g., *Komunik Corp. (Arrangement relatif à)*, 2009 QCCS 6332 (CanLII), leave to appeal granted, 2010 QCCA 183 (CanLII)). Century Services relied, in its written submissions to this Court, on the argument that the court had authority under the *CCAA* to continue the stay against the Crown's claim for unremitted GST. In oral argument, the question of whether *Ottawa Senators* was correctly decided nonetheless arose. After the hearing, the parties were asked to make further written submissions on this point. As appears evident from the reasons of my colleague Abella J., this issue has become prominent

before this Court. In those circumstances, this Court needs to determine the correctness of the reasoning in *Ottawa Senators*.

28 The policy backdrop to this question involves the Crown's priority as a creditor in insolvency situations which, as I mentioned above, has evolved considerably. Prior to the 1990s, Crown claims largely enjoyed priority in insolvency. This was widely seen as unsatisfactory as shown by both the 1970 and 1986 insolvency reform proposals, which recommended that Crown claims receive no preferential treatment. A closely related matter was whether the *CCAA* was binding at all upon the Crown. Amendments to the *CCAA* in 1997 confirmed that it did indeed bind the Crown (see *CCAA*, s. 21, as am. by S.C. 1997, c. 12, s. 126).

29 Claims of priority by the state in insolvency situations receive different treatment across jurisdictions worldwide. For example, in Germany and Australia, the state is given no priority at all, while the state enjoys wide priority in the United States and France (see B. K. Morgan, "Should the Sovereign be Paid First? A Comparative International Analysis of the Priority for Tax Claims in Bankruptcy" (2000), 74 *Am. Bank. L.J.* 461, at p. 500). Canada adopted a middle course through legislative reform of Crown priority initiated in 1992. The Crown retained priority for source deductions of income tax, Employment Insurance ("EI") and Canada Pension Plan ("CPP") premiums, but ranks as an ordinary unsecured creditor for most other claims.

30 Parliament has frequently enacted statutory mechanisms to secure Crown claims and permit their enforcement. The two most common are statutory deemed trusts and powers to garnish funds third parties owe the debtor (see F. L. Lamer, *Priority of Crown Claims in Insolvency* (loose-leaf), at s. 2).

31 With respect to GST collected, Parliament has enacted a deemed trust. The *ETA* states that every person who collects an amount on account of GST is deemed to hold that amount in trust for the Crown (s. 222(1)). The deemed trust extends to other property of the person collecting the tax equal in value to the amount deemed to be in trust if that amount has not been remitted in accordance with the *ETA*. The deemed trust also extends to property held by a secured creditor that, but for the security interest, would be property of the person collecting the tax (s. 222(3)).

32 Parliament has created similar deemed trusts using almost identical language in respect of source deductions of income tax, EI premiums and CPP premiums (see s. 227(4) of the *Income Tax Act*, R.S.C. 1985, c. 1 (5th Supp.) ("*ITA*"), ss. 86(2) and (2.1) of the *Employment Insurance Act*, S.C. 1996, c. 23, and ss. 23(3) and (4) of the *Canada Pension Plan*, R.S.C. 1985, c. C-8). I will refer to income tax, EI and CPP deductions as "source deductions".

33 In *Royal Bank of Canada v. Sparrow Electric Corp.*, [1997] 1 S.C.R. 411, this Court addressed a priority dispute between a deemed trust for source deductions under the *ITA* and security interests taken under both the *Bank Act*, S.C. 1991, c. 46, and the Alberta *Personal Property Security Act*, S.A. 1988, c. P-4.05 ("*PPSA*"). As then worded, an *ITA* deemed trust over the debtor's property equivalent to the amount owing in respect of income tax became effective at the time of liquidation, receivership, or assignment in bankruptcy. *Sparrow Electric* held that the *ITA* deemed trust could not prevail over the security interests because, being fixed charges, the latter attached as soon as the debtor acquired rights in the property such that the *ITA* deemed trust had no property on which to attach when it subsequently arose. Later, in *First Vancouver Finance v. M.N.R.*, 2002 SCC 49, [2002] 2 S.C.R. 720, this Court observed that Parliament had legislated to strengthen the statutory deemed trust in the *ITA* by deeming it to operate from the moment the deductions were not paid

to the Crown as required by the *ITA*, and by granting the Crown priority over all security interests (paras. 27-29) (the "*Sparrow Electric* amendment").

34 The amended text of s. 227(4.1) of the *ITA* and concordant source deductions deemed trusts in the *Canada Pension Plan* and the *Employment Insurance Act* state that the deemed trust operates notwithstanding any other enactment of Canada, except ss. 81.1 and 81.2 of the *BIA*. The *ETA* deemed trust at issue in this case is similarly worded, but it excepts the *BIA* in its entirety. The provision reads as follows:

> **222**... .
>
> ...
>
> (3) Despite any other provision of this Act (except subsection (4)), any other enactment of Canada (except the *Bankruptcy and Insolvency Act*), any enactment of a province or any other law, if at any time an amount deemed by subsection (1) to be held by a person in trust for Her Majesty is not remitted to the Receiver General or withdrawn in the manner and at the time provided under this Part, property of the person and property held by any secured creditor of the person that, but for a security interest, would be property of the person, equal in value to the amount so deemed to be held in trust, is deemed ... .

35 The Crown submits that the *Sparrow Electric* amendment, added by Parliament to the *ETA* in 2000, was intended to preserve the Crown's priority over collected GST under the *CCAA* while subordinating the Crown to the status of an unsecured creditor in respect of GST only under the *BIA*. This is because the *ETA* provides that the GST deemed trust is effective "despite" any other enactment except the *BIA*.

36 The language used in the *ETA* for the GST deemed trust creates an apparent conflict with the *CCAA*, which provides that subject to certain exceptions, property deemed by statute to be held in trust for the Crown shall not be so regarded.

37 Through a 1997 amendment to the *CCAA* (S.C. 1997, c. 12, s. 125), Parliament appears to have, subject to specific exceptions, nullified deemed trusts in favour of the Crown once reorganization proceedings are commenced under the Act. The relevant provision reads:

> **18.3** (1) Subject to subsection (2), notwithstanding any provision in federal or provincial legislation that has the effect of deeming property to be held in trust for Her Majesty, property of a debtor company shall not be regarded as held in trust for Her Majesty unless it would be so regarded in the absence of that statutory provision.

This nullification of deemed trusts was continued in further amendments to the *CCAA* (S.C. 2005, c. 47), where s. 18.3(1) was renumbered and reformulated as s. 37(1):

> **37.** (1) Subject to subsection (2), despite any provision in federal or provincial legislation that has the effect of deeming property to be held in trust for Her Majesty, property of a debtor company shall not be regarded as being held in

> trust for Her Majesty unless it would be so regarded in the absence of that statutory provision.

38 An analogous provision exists in the *BIA*, which, subject to the same specific exceptions, nullifies statutory deemed trusts and makes property of the bankrupt that would otherwise be subject to a deemed trust part of the debtor's estate and available to creditors (S.C. 1992, c. 27, s. 39; S.C. 1997, c. 12, s. 73; *BIA*, s. 67(2)). It is noteworthy that in both the *CCAA* and the *BIA*, the exceptions concern source deductions (*CCAA*, s. 18.3(2); *BIA*, s. 67(3)). The relevant provision of the *CCAA* reads:

> **18.3** ...
>
> (2) Subsection (1) does not apply in respect of amounts deemed to be held in trust under subsection 227(4) or (4.1) of the *Income Tax Act*, subsection 23(3) or (4) of the *Canada Pension Plan* or subsection 86(2) or (2.1) of the *Employment Insurance Act*... .

Thus, the Crown's deemed trust and corresponding priority in source deductions remain effective both in reorganization and in bankruptcy.

39 Meanwhile, in both s. 18.4(1) of the *CCAA* and s. 86(1) of the *BIA*, other Crown claims are treated as unsecured. These provisions, establishing the Crown's status as an unsecured creditor, explicitly exempt statutory deemed trusts in source deductions (*CCAA*, s. 18.4(3); *BIA*, s. 86(3)). The *CCAA* provision reads as follows:

> **18.4** ...
>
> ...
>
> (3) Subsection (1) [Crown ranking as unsecured creditor] does not affect the operation of
>
> (*a*) subsections 224(1.2) and (1.3) of the *Income Tax Act*,
>
> (*b*) any provision of the *Canada Pension Plan* or of the *Employment Insurance Act* that refers to subsection 224(1.2) of the *Income Tax Act* and provides for the collection of a contribution ... .

Therefore, not only does the *CCAA* provide that Crown claims do not enjoy priority over the claims of other creditors (s. 18.3(1)), but the exceptions to this rule (i.e., that Crown priority is maintained for source deductions) are repeatedly stated in the statute.

40 The apparent conflict in this case is whether the rule in the *CCAA* first enacted as s. 18.3 in 1997, which provides that subject to certain explicit exceptions, statutory deemed trusts are ineffective under the *CCAA*, is overridden by the one in the *ETA* enacted in 2000 stating that GST deemed trusts operate despite any enactment of Canada except the *BIA*. With respect for my colleague Fish J., I do not think the apparent conflict can be resolved by denying it and creating a rule requiring both a statutory provision enacting the deemed trust, and a second statutory provision confirming it.

Such a rule is unknown to the law. Courts must recognize conflicts, apparent or real, and resolve them when possible.

41 A line of jurisprudence across Canada has resolved the apparent conflict in favour of the *ETA*, thereby maintaining GST deemed trusts under the *CCAA*. *Ottawa Senators*, the leading case, decided the matter by invoking the doctrine of implied repeal to hold that the later in time provision of the *ETA* should take precedence over the *CCAA* (see also *Solid Resources Ltd., Re* (2002), 40 C.B.R. (4th) 219 (Alta. Q.B.); *Gauntlet*).

42 The Ontario Court of Appeal in *Ottawa Senator* s rested its conclusion on two considerations. First, it was persuaded that by explicitly mentioning the *BIA* in *ETA* s. 222(3), but not the *CCAA*, Parliament made a deliberate choice. In the words of MacPherson J.A.:

> The *BIA* and the *CCAA* are closely related federal statutes. I cannot conceive that Parliament would specifically identify the *BIA* as an exception, but accidentally fail to consider the *CCAA* as a possible second exception. In my view, the omission of the *CCAA* from s. 222(3) of the *ETA* was almost certainly a considered omission. [para. 43]

43 Second, the Ontario Court of Appeal compared the conflict between the *ETA* and the *CCAA* to that before this Court in *Doré v. Verdun (City)*, [1997] 2 S.C.R. 862, and found them to be "identical" (para. 46). It therefore considered *Doré* binding (para. 49). In *Doré*, a limitations provision in the more general and recently enacted *Civil Code of Québec*, S.Q. 1991, c. 64 ("*C.C.Q.*"), was held to have repealed a more specific provision of the earlier Quebec *Cities and Towns Act*, R.S.Q., c. C-19, with which it conflicted. By analogy, the Ontario Court of Appeal held that the later in time and more general provision, s. 222(3) of the *ETA*, impliedly repealed the more specific and earlier in time provision, s. 18.3(1) of the *CCAA* (paras. 47-49).

44 Viewing this issue in its entire context, several considerations lead me to conclude that neither the reasoning nor the result in *Ottawa Senators* can stand. While a conflict may exist at the level of the statutes' wording, a purposive and contextual analysis to determine Parliament's true intent yields the conclusion that Parliament could not have intended to restore the Crown's deemed trust priority in GST claims under the *CCAA* when it amended the *ETA* in 2000 with the *Sparrow Electric* amendment.

45 I begin by recalling that Parliament has shown its willingness to move away from asserting priority for Crown claims in insolvency law. Section 18.3(1) of the *CCAA* (subject to the s. 18.3(2) exceptions) provides that the Crown's deemed trusts have no effect under the *CCAA*. Where Parliament has sought to protect certain Crown claims through statutory deemed trusts and intended that these deemed trusts continue in insolvency, it has legislated so explicitly and elaborately. For example, s. 18.3(2) of the *CCAA* and s. 67(3) of the *BIA* expressly provide that deemed trusts for source deductions remain effective in insolvency. Parliament has, therefore, clearly carved out exceptions from the general rule that deemed trusts are ineffective in insolvency. The *CCAA* and *BIA* are in harmony, preserving deemed trusts and asserting Crown priority only in respect of source deductions. Meanwhile, there is no express statutory basis for concluding that GST claims enjoy a preferred treatment under the *CCAA* or the *BIA*. Unlike source deductions, which are clearly and expressly dealt with under both these insolvency statutes, no such clear and express language exists in those Acts carving out an exception for GST claims.

46 The internal logic of the *CCAA* also militates against upholding the *ETA* deemed trust for GST. The *CCAA* imposes limits on a suspension by the court of the Crown's rights in respect of source deductions but does not mention the *ETA* (s. 11.4). Since source deductions deemed trusts are granted explicit protection under the *CCAA*, it would be inconsistent to afford a better protection to the *ETA* deemed trust absent explicit language in the *CCAA*. Thus, the logic of the *CCAA* appears to subject the *ETA* deemed trust to the waiver by Parliament of its priority (s. 18.4).

47 Moreover, a strange asymmetry would arise if the interpretation giving the *ETA* priority over the *CCAA* urged by the Crown is adopted here: the Crown would retain priority over GST claims during *CCAA* proceedings but not in bankruptcy. As courts have reflected, this can only encourage statute shopping by secured creditors in cases such as this one where the debtor's assets cannot satisfy both the secured creditors' and the Crown's claims (*Gauntlet*, at para. 21). If creditors' claims were better protected by liquidation under the *BIA*, creditors' incentives would lie overwhelmingly with avoiding proceedings under the *CCAA* and not risking a failed reorganization. Giving a key player in any insolvency such skewed incentives against reorganizing under the *CCAA* can only undermine that statute's remedial objectives and risk inviting the very social ills that it was enacted to avert.

48 Arguably, the effect of *Ottawa Senators* is mitigated if restructuring is attempted under the *BIA* instead of the *CCAA*, but it is not cured. If *Ottawa Senators* were to be followed, Crown priority over GST would differ depending on whether restructuring took place under the *CCAA* or the *BIA*. The anomaly of this result is made manifest by the fact that it would deprive companies of the option to restructure under the more flexible and responsive *CCAA* regime, which has been the statute of choice for complex reorganizations.

49 Evidence that Parliament intended different treatments for GST claims in reorganization and bankruptcy is scant, if it exists at all. Section 222(3) of the *ETA* was enacted as part of a wide-ranging budget implementation bill in 2000. The summary accompanying that bill does not indicate that Parliament intended to elevate Crown priority over GST claims under the *CCAA* to the same or a higher level than source deductions claims. Indeed, the summary for deemed trusts states only that amendments to existing provisions are aimed at "ensuring that employment insurance premiums and Canada Pension Plan contributions that are required to be remitted by an employer are fully recoverable by the Crown in the case of the bankruptcy of the employer" (Summary to S.C. 2000, c. 30, at p. 4a). The wording of GST deemed trusts resembles that of statutory deemed trusts for source deductions and incorporates the same overriding language and reference to the *BIA*. However, as noted above, Parliament's express intent is that only source deductions deemed trusts remain operative. An exception for the *BIA* in the statutory language establishing the source deductions deemed trusts accomplishes very little, because the explicit language of the *BIA* itself (and the *CCAA*) carves out these source deductions deemed trusts and maintains their effect. It is however noteworthy that no equivalent language maintaining GST deemed trusts exists under either the *BIA* or the *CCAA*.

50 It seems more likely that by adopting the same language for creating GST deemed trusts in the *ETA* as it did for deemed trusts for source deductions, and by overlooking the inclusion of an exception for the *CCAA* alongside the *BIA* in s. 222(3) of the *ETA*, Parliament may have inadvertently succumbed to a drafting anomaly. Because of a statutory lacuna in the *ETA*, the GST deemed trust could be seen as remaining effective in the *CCAA*, while ceasing to have any effect under the *BIA*, thus creating an apparent conflict with the wording of the *CCAA*. However, it should be seen

for what it is: a facial conflict only, capable of resolution by looking at the broader approach taken to Crown priorities and by giving precedence to the statutory language of s. 18.3 of the *CCAA* in a manner that does not produce an anomalous outcome.

51 Section 222(3) of the *ETA* evinces no explicit intention of Parliament to repeal *CCAA* s. 18.3. It merely creates an apparent conflict that must be resolved by statutory interpretation. Parliament's intent when it enacted *ETA* s. 222(3) was therefore far from unambiguous. Had it sought to give the Crown a priority for GST claims, it could have done so explicitly as it did for source deductions. Instead, one is left to infer from the language of *ETA* s. 222(3) that the GST deemed trust was intended to be effective under the *CCAA*.

52 I am not persuaded that the reasoning in *Doré* requires the application of the doctrine of implied repeal in the circumstances of this case. The main issue in *Doré* concerned the impact of the adoption of the *C.C.Q.* on the administrative law rules with respect to municipalities. While Gonthier J. concluded in that case that the limitation provision in art. 2930 *C.C.Q.* had repealed by implication a limitation provision in the *Cities and Towns Act*, he did so on the basis of more than a textual analysis. The conclusion in *Doré* was reached after thorough contextual analysis of both pieces of legislation, including an extensive review of the relevant legislative history (paras. 31-41). Consequently, the circumstances before this Court in *Doré* are far from "identical" to those in the present case, in terms of text, context and legislative history. Accordingly, *Doré* cannot be said to require the automatic application of the rule of repeal by implication.

53 A noteworthy indicator of Parliament's overall intent is the fact that in subsequent amendments it has not displaced the rule set out in the *CCAA*. Indeed, as indicated above, the recent amendments to the *CCAA* in 2005 resulted in the rule previously found in s. 18.3 being renumbered and reformulated as s. 37. Thus, to the extent the interpretation allowing the GST deemed trust to remain effective under the *CCAA* depends on *ETA* s. 222(3) having impliedly repealed *CCAA* s. 18.3(1) because it is later in time, we have come full circle. Parliament has renumbered and reformulated the provision of the *CCAA* stating that, subject to exceptions for source deductions, deemed trusts do not survive the *CCAA* proceedings and thus the *CCAA* is now the later in time statute. This confirms that Parliament's intent with respect to GST deemed trusts is to be found in the *CCAA*.

54 I do not agree with my colleague Abella J. that s. 44(*f*) of the *Interpretation Act*, R.S.C. 1985, c. I-21, can be used to interpret the 2005 amendments as having no effect. The new statute can hardly be said to be a mere re-enactment of the former statute. Indeed, the *CCAA* underwent a substantial review in 2005. Notably, acting consistently with its goal of treating both the *BIA* and the *CCAA* as sharing the same approach to insolvency, Parliament made parallel amendments to both statutes with respect to corporate proposals. In addition, new provisions were introduced regarding the treatment of contracts, collective agreements, interim financing and governance agreements. The appointment and role of the Monitor was also clarified. Noteworthy are the limits imposed by *CCAA* s. 11.09 on the court's discretion to make an order staying the Crown's source deductions deemed trusts, which were formerly found in s. 11.4. No mention whatsoever is made of GST deemed trusts (see Summary to S.C. 2005, c. 47). The review went as far as looking at the very expression used to describe the statutory override of deemed trusts. The comments cited by my colleague only emphasize the clear intent of Parliament to maintain its policy that only source deductions deemed trusts survive in *CCAA* proceedings.

55 In the case at bar, the legislative context informs the determination of Parliament's legislative intent and supports the conclusion that *ETA* s. 222(3) was not intended to narrow the scope of

the *CCAA*'s override provision. Viewed in its entire context, the conflict between the *ETA* and the *CCAA* is more apparent than real. I would therefore not follow the reasoning in *Ottawa Senators* and affirm that *CCAA* s. 18.3 remained effective.

56 My conclusion is reinforced by the purpose of the *CCAA* as part of Canadian remedial insolvency legislation. As this aspect is particularly relevant to the second issue, I will now discuss how courts have interpreted the scope of their discretionary powers in supervising a *CCAA* reorganization and how Parliament has largely endorsed this interpretation. Indeed, the interpretation courts have given to the *CCAA* helps in understanding how the *CCAA* grew to occupy such a prominent role in Canadian insolvency law.

3.3 *Discretionary Power of a Court Supervising a CCAA Reorganization*

57 Courts frequently observe that "[t]he *CCAA* is skeletal in nature" and does not "contain a comprehensive code that lays out all that is permitted or barred" (*Metcalfe & Mansfield Alternative Investments II Corp. (Re)*, 2008 ONCA 587, 92 O.R. (3d) 513, at para. 44, *per* Blair J.A.). Accordingly, "[t]he history of CCAA law has been an evolution of judicial interpretation" (*Dylex Ltd., Re* (1995), 31 C.B.R. (3d) 106 (Ont. Ct. (Gen. Div.)), at para. 10, *per* Farley J.).

58 *CCAA* decisions are often based on discretionary grants of jurisdiction. The incremental exercise of judicial discretion in commercial courts under conditions one practitioner aptly describes as "the hothouse of real-time litigation" has been the primary method by which the *CCAA* has been adapted and has evolved to meet contemporary business and social needs (see Jones, at p. 484).

59 Judicial discretion must of course be exercised in furtherance of the *CCAA*'s purposes. The remedial purpose I referred to in the historical overview of the Act is recognized over and over again in the jurisprudence. To cite one early example:

> The legislation is remedial in the purest sense in that it provides a means whereby the devastating social and economic effects of bankruptcy or creditor initiated termination of ongoing business operations can be avoided while a court-supervised attempt to reorganize the financial affairs of the debtor company is made.
>
> (*Elan Corp. v. Comiskey* (1990), 41 O.A.C. 282, at para. 57, *per* Doherty J.A., dissenting)

60 Judicial decision making under the *CCAA* takes many forms. A court must first of all provide the conditions under which the debtor can attempt to reorganize. This can be achieved by staying enforcement actions by creditors to allow the debtor's business to continue, preserving the *status quo* while the debtor plans the compromise or arrangement to be presented to creditors, and supervising the process and advancing it to the point where it can be determined whether it will succeed (see, e.g., *Chef Ready Foods Ltd. v. Hongkong Bank of Can.* (1990), 51 B.C.L.R. (2d) 84 (C.A.), at pp. 88-89; *Pacific National Lease Holding Corp., Re* (1992), 19 B.C.A.C. 134, at para. 27). In doing so, the court must often be cognizant of the various interests at stake in the reorganization, which can extend beyond those of the debtor and creditors to include employees, directors, shareholders, and even other parties doing business with the insolvent company (see, e.g., *Canadian Airlines Corp., Re*, 2000 ABQB 442, 84 Alta. L.R. (3d) 9, at para. 144, *per* Paperny J. (as she then was); *Air Canada, Re* (2003), 42 C.B.R. (4th) 173 (Ont. S.C.J.), at para. 3; *Air Canada, Re*, 2003 CanLII 49366 (Ont. S.C.J.), at para. 13, *per* Farley J.; Sarra, *Creditor Rights*, at pp. 181-92 and 217-26). In

addition, courts must recognize that on occasion the broader public interest will be engaged by aspects of the reorganization and may be a factor against which the decision of whether to allow a particular action will be weighed (see, e.g., *Canadian Red Cross Society/Société Canadienne de la Croix Rouge, Re* (2000), 19 C.B.R. (4th) 158 (Ont. S.C.J.), at para. 2, *per* Blair J. (as he then was); Sarra, *Creditor Rights*, at pp. 195-214).

61 When large companies encounter difficulty, reorganizations become increasingly complex. *CCAA* courts have been called upon to innovate accordingly in exercising their jurisdiction beyond merely staying proceedings against the debtor to allow breathing room for reorganization. They have been asked to sanction measures for which there is no explicit authority in the *CCAA*. Without exhaustively cataloguing the various measures taken under the authority of the *CCAA*, it is useful to refer briefly to a few examples to illustrate the flexibility the statute affords supervising courts.

62 Perhaps the most creative use of *CCAA* authority has been the increasing willingness of courts to authorize post-filing security for debtor in possession financing or super-priority charges on the debtor's assets when necessary for the continuation of the debtor's business during the reorganization (see, e.g., *Skydome Corp., Re* (1998), 16 C.B.R. (4th) 118 (Ont. Ct. (Gen. Div.)); *United Used Auto & Truck Parts Ltd., Re*, 2000 BCCA 146, 135 B.C.A.C. 96, aff'g (1999), 12 C.B.R. (4th) 144 (S.C.); and generally, J. P. Sarra, *Rescue! The Companies' Creditors Arrangement Act* (2007), at pp. 93-115). The *CCAA* has also been used to release claims against third parties as part of approving a comprehensive plan of arrangement and compromise, even over the objections of some dissenting creditors (see *Metcalfe & Mansfield*). As well, the appointment of a Monitor to oversee the reorganization was originally a measure taken pursuant to the *CCAA*'s supervisory authority; Parliament responded, making the mechanism mandatory by legislative amendment.

63 Judicial innovation during *CCAA* proceedings has not been without controversy. At least two questions it raises are directly relevant to the case at bar: (1) what are the sources of a court's authority during *CCAA* proceedings? (2) what are the limits of this authority?

64 The first question concerns the boundary between a court's statutory authority under the *CCAA* and a court's residual authority under its inherent and equitable jurisdiction when supervising a reorganization. In authorizing measures during *CCAA* proceedings, courts have on occasion purported to rely upon their equitable jurisdiction to advance the purposes of the Act or their inherent jurisdiction to fill gaps in the statute. Recent appellate decisions have counselled against purporting to rely on inherent jurisdiction, holding that the better view is that courts are in most cases simply construing the authority supplied by the *CCAA* itself (see, e.g., *Skeena Cellulose Inc., Re*, 2003 BCCA 344, 13 B.C.L.R. (4th) 236, at paras. 45-47, *per* Newbury J.A.; *Stelco Inc. (Re)* (2005), 75 O.R. (3d) 5 (C.A.), paras. 31-33, *per* Blair J.A.).

65 I agree with Justice Georgina R. Jackson and Professor Janis Sarra that the most appropriate approach is a hierarchical one in which courts rely first on an interpretation of the provisions of the *CCAA* text before turning to inherent or equitable jurisdiction to anchor measures taken in a *CCAA* proceeding (see G. R. Jackson and J. Sarra, "Selecting the Judicial Tool to get the Job Done: An Examination of Statutory Interpretation, Discretionary Power and Inherent Jurisdiction in Insolvency Matters", in J. P. Sarra, ed., *Annual Review of Insolvency Law 2007* (2008), 41, at p. 42). The authors conclude that when given an appropriately purposive and liberal interpretation, the *CCAA* will be sufficient in most instances to ground measures necessary to achieve its objectives (p. 94).

66 Having examined the pertinent parts of the *CCAA* and the recent history of the legislation, I accept that in most instances the issuance of an order during *CCAA* proceedings should be considered an exercise in statutory interpretation. Particularly noteworthy in this regard is the expansive interpretation the language of the statute at issue is capable of supporting.

67 The initial grant of authority under the *CCAA* empowered a court "where an application is made under this Act in respect of a company ... on the application of any person interested in the matter ..., subject to this Act, [to] make an order under this section" (*CCAA*, s. 11(1)). The plain language of the statute was very broad.

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

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

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

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

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

73 In the Court of Appeal, Tysoe J.A. held that no authority existed under the *CCAA* to continue staying the Crown's enforcement of the GST deemed trust once efforts at reorganization had come to an end. The appellant submits that in so holding, Tysoe J.A. failed to consider the underlying purpose of the *CCAA* and give the statute an appropriately purposive and liberal interpretation under which the order was permissible. The Crown submits that Tysoe J.A. correctly held that the mandatory language of the *ETA* gave the court no option but to permit enforcement of the GST

deemed trust when lifting the *CCAA* stay to permit the debtor to make an assignment under the *BIA*. Whether the *ETA* has a mandatory effect in the context of a *CCAA* proceeding has already been discussed. I will now address the question of whether the order was authorized by the *CCAA*.

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

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

76 There is no doubt that had reorganization been commenced under the *BIA* instead of the *CCAA*, the Crown's deemed trust priority for the GST funds would have been lost. Similarly, the Crown does not dispute that under the scheme of distribution in bankruptcy under the *BIA*, the deemed trust for GST ceases to have effect. Thus, after reorganization under the *CCAA* failed, creditors would have had a strong incentive to seek immediate bankruptcy and distribution of the debtor's assets under the *BIA*. In order to conclude that the discretion does not extend to partially lifting the stay in order to allow for an assignment in bankruptcy, one would have to assume a gap between the *CCAA* and the *BIA* proceedings. Brenner C.J.S.C.'s order staying Crown enforcement of the GST claim ensured that creditors would not be disadvantaged by the attempted reorganization under the *CCAA*. The effect of his order was to blunt any impulse of creditors to interfere in an orderly liquidation. His order was thus in furtherance of the *CCAA*'s objectives to the extent that it allowed a bridge between the *CCAA* and *BIA* proceedings. This interpretation of the tribunal's discretionary power is buttressed by s. 20 of the *CCAA*. That section provides that the *CCAA* "may be applied together with the provisions of any Act of Parliament ... that authorizes or makes provision for the sanction of compromises or arrangements between a company and its shareholders or any class of them", such as the *BIA*. Section 20 clearly indicates the intention of Parliament for the *CCAA* to operate *in tandem* with other insolvency legislation, such as the *BIA*.

77 The *CCAA* creates conditions for preserving the *status quo* while attempts are made to find common ground amongst stakeholders for a reorganization that is fair to all. Because the alternative to reorganization is often bankruptcy, participants will measure the impact of a reorganization against the position they would enjoy in liquidation. In the case at bar, the order fostered a harmonious transition between reorganization and liquidation while meeting the objective of a single collective proceeding that is common to both statutes.

78 Tysoe J.A. therefore erred in my view by treating the *CCAA* and the *BIA* as distinct regimes subject to a temporal gap between the two, rather than as forming part of an integrated body of insolvency law. Parliament's decision to maintain two statutory schemes for reorganization, the *BIA* and the *CCAA*, reflects the reality that reorganizations of differing complexity require different legal mechanisms. By contrast, only one statutory scheme has been found to be needed to liquidate a bankrupt debtor's estate. The transition from the *CCAA* to the *BIA* may require the partial lifting of a stay of proceedings under the *CCAA* to allow commencement of the *BIA* proceedings. However, as Laskin J.A. for the Ontario Court of Appeal noted in a similar competition between secured creditors and the Ontario Superintendent of Financial Services seeking to enforce a deemed trust, "[t]he two statutes are related" and no "gap" exists between the two statutes which would allow the en-

forcement of property interests at the conclusion of *CCAA* proceedings that would be lost in bankruptcy (*Ivaco Inc. (Re)* (2006), 83 O.R. (3d) 108, at paras. 62-63).

79 The Crown's priority in claims pursuant to source deductions deemed trusts does not undermine this conclusion. Source deductions deemed trusts survive under both the *CCAA* and the *BIA*. Accordingly, creditors' incentives to prefer one Act over another will not be affected. While a court has a broad discretion to stay source deductions deemed trusts in the *CCAA* context, this discretion is nevertheless subject to specific limitations applicable only to source deductions deemed trusts (*CCAA*, s. 11.4). Thus, if *CCAA* reorganization fails (e.g., either the creditors or the court refuse a proposed reorganization), the Crown can immediately assert its claim in unremitted source deductions. But this should not be understood to affect a seamless transition into bankruptcy or create any "gap" between the *CCAA* and the *BIA* for the simple reason that, regardless of what statute the reorganization had been commenced under, creditors' claims in both instances would have been subject to the priority of the Crown's source deductions deemed trust.

80 Source deductions deemed trusts aside, the comprehensive and exhaustive mechanism under the *BIA* must control the distribution of the debtor's assets once liquidation is inevitable. Indeed, an orderly transition to liquidation is mandatory under the *BIA* where a proposal is rejected by creditors. The *CCAA* is silent on the transition into liquidation but the breadth of the court's discretion under the Act is sufficient to construct a bridge to liquidation under the *BIA*. The court must do so in a manner that does not subvert the scheme of distribution under the *BIA*. Transition to liquidation requires partially lifting the *CCAA* stay to commence proceedings under the *BIA*. This necessary partial lifting of the stay should not trigger a race to the courthouse in an effort to obtain priority unavailable under the *BIA*.

81 I therefore conclude that Brenner C.J.S.C. had the authority under the *CCAA* to lift the stay to allow entry into liquidation.

3.4 *Express Trust*

82 The last issue in this case is whether Brenner C.J.S.C. created an express trust in favour of the Crown when he ordered on April 29, 2008, that proceeds from the sale of LeRoy Trucking's assets equal to the amount of unremitted GST be held back in the Monitor's trust account until the results of the reorganization were known. Tysoe J.A. in the Court of Appeal concluded as an alternative ground for allowing the Crown's appeal that it was the beneficiary of an express trust. I disagree.

83 Creation of an express trust requires the presence of three certainties: intention, subject matter, and object. Express or "true trusts" arise from the acts and intentions of the settlor and are distinguishable from other trusts arising by operation of law (see D. W. M. Waters, M. R. Gillen and L. D. Smith, eds., *Waters' Law of Trusts in Canada* (3rd ed. 2005), at pp. 28-29 especially fn. 42).

84 Here, there is no certainty to the object (i.e. the beneficiary) inferrable from the court's order of April 29, 2008, sufficient to support an express trust.

85 At the time of the order, there was a dispute between Century Services and the Crown over part of the proceeds from the sale of the debtor's assets. The court's solution was to accept LeRoy Trucking's proposal to segregate those monies until that dispute could be resolved. Thus there was no certainty that the Crown would actually be the beneficiary, or object, of the trust.

86 The fact that the location chosen to segregate those monies was the Monitor's trust account has no independent effect such that it would overcome the lack of a clear beneficiary. In any event, under the interpretation of *CCAA* s. 18.3(1) established above, no such priority dispute would even arise because the Crown's deemed trust priority over GST claims would be lost under the *CCAA* and the Crown would rank as an unsecured creditor for this amount. However, Brenner C.J.S.C. may well have been proceeding on the basis that, in accordance with *Ottawa Senators*, the Crown's GST claim would remain effective if reorganization was successful, which would not be the case if transition to the liquidation process of the *BIA* was allowed. An amount equivalent to that claim would accordingly be set aside pending the outcome of reorganization.

87 Thus, uncertainty surrounding the outcome of the *CCAA* restructuring eliminates the existence of any certainty to permanently vest in the Crown a beneficial interest in the funds. That much is clear from the oral reasons of Brenner C.J.S.C. on April 29, 2008, when he said: "Given the fact that [*CCAA* proceedings] are known to fail and filings in bankruptcy result, it seems to me that maintaining the status quo in the case at bar supports the proposal to have the monitor hold these funds in trust." Exactly who might take the money in the final result was therefore evidently in doubt. Brenner C.J.S.C.'s subsequent order of September 3, 2008, denying the Crown's application to enforce the trust once it was clear that bankruptcy was inevitable, confirms the absence of a clear beneficiary required to ground an express trust.

4. Conclusion

88 I conclude that Brenner C.J.S.C. had the discretion under the *CCAA* to continue the stay of the Crown's claim for enforcement of the GST deemed trust while otherwise lifting it to permit LeRoy Trucking to make an assignment in bankruptcy. My conclusion that s. 18.3(1) of the *CCAA* nullified the GST deemed trust while proceedings under that Act were pending confirms that the discretionary jurisdiction under s. 11 utilized by the court was not limited by the Crown's asserted GST priority, because there is no such priority under the *CCAA*.

89 For these reasons, I would allow the appeal and declare that the $305,202.30 collected by LeRoy Trucking in respect of GST but not yet remitted to the Receiver General of Canada is not subject to deemed trust or priority in favour of the Crown. Nor is this amount subject to an express trust. Costs are awarded for this appeal and the appeal in the court below.

The following are the reasons delivered by

FISH J.:--

I

90 I am in general agreement with the reasons of Justice Deschamps and would dispose of the appeal as she suggests.

91 More particularly, I share my colleague's interpretation of the scope of the judge's discretion under s. 11 of the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36 ("*CCAA*"). And I share my colleague's conclusion that Brenner C.J.S.C. did not create an express trust in favour of the Crown when he segregated GST funds into the Monitor's trust account (2008 BCSC 1805, [2008] G.S.T.C. 221).

92 I nonetheless feel bound to add brief reasons of my own regarding the interaction between the *CCAA* and the *Excise Tax Act*, R.S.C. 1985, c. E-15 ("*ETA*").

93 In upholding deemed trusts created by the *ETA* notwithstanding insolvency proceedings, *Ottawa Senators Hockey Club Corp. (Re)* (2005), 73 O.R. (3d) 737 (C.A.), and its progeny have been unduly protective of Crown interests which Parliament itself has chosen to subordinate to competing prioritized claims. In my respectful view, a clearly marked departure from that jurisprudential approach is warranted in this case.

94 Justice Deschamps develops important historical and policy reasons in support of this position and I have nothing to add in that regard. I do wish, however, to explain why a comparative analysis of related statutory provisions adds support to our shared conclusion.

95 Parliament has in recent years given detailed consideration to the Canadian insolvency scheme. It has declined to amend the provisions at issue in this case. Ours is not to wonder why, but rather to treat Parliament's preservation of the relevant provisions as a deliberate exercise of the legislative discretion that is Parliament's alone. With respect, I reject any suggestion that we should instead characterize the apparent conflict between s. 18.3(1) (now s. 37(1)) of the *CCAA* and s. 222 of the *ETA* as a drafting anomaly or statutory lacuna properly subject to judicial correction or repair.

II

96 In the context of the Canadian insolvency regime, a deemed trust will be found to exist only where two complementary elements co-exist: first, a statutory provision *creating* the trust; and second, a *CCAA* or *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3 ("*BIA*") provision *confirming* -- or explicitly preserving -- its effective operation.

97 This interpretation is reflected in three federal statutes. Each contains a deemed trust provision framed in terms strikingly similar to the wording of s. 222 of the *ETA*.

98 The first is the *Income Tax Act*, R.S.C. 1985, c. 1 (5th Supp.) ("*ITA*") where s. 227(4) *creates* a deemed trust:

> (4) Every person who deducts or withholds an amount under this Act is deemed, notwithstanding any security interest (as defined in subsection 224(1.3)) in the amount so deducted or withheld, to hold the amount separate and apart from the property of the person and from property held by any secured creditor (as defined in subsection 224(1.3)) of that person that but for the security interest would be property of the person, in trust for Her Majesty and for payment to Her Majesty in the manner and at the time provided under this Act. [Here and below, the emphasis is of course my own.]

99 In the next subsection, Parliament has taken care to make clear that this trust is unaffected by federal or provincial legislation to the contrary:

> (4.1) Notwithstanding any other provision of this Act, the *Bankruptcy and Insolvency Act* (except sections 81.1 and 81.2 of that Act), any other enactment of Canada, any enactment of a province or any other law, where at any time an amount deemed by subsection 227(4) to be held by a person in trust for Her Majesty is not paid to Her Majesty in the manner and at the time provided under

> this Act, property of the person ... equal in value to the amount so deemed to be held in trust is deemed
>
> (*a*) to be held, from the time the amount was deducted or withheld by the person, separate and apart from the property of the person, in trust for Her Majesty whether or not the property is subject to such a security interest, ...
>
> ...
>
> ... and the proceeds of such property shall be paid to the Receiver General in priority to all such security interests.

100 The continued operation of this deemed trust is expressly *confirmed* in s. 18.3 of the *CCAA*:

> **18.3** (1) Subject to subsection (2), notwithstanding any provision in federal or provincial legislation that has the effect of deeming property to be held in trust for Her Majesty, property of a debtor company shall not be regarded as being held in trust for Her Majesty unless it would be so regarded in the absence of that statutory provision.
>
> (2) Subsection (1) does not apply in respect of amounts deemed to be held in trust under subsection 227(4) or (4.1) of the *Income Tax Act*, subsection 23(3) or (4) of the *Canada Pension Plan* or subsection 86(2) or (2.1) of the *Employment Insurance Act* ... .

101 The operation of the *ITA* deemed trust is also confirmed in s. 67 of the *BIA*:

> (2) Subject to subsection (3), notwithstanding any provision in federal or provincial legislation that has the effect of deeming property to be held in trust for Her Majesty, property of a bankrupt shall not be regarded as held in trust for Her Majesty for the purpose of paragraph (1)(*a*) unless it would be so regarded in the absence of that statutory provision.
>
> (3) Subsection (2) does not apply in respect of amounts deemed to be held in trust under subsection 227(4) or (4.1) of the *Income Tax Act*, subsection 23(3) or (4) of the *Canada Pension Plan* or subsection 86(2) or (2.1) of the *Employment Insurance Act* ... .

102 Thus, Parliament has first *created* and then *confirmed the continued operation of* the Crown's *ITA* deemed trust under *both* the *CCAA* and the *BIA* regimes.

103 The second federal statute for which this scheme holds true is the *Canada Pension Plan*, R.S.C. 1985, c. C-8 ("*CPP*"). At s. 23, Parliament creates a deemed trust in favour of the Crown and specifies that it exists despite all contrary provisions in any other Canadian statute. Finally, and in almost identical terms, the *Employment Insurance Act*, S.C. 1996, c. 23 ("*EIA*"), creates a deemed trust in favour of the Crown: see ss. 86(2) and (2.1).

104 As we have seen, the survival of the deemed trusts created under these provisions of the *ITA*, the *CPP* and the *EIA* is confirmed in s. 18.3(2) the *CCAA* and in s. 67(3) the *BIA*. In all three cases, Parliament's intent to enforce the Crown's deemed trust through insolvency proceedings is expressed in clear and unmistakable terms.

105 The same is not true with regard to the deemed trust created under the *ETA*. Although Parliament creates a deemed trust in favour of the Crown to hold unremitted GST monies, and although it purports to maintain this trust notwithstanding any contrary federal or provincial legislation, it does not *confirm* the trust -- or expressly provide for its continued operation -- in either the *BIA* or the *CCAA*. The second of the two mandatory elements I have mentioned is thus absent reflecting Parliament's intention to allow the deemed trust to lapse with the commencement of insolvency proceedings.

106 The language of the relevant *ETA* provisions is identical in substance to that of the *ITA*, *CPP*, and *EIA* provisions:

> **222.** (1) Subject to subsection (1.1), every person who collects an amount as or on account of tax under Division II is deemed, for all purposes and despite any security interest in the amount, to hold the amount in trust for Her Majesty in right of Canada, separate and apart from the property of the person and from property held by any secured creditor of the person that, but for a security interest, would be property of the person, until the amount is remitted to the Receiver General or withdrawn under subsection (2).
>
> ...
>
> (3) Despite any other provision of this Act (except subsection (4)), any other enactment of Canada (except the *Bankruptcy and InsolvencyAct*), any enactment of a province or any other law, if at any time an amount deemed by subsection (1) to be held by a person in trust for Her Majesty is not remitted to the Receiver General or withdrawn in the manner and at the time provided under this Part, property of the person and property held by any secured creditor of the person that, but for a security interest, would be property of the person, equal in value to the amount so deemed to be held in trust, is deemed
>
> (*a*) to be held, from the time the amount was collected by the person, in trust for Her Majesty, separate and apart from the property of the person, whether or not the property is subject to a security interest, ...
>
> ...
>
> ... and the proceeds of the property shall be paid to the Receiver General in priority to all security interests.

107 Yet no provision of the *CCAA* provides for the continuation of this deemed trust after the *CCAA* is brought into play.

108 In short, Parliament has imposed *two* explicit conditions, or "building blocks", for survival under the *CCAA* of deemed trusts created by the *ITA*, *CPP*, and *EIA*. Had Parliament intended to likewise preserve under the *CCAA* deemed trusts created by the *ETA*, it would have included in the *CCAA* the sort of confirmatory provision that explicitly preserves other deemed trusts.

109 With respect, unlike Tysoe J.A., I do not find it "inconceivable that Parliament would specifically identify the *BIA* as an exception when enacting the current version of s. 222(3) of the *ETA* without considering the *CCAA* as a possible second exception" (2009 BCCA 205, 98 B.C.L.R. (4th) 242, at para. 37). *All* of the deemed trust provisions excerpted above make explicit reference to the *BIA*. Section 222 of the *ETA* does not break the pattern. Given the near-identical wording of the four deemed trust provisions, it would have been surprising indeed had Parliament not addressed the *BIA* at all in the *ETA*.

110 Parliament's evident intent was to render GST deemed trusts inoperative upon the institution of insolvency proceedings. Accordingly, s. 222 mentions the *BIA* so as to *exclude* it from its ambit -- rather than to *include* it, as do the *ITA*, the *CPP*, and the *EIA*.

111 Conversely, I note that *none* of these statutes mentions the *CCAA* expressly. Their specific reference to the *BIA* has no bearing on their interaction with the *CCAA*. Again, it is the confirmatory provisions *in the insolvency statutes* that determine whether a given deemed trust will subsist during insolvency proceedings.

112 Finally, I believe that chambers judges should not segregate GST monies into the Monitor's trust account during *CCAA* proceedings, as was done in this case. The result of Justice Deschamps's reasoning is that GST claims become unsecured under the *CCAA*. Parliament has deliberately chosen to nullify certain Crown super-priorities during insolvency; this is one such instance.

III

113 For these reasons, like Justice Deschamps, I would allow the appeal with costs in this Court and in the courts below and order that the $305,202.30 collected by LeRoy Trucking in respect of GST but not yet remitted to the Receiver General of Canada be subject to no deemed trust or priority in favour of the Crown.

The following are the reasons delivered by

114 ABELLA J. (dissenting):-- The central issue in this appeal is whether s. 222 of the *Excise Tax Act*, R.S.C. 1985, c. E-15 ("*ETA*"), and specifically s. 222(3), gives priority during *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36 ("*CCAA*"), proceedings to the Crown's deemed trust in unremitted GST. I agree with Tysoe J.A. that it does. It follows, in my respectful view, that a court's discretion under s. 11 of the *CCAA* is circumscribed accordingly.

115 Section 11[1] of the *CCAA* stated:

> **11.** (1) Notwithstanding anything in the *Bankruptcy and Insolvency Act* or the *Winding-up Act*, where an application is made under this Act in respect of a company, the court, on the application of any person interested in the matter, may, subject to this Act, on notice to any other person or without notice as it may see fit, make an order under this section.

To decide the scope of the court's discretion under s. 11, it is necessary to first determine the priority issue. Section 222(3), the provision of the *ETA* at issue in this case, states:

> (3) Despite any other provision of this Act (except subsection (4)), any other enactment of Canada (except the *Bankruptcy and Insolvency Act*), any enactment of a province or any other law, if at any time an amount deemed by subsection (1) to be held by a person in trust for Her Majesty is not remitted to the Receiver General or withdrawn in the manner and at the time provided under this Part, property of the person and property held by any secured creditor of the person that, but for a security interest, would be property of the person, equal in value to the amount so deemed to be held in trust, is deemed
>
> > (*a*) to be held, from the time the amount was collected by the person, in trust for Her Majesty, separate and apart from the property of the person, whether or not the property is subject to a security interest, and
> >
> > (*b*) to form no part of the estate or property of the person from the time the amount was collected, whether or not the property has in fact been kept separate and apart from the estate or property of the person and whether or not the property is subject to a security interest
>
> and is property beneficially owned by Her Majesty in right of Canada despite any security interest in the property or in the proceeds thereof and the proceeds of the property shall be paid to the Receiver General in priority to all security interests.

116 Century Services argued that the *CCAA*'s general override provision, s. 18.3(1), prevailed, and that the deeming provisions in s. 222 of the *ETA* were, accordingly, inapplicable during *CCAA* proceedings. Section 18.3(1) states:

> **18.3** (1) ... [N]otwithstanding any provision in federal or provincial legislation that has the effect of deeming property to be held in trust for Her Majesty, property of a debtor company shall not be regarded as held in trust for Her Majesty unless it would be so regarded in the absence of that statutory provision.

117 As MacPherson J.A. correctly observed in *Ottawa Senators Hockey Club Corp. (Re)* (2005), 73 O.R. (3d) 737 (C.A.), s. 222(3) of the *ETA* is in "clear conflict" with s. 18.3(1) of the *CCAA* (para. 31). Resolving the conflict between the two provisions is, essentially, what seems to me to be a relatively uncomplicated exercise in statutory interpretation: does the language reflect a clear legislative intention? In my view it does. The deemed trust provision, s. 222(3) of the *ETA*, has unambiguous language stating that it operates notwithstanding any law except the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3 ("*BIA*").

118 By expressly excluding only one statute from its legislative grasp, and by unequivocally stating that it applies despite any other law anywhere in Canada *except* the *BIA*, s. 222(3) has defined its boundaries in the clearest possible terms. I am in complete agreement with the following comments of MacPherson J.A. in *Ottawa Senators*:

> The legislative intent of s. 222(3) of the *ETA* is clear. If there is a conflict with "any other enactment of Canada (except the *Bankruptcy and Insolvency Act*)", s. 222(3) prevails. In these words Parliament did two things: it decided that s. 222(3) should trump all other federal laws and, importantly, it addressed the topic of exceptions to its trumping decision and identified a single exception, the *Bankruptcy and Insolvency Act*... . The *BIA* and the *CCAA* are closely related federal statutes. I cannot conceive that Parliament would specifically identify the *BIA* as an exception, but accidentally fail to consider the *CCAA* as a possible second exception. In my view, the omission of the *CCAA* from s. 222(3) of the *ETA* was almost certainly a considered omission. [para. 43]

119 MacPherson J.A.'s view that the failure to exempt the *CCAA* from the operation of the *ETA* is a reflection of a clear legislative intention, is borne out by how the *CCAA* was subsequently changed after s. 18.3(1) was enacted in 1997. In 2000, when s. 222(3) of the *ETA* came into force, amendments were also introduced to the *CCAA*. Section 18.3(1) was not amended.

120 The failure to amend s. 18.3(1) is notable because its effect was to protect the legislative *status quo*, notwithstanding repeated requests from various constituencies that s. 18.3(1) be amended to make the priorities in the *CCAA* consistent with those in the *BIA*. In 2002, for example, when Industry Canada conducted a review of the *BIA* and the *CCAA*, the Insolvency Institute of Canada and the Canadian Association of Insolvency and Restructuring Professionals recommended that the priority regime under the *BIA* be extended to the *CCAA* (Joint Task Force on Business Insolvency Law Reform, *Report* (March 15, 2002), Sch. B, proposal 71, at pp. 37-38). The same recommendations were made by the Standing Senate Committee on Banking, Trade and Commerce in its 2003 report, *Debtors and Creditors Sharing the Burden: A Review of the Bankruptcy and Insolvency Act and the Companies' Creditors Arrangement Act*; by the Legislative Review Task Force (Commercial) of the Insolvency Institute of Canada and the Canadian Association of Insolvency and Restructuring Professionals in its 2005 *Report on the Commercial Provisions of Bill C-55*; and in 2007 by the Insolvency Institute of Canada in a submission to the Standing Senate Committee on Banking, Trade and Commerce commenting on reforms then under consideration.

121 Yet the *BIA* remains the only exempted statute under s. 222(3) of the *ETA*. Even after the 2005 decision in *Ottawa Senators* which confirmed that the *ETA* took precedence over the *CCAA*, there was no responsive legislative revision. I see this lack of response as relevant in this case, as it was in *Tele-Mobile Co. v. Ontario*, 2008 SCC 12, [2008] 1 S.C.R. 305, where this Court stated:

> While it cannot be said that legislative silence is necessarily determinative of legislative intention, in this case the silence is Parliament's answer to the consistent urging of Telus and other affected businesses and organizations that there be express language in the legislation to ensure that businesses can be reimbursed for the reasonable costs of complying with evidence-gathering orders. I see the legislative history as reflecting Parliament's intention that compensation not be paid for compliance with production orders. [para. 42]

122 All this leads to a clear inference of a deliberate legislative choice to protect the deemed trust in s. 222(3) from the reach of s. 18.3(1) of the *CCAA*.

123 Nor do I see any "policy" justification for interfering, through interpretation, with this clarity of legislative intention. I can do no better by way of explaining why I think the policy argument cannot succeed in this case, than to repeat the words of Tysoe J.A. who said:

> I do not dispute that there are valid policy reasons for encouraging insolvent companies to attempt to restructure their affairs so that their business can continue with as little disruption to employees and other stakeholders as possible. It is appropriate for the courts to take such policy considerations into account, but only if it is in connection with a matter that has not been considered by Parliament. Here, Parliament must be taken to have weighed policy considerations when it enacted the amendments to the *CCAA* and *ETA* described above. As Mr. Justice MacPherson observed at para. 43 of *Ottawa Senators*, it is inconceivable that Parliament would specifically identify the *BIA* as an exception when enacting the current version of s. 222(3) of the *ETA* without considering the *CCAA* as a possible second exception. I also make the observation that the 1992 set of amendments to the *BIA* enabled proposals to be binding on secured creditors and, while there is more flexibility under the *CCAA*, it is possible for an insolvent company to attempt to restructure under the auspices of the *BIA*. [para. 37]

124 Despite my view that the clarity of the language in s. 222(3) is dispositive, it is also my view that even the application of other principles of interpretation reinforces this conclusion. In their submissions, the parties raised the following as being particularly relevant: the Crown relied on the principle that the statute which is "later in time" prevails; and Century Services based its argument on the principle that the general provision gives way to the specific (*generalia specialibus non derogant*).

125 The "later in time" principle gives priority to a more recent statute, based on the theory that the legislature is presumed to be aware of the content of existing legislation. If a new enactment is inconsistent with a prior one, therefore, the legislature is presumed to have intended to derogate from the earlier provisions (Ruth Sullivan, *Sullivan on the Construction of Statutes* (5th ed. 2008), at pp. 346-47; Pierre-André Côté, *The Interpretation of Legislation in Canada* (3rd ed. 2000), at p. 358).

126 The exception to this presumptive displacement of pre-existing inconsistent legislation, is the *generalia specialibus non derogant* principle that "[a] more recent, general provision will not be construed as affecting an earlier, special provision" (Côté, at p. 359). Like a Russian Doll, there is also an exception within this exception, namely, that an earlier, specific provision may in fact be "overruled" by a subsequent general statute if the legislature indicates, through its language, an intention that the general provision prevails (*Doré v. Verdun (City)*, [1997] 2 S.C.R. 862).

127 The primary purpose of these interpretive principles is to assist in the performance of the task of determining the intention of the legislature. This was confirmed by MacPherson J.A. in *Ottawa Senators*, at para. 42:

> [T]he overarching rule of statutory interpretation is that statutory provisions should be interpreted to give effect to the intention of the legislature in enacting the law. This primary rule takes precedence over all maxims or canons or aids relating to statutory interpretation, including the maxim that the specific prevails

over the general (*generalia specialibus non derogant*). As expressed by Hudson J. in *Canada v. Williams*, [1944] S.C.R. 226, ... at p. 239 ... :

> The maxim *generalia specialibus non derogant* is relied on as a rule which should dispose of the question, but the maxim is not a rule of law but a rule of construction and bows to the intention of the legislature, if such intention can reasonably be gathered from all of the relevant legislation.

(See also Côté, at p. 358, and Pierre-Andre Côté, with the collaboration of S. Beaulac and M. Devinat, *Interprétation des lois* (4th ed. 2009), at para. 1335.)

128 I accept the Crown's argument that the "later in time" principle is conclusive in this case. Since s. 222(3) of the *ETA* was enacted in 2000 and s. 18.3(1) of the *CCAA* was introduced in 1997, s. 222(3) is, on its face, the later provision. This chronological victory can be displaced, as Century Services argues, if it is shown that the more recent provision, s. 222(3) of the *ETA*, is a general one, in which case the earlier, specific provision, s. 18.3(1), prevails (*generalia specialibus non derogant*). But, as previously explained, the prior specific provision does not take precedence if the subsequent general provision appears to "overrule" it. This, it seems to me, is precisely what s. 222(3) achieves through the use of language stating that it prevails despite any law of Canada, of a province, or "any other law" *other than the BIA*. Section 18.3(1) of the *CCAA*, is thereby rendered inoperative for purposes of s. 222(3).

129 It is true that when the *CCAA* was amended in 2005,[2] s. 18.3(1) was re-enacted as s. 37(1) (S.C. 2005, c. 47, s. 131). Deschamps J. suggests that this makes s. 37(1) the new, "later in time" provision. With respect, her observation is refuted by the operation of s. 44(f) of the *Interpretation Act*, R.S.C. 1985, c. I-21, which expressly deals with the (non) effect of re-enacting, without significant substantive changes, a repealed provision (see *Attorney General of Canada v. Public Service Staff Relations Board*, [1977] 2 F.C. 663, dealing with the predecessor provision to s. 44(f)). It directs that new enactments not be construed as "new law" unless they differ in substance from the repealed provision:

> **44.** Where an enactment, in this section called the "former enactment", is repealed and another enactment, in this section called the "new enactment", is substituted therefor,
>
> ...
>
> (*f*) <u>except to the extent that the provisions of the new enactment are not in substance the same as those of the former enactment, the new enactment shall not be held to operate as new law</u>, but shall be construed and have effect as a consolidation and as declaratory of the law as contained in the former enactment;

Section 2 of the *Interpretation Act* defines an enactment as "an Act or regulation or <u>any portion of an Act or regulation</u>".

130 Section 37(1) of the current *CCAA* is almost identical to s. 18.3(1). These provisions are set out for ease of comparison, with the differences between them underlined:

> **37.** (1) Subject to subsection (2), despite any provision in federal or provincial legislation that has the effect of deeming property to be held in trust for Her Majesty, property of a debtor company shall not be regarded as being held in trust for Her Majesty unless it would be so regarded in the absence of that statutory provision.

> **18.3** (1) Subject to subsection (2), notwithstanding any provision in federal or provincial legislation that has the effect of deeming property to be held in trust for Her Majesty, property of a debtor company shall not be regarded as held in trust for Her Majesty unless it would be so regarded in the absence of that statutory provision.

131 The application of s. 44(*f*) of the *Interpretation Act* simply confirms the government's clearly expressed intent, found in Industry Canada's clause-by-clause review of Bill C-55, where s. 37(1) was identified as "a technical amendment to re-order the provisions of this Act". During second reading, the Hon. Bill Rompkey, then the Deputy Leader of the Government in the Senate, confirmed that s. 37(1) represented only a technical change:

> On a technical note relating to the treatment of deemed trusts for taxes, the bill [*sic*] makes no changes to the underlying policy intent, despite the fact that in the case of a restructuring under the CCAA, sections of the act [*sic*] were repealed and substituted with renumbered versions due to the extensive reworking of the CCAA.
>
> (*Debates of the Senate*, vol. 142, 1st Sess., 38th Parl., November 23, 2005, at p. 2147)

132 Had the substance of s. 18.3(1) altered in any material way when it was replaced by s. 37(1), I would share Deschamps J.'s view that it should be considered a new provision. But since s. 18.3(1) and s. 37(1) are the same in substance, the transformation of s. 18.3(1) into s. 37(1) has no effect on the interpretive queue, and s. 222(3) of the *ETA* remains the "later in time" provision (Sullivan, at p. 347).

133 This means that the deemed trust provision in s. 222(3) of the *ETA* takes precedence over s. 18.3(1) during *CCAA* proceedings. The question then is how that priority affects the discretion of a court under s. 11 of the *CCAA*.

134 While s. 11 gives a court discretion to make orders notwithstanding the *BIA* and the *Winding-up Act*, R.S.C. 1985, c. W-11, that discretion is not liberated from the operation of any other federal statute. Any exercise of discretion is therefore circumscribed by whatever limits are imposed by statutes *other* than the *BIA* and the *Winding-up Act*. That includes the *ETA*. The chambers judge in this case was, therefore, required to respect the priority regime set out in s. 222(3) of the *ETA*. Neither s. 18.3(1) nor s. 11 of the *CCAA* gave him the authority to ignore it. He could not, as a result, deny the Crown's request for payment of the GST funds during the *CCAA* proceedings.

135 Given this conclusion, it is unnecessary to consider whether there was an express trust.

136 I would dismiss the appeal.

Appeal allowed with costs, ABELLA J. *dissenting.*

* * * * *

APPENDIX

Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36 (as at December 13, 2007)

11. (1) [Powers of court] Notwithstanding anything in the *Bankruptcy and Insolvency Act* or the *Winding-up Act*, where an application is made under this Act in respect of a company, the court, on the application of any person interested in the matter, may, subject to this Act, on notice to any other person or without notice as it may see fit, make an order under this section.

...

(3) [Initial application court orders] 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.

(4) [Other than initial application court orders] A court may, on an application in respect of a company other than an initial application, make an order on such terms as it may impose,

(*a*) staying, until otherwise ordered by the court, for such period as the court deems necessary, 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.

...

(6) [Burden of proof on application] The court shall not make an order under subsection (3) or (4) unless

(*a*) the applicant satisfies the court that circumstances exist that make such an order appropriate; and

(*b*) in the case of an order under subsection (4), the applicant also satisfies the court that the applicant has acted, and is acting, in good faith and with due diligence.

11.4 (1) [Her Majesty affected] An order made under section 11 may provide that

(*a*) Her Majesty in right of Canada may not exercise rights under subsection 224(1.2) of the *Income Tax Act* or any provision of the *Canada Pension Plan* or of the *Employment Insurance Act* that refers to subsection 224(1.2) of the *Income Tax Act* and provides for the collection of a contribution, as defined in the *Canada Pension Plan*, or an employee's premium, or employer's premium, as defined in the *Employment Insurance Act*, and of any related interest, penalties or other amounts, in respect of the company if the company is a tax debtor under that subsection or provision, for such period as the court considers appropriate but ending not later than

(i) the expiration of the order,
(ii) the refusal of a proposed compromise by the creditors or the court,
(iii) six months following the court sanction of a compromise or arrangement,
(iv) the default by the company on any term of a compromise or arrangement, or
(v) the performance of a compromise or arrangement in respect of the company; and

(*b*) Her Majesty in right of a province may not exercise rights under any provision of provincial legislation in respect of the company where the company is a debtor under that legislation and the provision has a similar purpose to subsection 224(1.2) of the *Income Tax Act*, or refers to that subsection, to the extent that it provides for the collection of a sum, and of any related interest, penalties or other amounts, where the sum

(i) has been withheld or deducted by a person from a payment to another person and is in respect of a tax similar in nature to the income tax imposed on individuals under the *Income Tax Act*, or
(ii) is of the same nature as a contribution under the *Canada Pension Plan* if the province is a "province providing a comprehensive pension plan" as defined in subsection 3(1) of the *Canada Pension Plan* and the provincial legislation establishes a "provincial pension plan" as defined in that subsection,

for such period as the court considers appropriate but ending not later than the occurrence or time referred to in whichever of subparagraphs (*a*)(i) to (v) may apply.

(2) [When order ceases to be in effect] An order referred to in subsection (1) ceases to be in effect if

(*a*) the company defaults on payment of any amount that becomes due to Her Majesty after the order is made and could be subject to a demand under

(i) subsection 224(1.2) of the *Income Tax Act*,
(ii) any provision of the *Canada Pension Plan* or of the *Employment Insurance Act* that refers to subsection 224(1.2) of the *Income Tax Act* and provides for the collection of a contribution, as defined in the *Canada Pension Plan*, or an employee's premium, or employer's premium, as defined in the *Employment Insurance Act*, and of any related interest, penalties or other amounts, or
(iii) under any provision of provincial legislation that has a similar purpose to subsection 224(1.2) of the *Income Tax Act*, or that refers to that subsection, to the extent that it provides for the collection of a sum, and of any related interest, penalties or other amounts, where the sum

(A) has been withheld or deducted by a person from a payment to another person and is in respect of a tax similar in nature to the income tax imposed on individuals under the *Income Tax Act*, or
(B) is of the same nature as a contribution under the *Canada Pension Plan* if the province is a "province providing a comprehensive pension plan" as defined in subsection 3(1) of the *Canada Pension Plan* and the provincial legislation establishes a "provincial pension plan" as defined in that subsection; or

(*b*) any other creditor is or becomes entitled to realize a security on any property that could be claimed by Her Majesty in exercising rights under

(i) subsection 224(1.2) of the *Income Tax Act*,
(ii) any provision of the *Canada Pension Plan* or of the *Employment Insurance Act* that refers to subsection 224(1.2) of the *Income Tax Act* and provides for the collection of a contribution, as defined in the *Canada Pension Plan*, or an employee's premium, or employer's premium, as defined in the *Employment Insurance Act*, and of any related interest, penalties or other amounts, or
(iii) any provision of provincial legislation that has a similar purpose to subsection 224(1.2) of the *Income Tax Act*, or that refers to that subsection, to the extent that it provides for the collection of a sum, and of any related interest, penalties or other amounts, where the sum

(A) has been withheld or deducted by a person from a payment to another person and is in respect of a tax similar in nature to the income tax imposed on individuals under the *Income Tax Act*, or
(B) is of the same nature as a contribution under the *Canada Pension Plan* if the province is a "province providing a comprehensive pension plan" as defined in subsection 3(1) of the *Canada Pension Plan* and the provincial legislation establishes a "provincial pension plan" as defined in that subsection.

(3) [Operation of similar legislation] An order made under section 11, other than an order referred to in subsection (1) of this section, does not affect the operation of

(*a*) subsections 224(1.2) and (1.3) of the *Income Tax Act*,

(*b*) any provision of the *Canada Pension Plan* or of the *Employment Insurance Act* that refers to subsection 224(1.2) of the *Income Tax Act* and provides for the collection of a contribution, as defined in the *Canada Pension Plan*, or an employee's premium, or employer's premium, as defined in the *Employment Insurance Act*, and of any related interest, penalties or other amounts, or

(*c*) any provision of provincial legislation that has a similar purpose to subsection 224(1.2) of the *Income Tax Act*, or that refers to that subsection, to the extent that it provides for the collection of a sum, and of any related interest, penalties or other amounts, where the sum

(i) has been withheld or deducted by a person from a payment to another person and is in respect of a tax similar in nature to the income tax imposed on individuals under the *Income Tax Act*, or

(ii) is of the same nature as a contribution under the *Canada Pension Plan* if the province is a "province providing a comprehensive pension plan" as defined in subsection 3(1) of the *Canada Pension Plan* and the provincial legislation establishes a "provincial pension plan" as defined in that subsection,

and for the purpose of paragraph (*c*), the provision of provincial legislation is, despite any Act of Canada or of a province or any other law, deemed to have the same effect and scope against any creditor, however secured, as subsection 224(1.2) of the *Income Tax Act* in respect of a sum referred to in subparagraph (*c*)(i), or as subsection 23(2) of the *Canada Pension Plan* in respect of a sum referred to in subparagraph (*c*)(ii), and in respect of any related interest, penalties or other amounts.

18.3 (1) [Deemed trusts] Subject to subsection (2), notwithstanding any provision in federal or provincial legislation that has the effect of deeming property to be held in trust for Her Majesty, property of a debtor company shall not be regarded as held in trust for Her Majesty unless it would be so regarded in the absence of that statutory provision.

(2) [Exceptions] Subsection (1) does not apply in respect of amounts deemed to be held in trust under subsection 227(4) or (4.1) of the *Income Tax Act*, subsection 23(3) or (4) of the *Canada Pension Plan* or subsection 86(2) or (2.1) of the *Employment Insurance Act* (each of which is in this subsection referred to as a "federal provision") nor in respect of amounts deemed to be held in trust under any law of a province that creates a deemed trust the sole purpose of which is to ensure remittance to Her Majesty in right of the province of amounts deducted or withheld under a law of the province where

(*a*) that law of the province imposes a tax similar in nature to the tax imposed under the *Income Tax Act* and the amounts deducted or withheld under that law of the province are of the same nature as the amounts referred to in subsection 227(4) or (4.1) of the *Income Tax Act*, or

(*b*) the province is a "province providing a comprehensive pension plan" as defined in subsection 3(1) of the *Canada Pension Plan*, that law of the province establishes a "provincial pension plan" as defined in that subsection and the amounts deducted or withheld under that law of the province are of the same nature as amounts referred to in subsection 23(3) or (4) of the *Canada Pension Plan*,

and for the purpose of this subsection, any provision of a law of a province that creates a deemed trust is, notwithstanding any Act of Canada or of a province or any other law, deemed to have the same effect and scope against any creditor, however secured, as the corresponding federal provision.

18.4 (1) [Status of Crown claims] In relation to a proceeding under this Act, all claims, including secured claims, of Her Majesty in right of Canada or a province or any body under an enactment respecting workers' compensation, in this section and in section 18.5 called a "workers' compensation body", rank as unsecured claims.

...

(3) [Operation of similar legislation] Subsection (1) does not affect the operation of

(*a*) subsections 224(1.2) and (1.3) of the *Income Tax Act*,

(*b*) any provision of the *Canada Pension Plan* or of the *Employment Insurance Act* that refers to subsection 224(1.2) of the *Income Tax Act* and provides for the collection of a contribution, as defined in the *Canada Pension Plan*, or an employee's premium, or employer's premium, as defined in the *Employment Insurance Act*, and of any related interest, penalties or other amounts, or

(*c*) any provision of provincial legislation that has a similar purpose to subsection 224(1.2) of the *Income Tax Act*, or that refers to that subsection, to the extent that it provides for the collection of a sum, and of any related interest, penalties or other amounts, where the sum

(i) has been withheld or deducted by a person from a payment to another person and is in respect of a tax similar in nature to the income tax imposed on individuals under the *Income Tax Act*, or

(ii) is of the same nature as a contribution under the *Canada Pension Plan* if the province is a "provincc providing a comprehensive pension plan" as defined in subsection 3(1) of the *Canada Pension Plan* and the provincial legislation establishes a "provincial pension plan" as defined in that subsection,

and for the purpose of paragraph (*c*), the provision of provincial legislation is, despite any Act of Canada or of a province or any other law, deemed to have the same effect and scope against any creditor, however secured, as subsection 224(1.2) of the *Income Tax Act* in respect of a sum referred to in subparagraph (*c*)(i), or as subsection 23(2) of the *Canada Pension Plan* in respect of a sum referred to in subparagraph (*c*)(ii), and in respect of any related interest, penalties or other amounts.

20. [Act to be applied conjointly with other Acts] The provisions of this Act may be applied together with the provisions of any Act of Parliament or of the legislature of any province, that authorizes or makes provision for the sanction of compromises or arrangements between a company and its shareholders or any class of them.

Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36 (as at September 18, 2009)

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

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

> (*a*) staying, until otherwise ordered by the court, all proceedings taken or that might be taken in respect of the company under the *Bankruptcy and Insolvency Act* or the *Winding-up and Restructuring Act*;
>
> (*b*) restraining, until otherwise ordered by the court, further proceedings in any action, suit or proceeding against the company; and
>
> (*c*) prohibiting, until otherwise ordered by the court, the commencement of any action, suit or proceeding against the company.

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

> (*a*) staying, until otherwise ordered by the court, for any period that the court considers necessary, all proceedings taken or that might be taken in respect of the company under an Act referred to in paragraph (1)(*a*);
>
> (*b*) restraining, until otherwise ordered by the court, further proceedings in any action, suit or proceeding against the company; and
>
> (*c*) prohibiting, until otherwise ordered by the court, the commencement of any action, suit or proceeding against the company.

(3) [Burden of proof on application] The court shall not make the order unless

> (a) the applicant satisfies the court that circumstances exist that make the order appropriate; and
>
> (b) in the case of an order under subsection (2), the applicant also satisfies the court that the applicant has acted, and is acting, in good faith and with due diligence.

...

11.09 (1) [Stay -- Her Majesty] An order made under section 11.02 may provide that

(*a*) Her Majesty in right of Canada may not exercise rights under subsection 224(1.2) of the *Income Tax Act* or any provision of the *Canada Pension Plan* or of the *Employment Insurance Act* that refers to subsection 224(1.2) of the *Income Tax Act* and provides for the collection of a contribution, as defined in the *Canada Pension Plan*, or an employee's premium, or employer's premium, as defined in the *Employment Insurance Act*, and of any related interest, penalties or other amounts, in respect of the company if the company is a tax debtor under that subsection or provision, for the period that the court considers appropriate but ending not later than

(i) the expiry of the order,
(ii) the refusal of a proposed compromise by the creditors or the court,
(iii) six months following the court sanction of a compromise or an arrangement,
(iv) the default by the company on any term of a compromise or an arrangement, or
(v) the performance of a compromise or an arrangement in respect of the company; and

(*b*) Her Majesty in right of a province may not exercise rights under any provision of provincial legislation in respect of the company if the company is a debtor under that legislation and the provision has a purpose similar to subsection 224(1.2) of the *Income Tax Act*, or refers to that subsection, to the extent that it provides for the collection of a sum, and of any related interest, penalties or other amounts, and the sum

(i) has been withheld or deducted by a person from a payment to another person and is in respect of a tax similar in nature to the income tax imposed on individuals under the *Income Tax Act*, or
(ii) is of the same nature as a contribution under the *Canada Pension Plan* if the province is a "province providing a comprehensive pension plan" as defined in subsection 3(1) of the *Canada Pension Plan* and the provincial legislation establishes a "provincial pension plan" as defined in that subsection,

for the period that the court considers appropriate but ending not later than the occurrence or time referred to in whichever of subparagraphs (*a*)(i) to (v) that may apply.

(2) [When order ceases to be in effect] The portions of an order made under section 11.02 that affect the exercise of rights of Her Majesty referred to in paragraph (1)(*a*) or (*b*) cease to be in effect if

(*a*) the company defaults on the payment of any amount that becomes due to Her Majesty after the order is made and could be subject to a demand under

(i) subsection 224(1.2) of the *Income Tax Act*,

(ii) any provision of the *Canada Pension Plan* or of the *Employment Insurance Act* that refers to subsection 224(1.2) of the *Income Tax Act* and provides for the collection of a contribution, as defined in the *Canada Pension Plan*, or an employee's premium, or employer's premium, as defined in the *Employment Insurance Act*, and of any related interest, penalties or other amounts, or

(iii) any provision of provincial legislation that has a purpose similar to subsection 224(1.2) of the *Income Tax Act*, or that refers to that subsection, to the extent that it provides for the collection of a sum, and of any related interest, penalties or other amounts, and the sum

(A) has been withheld or deducted by a person from a payment to another person and is in respect of a tax similar in nature to the income tax imposed on individuals under the *Income Tax Act*, or

(B) is of the same nature as a contribution under the *Canada Pension Plan* if the province is a "province providing a comprehensive pension plan" as defined in subsection 3(1) of the *Canada Pension Plan* and the provincial legislation establishes a "provincial pension plan" as defined in that subsection; or

(*b*) any other creditor is or becomes entitled to realize a security on any property that could be claimed by Her Majesty in exercising rights under

(i) subsection 224(1.2) of the *Income Tax Act*,

(ii) any provision of the *Canada Pension Plan* or of the *Employment Insurance Act* that refers to subsection 224(1.2) of the *Income Tax Act* and provides for the collection of a contribution, as defined in the *Canada Pension Plan*, or an employee's premium, or employer's premium, as defined in the *Employment Insurance Act*, and of any related interest, penalties or other amounts, or

(iii) any provision of provincial legislation that has a purpose similar to subsection 224(1.2) of the *Income Tax Act*, or that refers to that subsection, to the extent that it provides for the collection of a sum, and of any related interest, penalties or other amounts, and the sum

(A) has been withheld or deducted by a person from a payment to another person and is in respect of a tax similar in nature to the income tax imposed on individuals under the *Income Tax Act*, or

(B) is of the same nature as a contribution under the *Canada Pension Plan* if the province is a "province providing a comprehensive pension plan" as defined in subsection 3(1) of the *Canada Pension Plan* and the provincial legislation establishes a "provincial pension plan" as defined in that subsection.

(3) [Operation of similar legislation] An order made under section 11.02, other than the portions of that order that affect the exercise of rights of Her Majesty referred to in paragraph (1)(*a*) or (*b*), does not affect the operation of

(*a*) subsections 224(1.2) and (1.3) of the *Income Tax Act*,

(*b*) any provision of the *Canada Pension Plan* or of the *Employment Insurance Act* that refers to subsection 224(1.2) of the *Income Tax Act* and provides for the collection of a contribution, as defined in the *Canada Pension Plan*, or an employee's premium, or employer's premium, as defined in the *Employment Insurance Act*, and of any related interest, penalties or other amounts, or

(*c*) any provision of provincial legislation that has a purpose similar to subsection 224(1.2) of the *Income Tax Act*, or that refers to that subsection, to the extent that it provides for the collection of a sum, and of any related interest, penalties or other amounts, and the sum

(i) has been withheld or deducted by a person from a payment to another person and is in respect of a tax similar in nature to the income tax imposed on individuals under the *Income Tax Act*, or
(ii) is of the same nature as a contribution under the *Canada Pension Plan* if the province is a "province providing a comprehensive pension plan" as defined in subsection 3(1) of the *Canada Pension Plan* and the provincial legislation establishes a "provincial pension plan" as defined in that subsection,

and for the purpose of paragraph (*c*), the provision of provincial legislation is, despite any Act of Canada or of a province or any other law, deemed to have the same effect and scope against any creditor, however secured, as subsection 224(1.2) of the *Income Tax Act* in respect of a sum referred to in subparagraph (*c*)(i), or as subsection 23(2) of the *Canada Pension Plan* in respect of a sum referred to in subparagraph (*c*)(ii), and in respect of any related interest, penalties or other amounts.

37. (1) [Deemed trusts] Subject to subsection (2), despite any provision in federal or provincial legislation that has the effect of deeming property to be held in trust for Her Majesty, property of a debtor company shall not be regarded as being held in trust for Her Majesty unless it would be so regarded in the absence of that statutory provision.

(2) [Exceptions] Subsection (1) does not apply in respect of amounts deemed to be held in trust under subsection 227(4) or (4.1) of the *Income Tax Act*, subsection 23(3) or (4) of the *Canada Pension Plan* or subsection 86(2) or (2.1) of the *Employment Insurance Act* (each of which is in this subsection referred to as a "federal provision"), nor does it apply in respect of amounts deemed to be held in trust under any law of a province that creates a deemed trust the sole purpose of which is to ensure remittance to Her Majesty in right of the province of amounts deducted or withheld under a law of the province if

(*a*) that law of the province imposes a tax similar in nature to the tax imposed under the *Income Tax Act* and the amounts deducted or withheld under that law of the province are of the same nature as the amounts referred to in subsection 227(4) or (4.1) of the *Income Tax Act*, or

(*b*) the province is a "province providing a comprehensive pension plan" as defined in subsection 3(1) of the *Canada Pension Plan*, that law of the province

establishes a "provincial pension plan" as defined in that subsection and the amounts deducted or withheld under that law of the province are of the same nature as amounts referred to in subsection 23(3) or (4) of the *Canada Pension Plan*,

and for the purpose of this subsection, any provision of a law of a province that creates a deemed trust is, despite any Act of Canada or of a province or any other law, deemed to have the same effect and scope against any creditor, however secured, as the corresponding federal provision.

Excise Tax Act, R.S.C. 1985, c. E-15 (as at December 13, 2007)

222. (1) [Trust for amounts collected] Subject to subsection (1.1), every person who collects an amount as or on account of tax under Division II is deemed, for all purposes and despite any security interest in the amount, to hold the amount in trust for Her Majesty in right of Canada, separate and apart from the property of the person and from property held by any secured creditor of the person that, but for a security interest, would be property of the person, until the amount is remitted to the Receiver General or withdrawn under subsection (2).

(1.1) [Amounts collected before bankruptcy] Subsection (1) does not apply, at or after the time a person becomes a bankrupt (within the meaning of the *Bankruptcy and Insolvency Act*), to any amounts that, before that time, were collected or became collectible by the person as or on account of tax under Division II.

...

(3) [Extension of trust] Despite any other provision of this Act (except subsection (4)), any other enactment of Canada (except the *Bankruptcy and Insolvency Act*), any enactment of a province or any other law, if at any time an amount deemed by subsection (1) to be held by a person in trust for Her Majesty is not remitted to the Receiver General or withdrawn in the manner and at the time provided under this Part, property of the person and property held by any secured creditor of the person that, but for a security interest, would be property of the person, equal in value to the amount so deemed to be held in trust, is deemed

(*a*) to be held, from the time the amount was collected by the person, in trust for Her Majesty, separate and apart from the property of the person, whether or not the property is subject to a security interest, and

(*b*) to form no part of the estate or property of the person from the time the amount was collected, whether or not the property has in fact been kept separate and apart from the estate or property of the person and whether or not the property is subject to a security interest

and is property beneficially owned by Her Majesty in right of Canada despite any security interest in the property or in the proceeds thereof and the proceeds of the property shall be paid to the Receiver General in priority to all security interests.

Bankruptcy and Insolvency Act, R.S.C. 1985, c. B-3 (as at December 13, 2007)

67. (1) [Property of bankrupt] The property of a bankrupt divisible among his creditors shall not comprise

(*a*) property held by the bankrupt in trust for any other person,

(*b*) any property that as against the bankrupt is exempt from execution or seizure under any laws applicable in the province within which the property is situated and within which the bankrupt resides, or

(*b*.1) such goods and services tax credit payments and prescribed payments relating to the essential needs of an individual as are made in prescribed circumstances and are not property referred to in paragraph (*a*) or (*b*),

but it shall comprise

(*c*) all property wherever situated of the bankrupt at the date of his bankruptcy or that may be acquired by or devolve on him before his discharge, and

(*d*) such powers in or over or in respect of the property as might have been exercised by the bankrupt for his own benefit.

(2) [Deemed trusts] Subject to subsection (3), notwithstanding any provision in federal or provincial legislation that has the effect of deeming property to be held in trust for Her Majesty, property of a bankrupt shall not be regarded as held in trust for Her Majesty for the purpose of paragraph (1)(*a*) unless it would be so regarded in the absence of that statutory provision.

(3) [Exceptions] Subsection (2) does not apply in respect of amounts deemed to be held in trust under subsection 227(4) or (4.1) of the *Income Tax Act*, subsection 23(3) or (4) of the *Canada Pension Plan* or subsection 86(2) or (2.1) of the *Employment Insurance Act* (each of which is in this subsection referred to as a "federal provision") nor in respect of amounts deemed to be held in trust under any law of a province that creates a deemed trust the sole purpose of which is to ensure remittance to Her Majesty in right of the province of amounts deducted or withheld under a law of the province where

(*a*) that law of the province imposes a tax similar in nature to the tax imposed under the *Income Tax Act* and the amounts deducted or withheld under that law of the province are of the same nature as the amounts referred to in subsection 227(4) or (4.1) of the *Income Tax Act*, or

(*b*) the province is a "province providing a comprehensive pension plan" as defined in subsection 3(1) of the *Canada Pension Plan*, that law of the province establishes a "provincial pension plan" as defined in that subsection and the amounts deducted or withheld under that law of the province are of the same nature as amounts referred to in subsection 23(3) or (4) of the *Canada Pension Plan*,

and for the purpose of this subsection, any provision of a law of a province that creates a deemed trust is, notwithstanding any Act of Canada or of a province or any other law, deemed to have the same effect and scope against any creditor, however secured, as the corresponding federal provision.

86. (1) [Status of Crown claims] In relation to a bankruptcy or proposal, all provable claims, including secured claims, of Her Majesty in right of Canada or a province or of any body under an Act respecting workers' compensation, in this section and in section 87 called a "workers' compensation body", rank as unsecured claims.

...

(3) [Exceptions] Subsection (1) does not affect the operation of

(*a*) subsections 224(1.2) and (1.3) of the *Income Tax Act*;

(*b*) any provision of the *Canada Pension Plan* or of the *Employment Insurance Act* that refers to subsection 224(1.2) of the *Income Tax Act* and provides for the collection of a contribution, as defined in the *Canada Pension Plan*, or an employee's premium, or employer's premium, as defined in the *Employment Insurance Act*, and of any related interest, penalties or other amounts; or

(*c*) any provision of provincial legislation that has a similar purpose to subsection 224(1.2) of the *Income Tax Act*, or that refers to that subsection, to the extent that it provides for the collection of a sum, and of any related interest, penalties or other amounts, where the sum

(i) has been withheld or deducted by a person from a payment to another person and is in respect of a tax similar in nature to the income tax imposed on individuals under the *Income Tax Act*, or
(ii) is of the same nature as a contribution under the *Canada Pension Plan* if the province is a "province providing a comprehensive pension plan" as defined in subsection 3(1) of the *Canada Pension Plan* and the provincial legislation establishes a "provincial pension plan" as defined in that subsection,

and for the purpose of paragraph (*c*), the provision of provincial legislation is, despite any Act of Canada or of a province or any other law, deemed to have the same effect and scope against any creditor, however secured, as subsection 224(1.2) of the *Income Tax Act* in respect of a sum referred to in subparagraph (*c*)(i), or as subsection 23(2) of the *Canada Pension Plan* in respect of a sum referred to in subparagraph (*c*)(ii), and in respect of any related interest, penalties or other amounts.

Solicitors:

Solicitors for the appellant: Fraser Milner Casgrain, Vancouver.

Solicitor for the respondent: Department of Justice, Vancouver.

1 Section 11 was amended, effective September 18, 2009, and now states:

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

2 The amendments did not come into force until September 18, 2009.

TAB 2

Paras 4-5

Case Name:
Earthfirst Canada Inc. (Re)

IN THE MATTER OF the Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36, As Amended AND IN THE MATTER OF a Plan of Compromise or Arrangement of Earthfirst Canada Inc.

[2009] A.J. No. 102

2009 ABQB 78

1 Alta. L.R. (5th) 311

2009 CarswellAlta 142

Docket: 0801 13559

Registry: Calgary

Alberta Court of Queen's Bench
Judicial District of Calgary

B.E.C. Romaine J.

Heard: January 28, 2009.
Judgment: February 3, 2009.

(9 paras.)

Counsel:

Howard A. Gorman and Randal Van de Mosselaer: for EarthFirst Canada Inc.

A. Robert Anderson, Q.C.: for the Monitor Ernst & Young Inc.

Brian P. O'Leary, Q.C., Doug S. Nishimura and Trevor A. Batty: for WestLB AG.

Jeffrey Thom, Q.C.: for the IDL Projects Ltd.

Susan Robinson-Burns: for Synergy Engineering Ltd.

Benjamin La Borie: for Gisborne Industrial Construction Ltd.

V. Philippe (Phil) Lalonde: for Interoute Construction Ltd.

[Editor's note: A corrigendum was released by the Court on July 8, 2009, the corrections have been made to the text and the corrigendum is appended to this document.]

Reasons for Judgment

B.E.C. ROMAINE J.:--

Introduction

1 EarthFirst Canada Inc., a corporation under the protection of an initial order granted under the *Companies' Creditors Arrangement Act*, R.S.C. 1985 c. C-36, as amended, sought to establish a "hardship fund" that would be used to allow it to pay pre-filing obligations owing to certain suppliers and contractors operating in the community near which EarthFirst is developing a wind farm project. I authorized the establishment of this fund, and these are the reasons for my decision.

Background

2 EarthFirst is a publicly-traded developer of renewable wind energy in Canada. It has several projects under development and the most advanced is a wind farm under construction at Dokie Ridge in northeast British Columbia. This project is to be developed in two phases, with the first involving the construction of eight turbines and the second involving a further 40 turbines.

3 EarthFirst's financial difficulties arose primarily from cost overruns on the Dokie Project, combined with difficulties in completing re-financing and/or restructuring initiatives, exacerbated by the general tightening of credit markets.

4 The Dokie Project is located in a remote area of British Columbia close to three first nations' communities. The development has involved local contractors and suppliers whose viability is significantly dependant on this project. Some of these local contractors and suppliers have significant account receivable balances owing from EarthFirst, and some have not received payment from EarthFirst for several months. Certain creditors face immediate financial difficulty, including the inability to fund payroll and purchase critical supplies to continue operations. If some relief is not available, these local operations face bankruptcy.

5 EarthFirst, with the aid and support of the Monitor, proposed the establishment of a fund of $1.5 million to be disbursed in payment of some pre-filing claims of certain local suppliers who are in significant financial difficulty. Payments from the hardship fund are to be at the discretion of EarthFirst's Chief Restructuring Officer and subject to the approval of the Monitor. Such payments are to be considered an interim distribution under a future plan of arrangement and will be reflected in any final distribution to creditors.

6 The amount of the hardship fund was arrived at following discussions among EarthFirst, the Monitor, the local suppliers and contractors. The proposal recognizes the potential domino effect of a failure to fund small, local businesses that are dependant on the continued development of the Dokie Projcct and are essential to future construction activities and the preservation of the project's value, and the dire and harsh consequences in the surrounding communities of the inability of such businesses to meet payroll obligations. The company and the Monitor submit that payments from

the fund would contribute to necessary goodwill in the area and that cooperation and support of the local community is required to ensure that the value of the project is maximized. EarthFirst also notes that, while a CCAA stay of proceedings affects many creditors, the proposed recipients of the hardship fund in this isolated community are particularly vulnerable and at risk.

7 While the nature of payments from the hardship fund is different from the issue that was before Farley, J. in Re Air Canada, [2003] O.J. No. 5319, 2003 CarswellOnt. 5296 (at para. 4), and while EarthFirst is not suggesting that recipients of the fund are "critical suppliers" in the usual sense of the term, it appears to be the case that, as in Air Canada, the potential future benefit to the company of these relatively modest payments of pre-filing debt is considerable and of value to the estate as a whole. The decision to allow the hardship fund thus outweighs the prejudice to other creditors, justifying a departure from the usual rule.

8 Counsel for the Monitor noted that the payments are likely necessary in order to preserve the opportunity to complete the Dokie Project, if that option appears to be the best way to maximize recovery for creditors. It was likely the recognition of this factor that led to little opposition to the application, including from the primary secured creditor. The opposition that was expressed related to a lack of certainty over which unsecured creditors would benefit. While the Monitor would not commit to full public disclosure of the recipients of the hardship fund, which might provoke the precise financial embarrassment and consequential business failure that payments from the fund are intended to prevent, the company and the Monitor were clear that payments would be limited to bare-bone payments "essential to keeping the lights of the recipient company on": *Re Smoky River Coal Ltd.*, [2000] A.J. No. 925, 2000 CarswellAlta 830 at para. 40.

9 I am satisfied that the payment of these case-specific pre-filing debts in a limited amount in order to preserve the value of this CCAA-debtor's primary asset and the option of continuing its development for the benefit of all creditors is fair and reasonable in the circumstances and in accordance with the purpose and objectives of the *Companies' Creditors Arrangement Act.*

B.E.C. ROMAINE J.

* * * * *

Corrigendum
Released: July 8, 2009

The citation Re Earthfirst Canada Inc. (*Companies' Creditors Arrangement Act* 2009 ABQB 78 was corrected to read "Earthfirst Canada Inc. (Re) 2009 ABQB 78".

TAB 3

Para 27

Case Name:

Essar Steel Algoma Inc. (Re)

IN THE MATTER OF the Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36, as amended
AND IN THE MATTER OF a Plan of Compromise or Arrangement of Essar Steel Algoma Inc., Essar Tech Algoma Inc., Algoma Holdings B.V., Essar Steel Algoma (Alberta) ULC, Cannelton Iron Ore Company and Essar Steel Algoma Inc. USA

[2016] O.J. No. 433

2016 ONSC 595

2016 CarswellOnt 1040

263 A.C.W.S. (3d) 301

33 C.B.R. (6th) 313

Court File No.: 15-CV-0011169-00CL

Ontario Superior Court of Justice
Commercial List

F.J.C. Newbould J.

Heard: January 14, 2016.
Judgment: January 25, 2016.

(99 paras.)

Conflict of laws -- Jurisdiction -- International issues -- Determination of -- Real and substantial connection -- Forum conveniens -- Procedure for determining -- Motion by Cleveland-Cliffs Iron Company et al. (Cliffs), objecting to the jurisdiction of the Ontario court with respect to a contract dispute with the applicant, Essar Steel Algoma (Algoma), dismissed -- Cliffs argued that the Ontar-

io court lacked jurisdiction, or that Ontario was not the most convenient forum -- The Ontario court had jurisdiction simpliciter -- The subject matter was connected to Ontario, where the contract was made, and where that Cliffs had been carrying on business -- Cliffs had not established that Ontario was not the most convenient forum -- Companies' Creditors Arrangement Act, s. 11.

Conflict of laws -- Conflicts by legal area -- Contracts -- Jurisdiction with most substantial connection -- Motion by Cleveland-Cliffs Iron Company et al. (Cliffs), objecting to the jurisdiction of the Ontario court with respect to a contract dispute with the applicant, Essar Steel Algoma (Algoma), dismissed -- Cliffs argued that the Ontario court lacked jurisdiction, or that Ontario was not the most convenient forum -- The Ontario court had jurisdiction simpliciter -- The subject matter was connected to Ontario, where the contract was made, and where that Cliffs had been carrying on business -- Cliffs had not established that Ontario was not the most convenient forum -- Companies' Creditors Arrangement Act, s. 11.

Motion by Cleveland-Cliffs Iron Company, Cliffs Mining Company and Northshore Mining Company (Cliffs) objecting to the jurisdiction of the Ontario court with respect to a contract dispute with the applicant Essar Steel Algoma. In 2001 Algoma Steel (Old Algoma) began proceedings under the Companies' Creditors Arrangement Act, and ultimately was restructured into the applicant Algoma. In 2002, Algoma contracted with Cliffs to exclusively source its long-term needs for iron ore pellets. Each year, Algoma was to "nominate" its future years' needs for iron ore and communicate this amount to Cliffs. In 2014, due to a harsh winter and late spring, Algoma did not require all the pellets it nominated in 2013. Algoma claimed that Cliffs negotiated to reduce the 2014 shipments; this was contested by Cliffs. In 2015, Cliffs terminated the contract and brought an action against Algoma in the Ohio court for breach. In November, 2015, Algoma commenced a CCAA proceeding. In December, 2015, Algoma moved for an order declaring that the CCAA proceedings were the proper forum for determining the issues between the parties, declaring the purported termination of the contract was not effective, and directing Cliffs to comply with its obligations under the contract. Cliffs moved to dismiss the Algoma motion on the grounds that Ohio, not Ontario, was the proper forum. Cliffs argued that the contract was governed by Ohio law, and that the relief sought was not available under the CCAA, because Cliffs had terminated the contract before the CCAA proceedings began. Algoma argued that the Ontario court had jurisdiction simpliciter under the CCAA and that, in any event, Ontario was the most convenient forum. Algoma claimed that the contract was made in Ontario, and that Cliffs carried on business in Ontario.

HELD: Application dismissed. The Ontario court had jurisdiction simpliciter over the dispute. Algoma had established a good arguable case for assuming jurisdiction. The subject matter of the dispute was whether the contract had been breached, and by whom. This subject matter was clearly connected to Ontario, where the contract was made in Ontario, and that Cliffs had been carrying on business in Ontario. Further, CCAA proceedings should be harmonized under the single control model. Cliffs was a creditor under the CCAA, by virtue of its Ohio action against Algoma. As to the issue of forum non conveniens, Cliffs had not met the onus of establishing that Ohio was a more convenient forum. Any delay or additional costs would be minimal. There was nothing to indicate that the Ontario court could not deal with the matter as quickly and efficiently as the Ohio court. While the applicable law was that of Ohio, Ontario courts often applied foreign law. There was evidence that an Ontario judgment would be enforced in Ohio.

Statutes, Regulations and Rules Cited:

11 U.S.C., s. 362

BIA,

Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36, s. 11, s. 11.4

Rules, Rule 17.02

U.S. Bankruptcy Code, Chapter 15

Counsel:

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Andrew Kent, Markus Koehnen and Jeffery Levine, for the Moving Parties The Cleveland-Cliffs Iron Company, Cliffs Mining Company and Northshore Mining Company ("Cliffs").

Derrick Tay, Clifton Prophet and Nicholas Kluge, for the Monitor.

L. Joseph Latham and Bradley Whiffen, for the Ad Hoc Committee of Noteholders.

Natalie E. Levine, for the Ad Hoc Committee of senior and junior secured Noteholders.

Sarah-Anne Van Allen, for Wilmington Trust, National Association.

Evan Cobb, for the directors of the applicants.

Andrea Lockhart, for Deutsche Bank.

Ronald Carr, for Her Majesty the Queen in Right of Ontario.

ENDORSEMENT

1 F.J.C. NEWBOULD J.:-- The Cleveland-Cliffs Iron Company, Cliffs Mining Company and Northshore Mining Company (collectively "Cliffs") move to object to the jurisdiction of this Court to hear a motion brought by the applicants (together "Essar Algoma") for relief in connection with a supply contract under which Cliffs supplied Essar Algoma for a number of years with all of its iron ore pellets until Cliffs purported to terminate the contract on October 5, 2015, shortly before this CCAA proceeding was commenced. Cliffs submits in the alternative that Ontario is not the convenient forum in which to determine the dispute between Cliffs and Essar Algoma, and in the further alternative a ruling that a summary procedure for the determination of the dispute is inappropriate.

2 For the reasons that follow, I have concluded that this Court does have jurisdiction over the claim of Essar Algoma against Cliffs and that Cliffs has not established that Ontario is not the convenient forum for the dispute. What the procedure will be to determine the dispute has not yet been settled.

Relevant history

3 In 2001 Algoma Steel Inc. ("Old Algoma") began proceedings under the CCAA and eventually put forward and had approved a plan of compromise and arrangement. As part of its restructur-

ing, Old Algoma divested itself of certain non-core assets, including its interest in a mine in Michigan (the "Tilden Mine") from which Old Algoma sourced its iron ore pellets. In January 2002 Old Algoma sold its interest in the Tilden Mine to Cliffs in consideration for an assumption by Cliffs of certain Old Algoma liabilities and future obligations in respect of the Tilden Mine and Old Algoma and Cliffs entering into a long-term supply agreement effective January 31, 2002 (the "Cliffs Contract"). The Cliffs Contract has been amended a number of times. Essar Algoma succeeded to Old Algoma's rights and obligations under the Cliffs Contract in 2007. The Cliffs Contract is governed by Ohio law.

4 The Cliffs Contract provides that Essar Algoma will source its long-term needs for iron ore pellets exclusively from Cliffs to 2016. As last amended by term sheet in 2013, the Cliffs Contract obliged Essar Algoma to purchase iron ore pellets exclusively from Cliffs until and including 2016. From 2017 to 2024 it obliged Essar Algoma to purchase a portion of its pellets each year from Cliffs. The Cliffs Contract provides that Essar Algoma is obliged in November of each year to provide to Cliffs its good faith estimate of its iron ore requirements (or nomination) for the next year. After Essar Algoma has set its nomination, it has certain rights to modify its nomination to increase or decrease its nomination within a specified range of percentages if it provides written notice to Cliffs by certain deadlines.

5 The Cliffs Contract specifies: (a) a formula for calculating the price of iron ore pellets for the 2013 calendar year; (b) a price for the purchase and sale of iron ore pellets for the 2014 calendar year; (c) a formula for fixing the price of iron ore pellets in 2015 and 2016; and (d) a separate pricing formula for calendar years 2017 to 2024.

6 Cliffs mines the iron ore in Michigan at its mines at the Tilden site and then processes and delivers iron ore pellets by rail to a dock in Michigan known as the Marquette dock or a railway yard in Michigan known as the Partridge rail yard, from which points Essar Algoma takes delivery. Essar Algoma then arranges delivery to Sault Ste. Marie by ship or train.

7 There have been several disputes between Cliffs and Essar Algoma under the Cliffs Contract. The most recent and relevant of such disputes relates to the timing and volume of shipments of iron ore pellets from Cliffs to Essar Algoma beginning in late 2013. At the end of 2013, Essar Algoma advised Cliffs of its nomination for the 2014 calendar year. However, it soon became apparent that the 2013/2014 winter season was one of the coldest and longest in recent history. As a result, the Great Lakes thawed later than usual and the 2014 shipping season was accordingly shortened and Essar Algoma determined that it would not be able to take and use all of the iron ore pellets that it had nominated for 2014. It met with Cliffs to discuss the situation.

8 Whether an agreement was reached to reduce the 2014 shipments became contested, Cliffs saying there was no agreement and Essar Algoma saying there was. The number of tons to be taken by Essar Algoma in 2014 remained a question of debate when Essar Algoma nominated in October 2014 what it would take in 2015 and when it reduced its nomination in July 2015. Cliffs took the position that Essar Algoma had to take the entire tonnage that it had nominated in 2014. Essar Algoma took the position that there was an agreement to reduce the tonnage for 2014.

9 On January 12, 2015, Cliffs filed a complaint in the United States District Court for the Northern District of Ohio (Eastern Division) (the "Ohio Court"). On August 31, 2015, Cliffs amended its complaint. In its Amended Complaint, Cliffs claimed, among other things, damages plus interest and costs for alleged breaches of the Cliffs Contract, including Essar Algoma's alleged

failure to take timely delivery of iron ore pellets in the requisite amounts, and a declaratory judgment that Essar Algoma had materially breached the Cliffs Contract by failing to take delivery of or pay for the full amount of ore that it nominated it would require in 2013, 2014 and 2015 by the end of each calendar. Cliffs did not claim any order or direction permitting it to terminate the Cliffs Contract.

10 In response to the Amended Complaint, Essar Algoma filed an Answer to Plaintiffs' Amended Complaint and Counterclaim on September 14, 2015, wherein it denied Cliffs' allegations and counterclaimed against Cliffs, seeking damages, including a claim for a long-term contract renewal credit payment payable to Essar Algoma pursuant to the Cliffs Contract and a claim for damages for alleged underreporting of moisture levels in pellets delivered by Cliffs.

11 On July 31, 2015, Cliffs filed a motion for partial summary judgment, seeking judgment on its claim that Essar Algoma breached a contractual duty to take its 2014 nomination and to dismiss Essar Algoma's claim for damages related to Cliffs' underreporting of moisture levels to Algoma since 2010. The Cliffs motion was scheduled to be heard on October 6, 2015.

12 On October 5, 2015 Cliffs purported to terminate the Cliffs Contract by letter which stated that as a result of multiple and material breaches and repudiation of the Cliffs Contract by Essar Algoma, Cliffs was treating the Cliffs Contract as terminated effective immediately. The termination came with no advance notice and within days of the next adjustment in price and at a time of year that Essar Algoma has historically begun building up inventory before the winter freeze.

13 On October 7, 2015, Cliffs offered to resume supplying Essar Algoma on a "just in time basis" at a materially higher price than provided for in the Cliffs Contract. The next day Essar Algoma notified Cliffs that the proposed price was commercially unfeasible for it. On October 14, 2015 Cliffs proposed a slightly lower price to Essar Algoma that was still materially higher than the price Essar Algoma had been paying.

14 The Cliffs summary judgment motion in the Ohio Court was heard on October 6, 2015. On the following day, Judge Nugent released his reasons. He granted Cliffs motion in part and denied it in part. He held that there had been no agreement reached in an exchange of emails in April 2014 regarding Essar Algoma's request to decrease its 2014 nomination and that Essar Algoma had thus failed to meet its annual requirements by a margin of at least 500,000 tons. He held however that there were issues as to whether Essar Algoma had given effective notice to reduce a further amount of tons for 2014, whether a force majeure clause gave Essar Algoma a defence to any liability for damages stemming from its alleged failure to meet its annual requirements nomination amounts for 2014, and whether any outstanding damages remained following any allowable off-sets for alleged over-billing caused by Cliffs' use of the 2014 pricing structure in its 2015 sales. In the result he dismissed Cliffs' motion for summary judgment for breach of contract relating to Essar Algoma's 2014 nomination. He also granted Cliffs' motion to dismiss the counterclaim of Essar Algoma with respect to moisture content.

15 On October 6, 2015, one day after Cliffs purported to terminate the Cliffs Contract, Essar Algoma moved in the Ohio Court for a temporary restraining order and a preliminary injunction requiring Cliffs to supply Essar Algoma with iron ore pellets. On October 15, 2015 Essar Algoma filed a notice of withdrawal of its motion. In the notice, Essar Algoma stated that it had obtained supply from another supplier that would provide it with supply for the next several weeks and that this supply removed the need for immediate injunctive relief.

16 A trial for all of the issues in the Ohio litigation was scheduled for December 7, 2015. On October 30, 2015 Essar Algoma filed a motion to adjourn the trial, essentially on the grounds that too much work, particularly documentary production, the conducting of depositions and the production of expert reports, was required for the parties to be ready to start the trial as scheduled.

17 This CCAA proceeding commenced on November 9, 2015 when the Initial Order was made. On November 10, 2015, Essar Algoma commenced ancillary insolvency proceedings under chapter 15 of the U.S. Bankruptcy Code in the U.S. Bankruptcy Court for the District of Delaware. On that day the foreign representative of Essar Algoma sought and obtained, among other things, orders recognizing and enforcing in the United States the orders granted in the CCAA proceeding which was recognized as a foreign main proceeding. The foreign representative of Essar Algoma also filed a complaint for a declaratory judgment against Cliffs and a motion for entry of an order compelling Cliffs to resume supplying iron ore pellets under the Cliffs Contract. Judge Shannon who heard the motions in Delaware was advised by counsel for the foreign representative that this motion was filed as a "placeholder" in the event that the Canadian Court declined to assume jurisdiction to hear Essar Algoma's motion for injunctive relief against Cliffs.

18 On November 11, 2015 Essar Algoma filed with the Ohio Court a notice pursuant to 11 U.S.C. Section 362 that the Ohio action was automatically stayed as to the defendant Essar Algoma. On December 3, 2015 Judge Nugent of the Ohio Court on his own without argument dismissed the case without prejudice. The order stated that upon application, the action may be reinstated, if necessary, when the bankruptcy proceedings have concluded.

19 On December 4, 2015 Cliffs moved in the Ohio Court for an order vacating the without prejudice dismissal of the action and instead placing the case on the suspense docket until the claim is resolved by the bankruptcy court. No decision on that motion has been rendered by Judge Nugent.

Relevant motions in the CCAA proceeding

20 In mid-November 2015 Essar Algoma served a motion seeking a critical supplier order against Cliffs under section 11.4 of the CCAA. The motion was adjourned to December 3, 2015 and then ultimately not proceeded with. The explanation given by Essar Algoma is that following the filing of the motion, it was able to find alternative suppliers for the shorter term. It now has supply of pellets to the end of March. What is at issue on its motion is the right of Essar Algoma under Cliffs Contract to the end of 2024.

21 On December 8, 2015 the applicants served a motion for an order (i) declaring that the CCAA proceedings are the correct forum for the determination of issues relating to the Cliffs Contract; (ii) declaring that the purported termination of the Cliffs Contract was not effective and that it remains in full force and effect and that Cliffs must supply iron ore pellets to Essar Algoma at the price payable under the Cliffs Contract; (iii) directing Cliffs to comply with its obligations under the Cliffs Contract, and (iv) directing Cliffs to pay damages resulting from its purported termination of the Cliffs Contract.

22 On December 23, 2015 Cliffs delivered a notice of motion for an order (i) dismissing or staying the applicants' motion on the grounds that this Court does not have jurisdiction to grant the relief sought by Essar Algoma; (ii) in the alternative, an order staying the applicants' motion on the grounds that Ontario is not a convenient forum for the hearing of the applicants' motion and (iii) in

the further alternative, an order dismissing the applicants' motion without prejudice to the applicants to seek the same relief in the form of an action. It is this motion that was heard on January 14, 2016.

Analysis

23 Cliffs raises a number of issues, including (i) the lack of power to deal with this matter under the CCAA, (ii) a lack of jurisdiction to deal with the claim against Cliffs in Ontario, (iii) Ontario is *forum non conveniens* and (iv) the relief sought is inappropriate for a summary CCAA proceeding.

Jurisdiction under the CCAA

24 Cliffs takes the position that there is no jurisdiction in the CCAA to grant the relief sought by Essar Algoma declaring the termination of the Cliffs Contract to be ineffective and requiring Cliffs to deliver iron ore pellets as required by that contract. It says that the Cliffs Contract was terminated before the CCAA proceedings were commenced and thus the powers of the Court given under the CCAA cannot be used in this case. It relies on *Re SNV Group Ltd.*, 2001 BCSC 1644 in which Justice Pitfield refused to make an order under the CCAA ordering the repayment of money paid before the CCAA proceeding was brought that was said to have been in breach of an agreement that the debtor had with a third party. In that case, Pitfield J. stated:

> The capacity to stay, whether pursuant to section 11 or by virtue of the Court's inherent jurisdiction, applies to prospective proceedings. By its very nature, a proceeding that has been carried to completion cannot be stayed. An order to repay an amount obtained in contravention of a stay granted by the Court would be appropriate, but it is my opinion that the Court cannot rely on the CCAA or its inherent jurisdiction to compel repayment of an amount alleged to have been obtained in reliance upon a contract in a manner that would amount to adjudication of a claim. The CCAA is not intended to give the Court the capacity to undo transactions completed before the effective date of the initial or subsequent orders.

25 Essar Algoma takes the position that Cliffs has misconstrued what Essar Algoma seeks. Rather, it says that it is requesting the Court to invoke its broad and inherent jurisdiction in exercising its territorial jurisdiction, retaining its territorial jurisdiction under the principles of *forum non conveniens*, and determining the appropriate procedures for the determination of the substantive issues in dispute between the parties. It is the consequent modification of Cliffs' procedural rights that Essar Algoma seeks under the CCAA which it says is routinely granted.

26 I do not see the *SNV Group* case as being apposite. Essar Algoma is not asking the Court on its motion to declare the Cliffs Contract as operative because of some provision of the CCAA, which is what the situation was in *SNV Group.*

27 The CCAA is skeletal in nature and does not contain a comprehensive code that lays out all that is permitted or barred. A court under the CCAA has both statutory authority granted under the CCAA and an inherent and equitable jurisdiction when supervising a reorganization. The most appropriate approach is a hierarchical one in which courts rely first on an interpretation of the provisions of the CCAA text before turning to inherent or equitable jurisdiction to anchor measures taken in a CCAA proceeding. See *Ted Leroy Trucking [Century Services] Ltd., Re*, [2010] 3 S.C.R. 379 at paras. 57, 64 and 65.

28 The CCAA provides in section 11 that a court has jurisdiction to make any order "that it considers appropriate in the circumstances"[1]. A CCAA court clearly has the power as per *Century Services* to make the procedural orders of the kind sought by Essar Algoma in this case. See also *Smokey River Coal Ltd., Re*, (1999), 12 C.B.R. (4th) 94 (Alta. C.A.) at paras. 60 and 67 per Hunt J.A. in which he held that a judge has the discretion under the CCAA to permit issues to be decided in another forum (in that case arbitration) but is under no obligation to do so.

29 The "single control" model also favours a CCAA court to deal with the issues between Essar Algoma and Cliffs. In *Eagle River International Ltd., Re* [2001] 3 S.C.R. 978 ["*Sam Lévy*"] Binnie J. referred to and adopted a "single control" model that favours litigation involving an insolvent company to be dealt with in one jurisdiction. He stated:

> **26** The trustees will often (and perhaps increasingly) have to deal with debtors and creditors residing in different parts of the country. They cannot do that efficiently, to borrow the phrase of Idington J. in *Stewart v. LePage* (1916), 53 S.C.R. 337, at p. 345, "if everyone is to be at liberty to interfere and pursue his own notions of his rights of litigation"...
>
> **27** Stewart was, as stated, a winding-up case, but the legislative policy in favour of "single control" applies as well to bankruptcy. There is the same public interest in the expeditious, efficient and economical clean-up of the aftermath of a financial collapse...

30 *Sam Lévy* involved a BIA proceeding. In it, Binnie J. referred to *Stewart*, a winding-up application. I see no reason why the principles in *Sam Lévy* should not be applicable in a CCAA proceeding. In *Century Services* it was noted that the harmonization of insolvency law common to the BIA and CCAA is desirable to the extent possible. The central nature of insolvency and the resolution of issues caused by insolvency are common to both BIA and CCAA proceedings and so too should the underlying principles. See my comments in *Nortel Networks Corp., Re*, (2015), 23 C.B.R. (6th) 264 at para. 24.

31 In this case Cliffs has sued in Ohio for damages claiming material breaches of the Cliffs Contract. It is thus a party that has claimed to be a creditor of Essar Algoma[2]. The single control model requires that its claim against Essar Algoma be dealt with in this CCAA proceeding. Essar Algoma claims in this Court a declaration that the Cliffs Contract has not been legally terminated. Cliffs says that the material breaches by Essar Algoma that it claimed in the Ohio litigation to have occurred permit it to terminate the Cliffs Contract. These issues are completely interwoven and it would make no sense to require Essar Algoma to litigate its claim against Cliffs in the United States[3] when Cliffs' claim against Essar Algoma must be dealt with in this Court in Ontario. The claim of Essar Algoma against Cliffs is an asset of the applicants to be dealt with in this Court.

32 In *Montréal, Maine & Atlantic Canada Co. Re*, 2013 QCCS 5194, a CCAA proceeding arising out of the Lac-Mégantic rail disaster, it was held that a claim by the debtor against its American insurer under a policy governed by Maine law with a forum selection clause in favour of Maine was an asset of the debtor and should be dealt with in Quebec. Dumas J.C.S. referred to the single control model for insolvencies and stated:

> In the present case, we deal with the contrary. It concerns a bankrupt's claim (via the trustee) against its insurance company. Without a shadow of a doubt, this is an asset of the debtor over which the Bankruptcy Court has jurisdiction.[4]

33 For the single control model to apply, the third-party, in this case Cliffs, must not be a stranger to the insolvency proceedings. Cliffs has raised significant damage claims against Essar Algoma and seeks to have those claims remain alive and dealt with in Ohio. Its purported termination of the Cliffs Contract was an important factor that led to Essar Algoma filing for protection under the CCAA. Cliffs is not a stranger to these proceedings.

Jurisdiction *simpliciter*

34 Jurisdiction must be established primarily on the basis of objective factors that connect the legal situation or the subject matter of the litigation with the forum. See *Van Breda v Village Resorts Ltd.*, 2012 SCC 17 at para. 82 per LeBel J. See also para. 79 in which LeBel J. referred to the link between the subject matter of the litigation and the defendant to the forum.

35 To establish jurisdiction *simpliciter*, a plaintiff need only establish that there is a good arguable case for assuming jurisdiction. See *Ontario (Attorney General) v. Rothmans Inc.*, 2013 ONCA 353 at para. 54, 110, 118-19. The phrase a "good arguable case" is not a high threshold and means no more than a "serious question to be tried" or a "genuine issue" or that the case has "some chance of success". See *Tucows.com Co. v. Lojas Renner S.A.*, 2011 ONCA 548 at para. 36.

36 It is for the plaintiff to establish that there is a presumptive connecting factor to the forum. If the plaintiff establishes that, the defendant has the burden of rebuttal and must establish facts which demonstrate that the presumptive connecting factor does not point to any real relationship between the subject matter of the litigation and the forum or points only to a weak relationship between them. See *Van Breda* at paras. 95 and 100.

37 Apart from this test of the connection between the subject matter of the litigation and the forum, traditional tests for basing jurisdiction continue to exist. See *Van Breda* at para. 79 in which LeBel J. stated:

> However, jurisdiction may also be based on traditional grounds, like the defendant's presence in the jurisdiction or consent to submit to the court's jurisdiction, if they are established. The real and substantial connection test does not oust the traditional private international law bases for court jurisdiction.

38 The subject matter of the dispute is whether the Cliffs Contract has been breached and by whom. Cliffs claims Essar Algoma has materially breached provisions of the contract, which if proven, would be grounds to terminate it under Ohio law. Essar Algoma claims that Cliffs had no basis to terminate the contract. Counsel for Cliffs in argument contended that the subject matter of the dispute is a request for specific performance of the contract in Ohio where the ore is mined and delivered to Essar Algoma. I do not agree with that contention. The subject matter of the dispute is the Cliffs Contract and who breached it. While the relief sought by Essar Algoma includes mandatory injunctive relief, that does not make that prayer for relief the subject matter of the dispute. LeBel J. in *Van Breda* stated that it was the legal situation or the subject matter of the litigation that must be connected to the forum. The legal situation is the contention that the Cliffs Contract has been breached and by whom.

39 Rule 17.02 provides a guide to what may be a presumptive factor. LeBel J. stated:

> **83** At this stage, I will briefly discuss certain connections that the courts could use as presumptive connecting factors. Like the Court of Appeal, I will begin with a number of factors drawn from rule 17.02 of the Ontario Rules of Civil Procedure. These factors relate to situations in which service *ex juris* is allowed, and they were not adopted as conflicts rules. Nevertheless, they represent an expression of wisdom and experience drawn from the life of the law. Several of them are based on objective facts that may also indicate when courts can properly assume jurisdiction...Thus they offer guidance for the development of this area of private international law.

40 Rule 17.02 refers to the following in dealing with contract claims:

> **17.02** A party to a proceeding may, without a court order, be served outside Ontario with an originating process or notice of a reference where the proceeding against the party consists of a claim or claims,
>
> (f) in respect of a contract where,
>
> (i) the contract was made in Ontario,...

41 Essar Algoma takes the position that the Cliffs Contract was made in Ontario.

42 The genesis of the Cliffs Contract was the 2001 CCAA proceeding of Old Algoma. As part of that restructuring, Old Algoma sold Cliffs its interest in the Tilden Mine and concurrently entered into the Cliffs Contract. Old Algoma's restructuring, including the Cliffs Contract, required the approval of the CCAA court which was given by order of Chief Justice LeSage of this Court in 2002.

43 There are traditional rules governing where a contract is made. The general rule of contract law is that a contract is made in the location where the offeror receives notification of the offeree's acceptance. See *Eastern Power Ltd. v. Azienda Communale Energia and Ambiente* (1999), 50 B.L.R. (2d) 33 at para. 22 per MacPherson J.A. When acceptance of a contract is transmitted electronically and instantaneously, the contract is usually considered to be made in the jurisdiction where the acceptance is received. See *Trillium Motor World Ltd. v. General Motors of Canada Ltd*, 2014 ONCA 497 at para. 66 per Lauwers J.A. There is an exception to this rule which is the postal acceptance rule that when contracts are to be concluded by post the place of mailing the acceptance is to be treated as the place where the contract was made. See *Eastern Power* at para. 22.

44 There is no provision in the Cliffs Contract or any of its amendments that would give rise to the postal acceptance rule. Thus the traditional rule that a contract is made in the location where the offeror receives notification of the offeree's acceptance would apply. The evidence as to how the original Cliffs Contract or its amendments was concluded is somewhat unclear but unlikely to get better. Mr. Mee of Cliffs in his affidavit stated:

> I no longer have a specific recollection of where the Agreement and each of its amendments was negotiated or signed. My general recollection is that Essar would sign amendments first and that Cliffs would sign them in Cleveland, Ohio after they had been signed by Essar. I have looked back in my calendar for face

> to face meetings with Essar in which I participated since 2002. I found a total of 50 meetings 20 of which were in Canada and 30 of which were in the United States.

45 Neither the original Cliffs Contract nor the amendments provide that the contract or amendments becomes binding when signed without delivery. The original Cliffs Contract states in the first recital that "concurrently with the execution and delivery of this Agreement [the parties] are entering into that Purchase and Sale Agreement in which [Cliffs is acquiring the interest of Algoma in the Tilden Mine Company]" (Underlining added). This language would indicate that the parties expected delivery of the contract to the other to be required for it to be binding.

46 Therefore if the evidence of Mr. Mee of Cliffs is accepted, it would mean that Essar Algoma generally signed the contract and amendments first, then sent them to Cliffs in Cleveland who then signed them and then sent them back to Essar Algoma. That would mean that the contract was formed when Essar Algoma received notice from Cliffs in Ontario of the acceptance of its offer.

47 There is no date of execution on the original Cliffs Contract effective January 31, 2002 or many of the amendments. There are exceptions. The second amendment was signed and dated by Algoma three days after it was signed by Cliffs. The third amendment was signed and dated by Algoma one day before it was signed by Cliffs. Some were signed the same day. The final amendment that extended the term to 2014 that was produced by Cliffs has an execution date by Essar Algoma of June 7, 2013 and no execution by Cliffs.

48 Based on the evidence led by Cliffs, I find that based on the traditional rules governing where a contract is made, Essar Algoma has at least an arguable case, and likely a stronger case than that, that the Cliffs Contract and its amendments generally were contracts made in Ontario.

49 Beyond this, the fact that the original Cliffs Contract became effective only when approved in Ontario by Justice LeSage under the CCAA is a strong indicator that there is a strong and substantial connection of the Cliffs Contract to Ontario. In *Trillium* Lauwers J.A. referred to Professor Waddams and consideration whether the traditional rules in determining the place of contract are appropriate for jurisdictional cases. He stated:

> **70** Should the traditional rules for determining the place of the contract be determinative in applying the fourth PCF [presumptive connecting factor]? This is perhaps an issue for another case, but I agree with the observation of Professor Waddams, at paras. 108-109, that the arbitrary common law rules for determining the place of a contract may not always be apposite in jurisdictional cases. The traditional contract placement rules respond to concerns that are different from those engaged by a jurisdictional analysis. A broader, more contextual analysis is required, which would inevitably engage the same considerations as the real and substantial connection test itself.

50 One may ask why a technical rule as to where an e-mail or fax was sent or received should determine the local of an international piece of litigation. The fact that the Cliffs Contract had its genesis in an Ontario CCAA process and required the approval of the CCAA court in Ontario appears to me to be at least as much a factor in holding that the contract is an Ontario contract as the factor of who sent or received confirmation of the terms of the contract. Often, and in this case,

contract terms or amendments are discussed and agreed orally over the phone or in meetings and then papered afterwards.

51 I conclude and find that Essar Algoma has established a presumptive connecting factor to Ontario for its claim under the Cliffs Contract to Ontario on the basis that the contract was made in Ontario.

52 Essar Algoma also says that Cliffs has operated its business in Ontario and on that basis Ontario has jurisdiction to hear the Essar Algoma request for relief against Cliffs. As stated in para. 79 of *Van Breda*, a defendant's presence in the jurisdiction is a traditional basis for a court having jurisdiction. LeBel J. also stated that carrying on business in a jurisdiction could be an appropriate connecting factor. He stated:

> **87** Carrying on business in the jurisdiction may also be considered an appropriate connecting factor. But considering it to be one may raise more difficult issues. Resolving those issues may require some caution in order to avoid creating what would amount to forms of universal jurisdiction in respect of tort claims arising out of certain categories of business or commercial activity. Active advertising in the jurisdiction or, for example, the fact that a Web site can be accessed from the jurisdiction would not suffice to establish that the defendant is carrying on business there. The notion of carrying on business requires some form of actual, not only virtual, presence in the jurisdiction, such as maintaining an office there or regularly visiting the territory of the particular jurisdiction. But the Court has not been asked in this appeal to decide whether and, if so, when e-trade in the jurisdiction would amount to a presence in the jurisdiction. With these reservations, "carrying on business" within the meaning of rule 17.02(p) may be an appropriate connecting factor. (Underlining added)

53 Rule 17.02(p) provides:

> 17.02 A party to a proceeding may, without a court order, be served outside Ontario with an originating process or notice of a reference where the proceeding against the party consists of a claim or claims,
>
> (p) against a person ordinarily resident or carrying on business in Ontario;

54 The three Cliffs corporations that are a party to the Cliffs Contract are The Cleveland-Cliffs Iron Company, an Ohio corporation with its principal place of business in Cleveland, Cliffs Mining Company, a Delaware corporation with its principal place of business in Cleveland and Northshore Mining Company, a Delaware corporation with its principal palce of business in Silver Bay, Minnesota. They are each wholly-owned subsidiaries of Cliffs Natural Resources Inc. which is an international mining and natural resources company and publicly traded in the United States and until 2014 owned a mining project in the "Ring of Fire" region of Ontario.

55 Under the Cliffs Contract, Cliffs mined the iron ore in Michigan, refined the ore into iron ore concentrate in Michigan, processed the iron ore concentrate into iron ore pellets in Michigan and delivered the iron ore pellets to Essar in Michigan. Cliffs asserts that it has not carried on any

business in Canada and has no presence here. However, the fact that all of the mining and delivery took place in Michigan does not by itself mean that it did not carry on business in Canada.

56 Essar Algoma relies on the fact that during the course of the Cliffs Contract representatives of Cliffs have continuously dealt with Essar Algoma or its predecessor Old Algoma in Sault Ste. Marie in Ontario. Mr. Mee of Cliffs stated that he himself had visited Canada 20 times in connection with the Cliffs Contract. Essar Algoma and its predecessor Old Algoma has been a significant customer of Cliffs. Mr. Marwah of Essar Algoma stated in his affidavit that representatives of Cliffs visit Sault Ste. Marie and representatives of Essar Algoma visit Cleveland in alternating years, during which visits they discuss the status of the Cliffs Contract and ongoing issues relating to their business relationship. Representatives of Cliffs review Essar Algoma's operations and stockpiles of iron ore pellets when they visit Sault Ste. Marie. The most recent visit by Cliffs' personnel was on September 18, 2015 shortly before Cliffs purported to terminate the Cliffs Contract. Prior to that, representatives of Cliffs, including sales, operational, safety and quality personnel visited Essar Algoma in Sault Ste. Marie in October 2014 and August 2013. All of these visits fall within LeBel J.'s statement in *Van Breda* that "regularly visiting the jurisdiction" can constitute carrying on business in the jurisdiction.

57 Cliffs has previously appeared in the Ontario Superior Court of Justice in connection with the Cliffs Contract. In 2010 after Cliffs purported to terminate the Cliffs Contract after a pricing dispute, Essar Algoma applied for and obtained interim injunctive relief. Cliffs appeared on the application and did not oppose the jurisdiction of the Court to hear the relief. Rather it opposed the injunction on the merits. Cliffs complied with the terms of the injunction.

58 I conclude and find that Essar Algoma has established a presumptive connecting factor to Ontario for its claim under the Cliffs Contract to Ontario on the basis that Cliffs has carried on business in Ontario.

59 Cliffs has the burden of rebuttal and must establish facts which demonstrate that the presumptive connecting factors in this case do not point to any real relationship between the subject matter of the litigation and the forum or points only to a weak relationship between them. I do not think Cliffs has met that burden. The relationship between the Cliffs Contract and Ontario is not weak and the visits and meetings by Cliffs personnel in Sault Ste. Marie were not for trivial purposes. They were regular visits to meet with an important customer.

60 Accordingly I find that this Court has jurisdiction over the claim of Essar Algoma against Cliffs.

Forum non conveniens

61 The party raising *forum non conveniens* has the burden of showing that the alternative forum is clearly more appropriate. The use of the word "clearly" should be interpreted as an acknowledgment that the normal state of affairs is that jurisdiction should be exercised once it is properly assumed. The burden is on a party who seeks to depart from this normal state of affairs to show that, in light of the characteristics of the alternative forum, it would be fairer and more efficient to do so and that the plaintiff should be denied the benefits of his or her decision to select a forum that is appropriate under the conflicts rules. The court should not exercise its discretion in favour of a stay solely because it finds, once all relevant concerns and factors are weighed, that comparable forums exist in other provinces or states. See *Van Breda* at paras. 108 and 109.

62 The factors to be considered are numerous and variable. See *Breeden v. Black*, [2012] 1 S.C.R. 666 at para. 23. In *Van Breda*, at para. 5 LeBel J. provided a non-exhaustive list of factors that could play a role. Cliffs relies on a number of these factors as supporting Ohio as the more convenient forum.

63 Before going through these factors, there is an issue as to whether Ohio is the alternative jurisdiction. Essar Algoma says the alternative jurisdiction is Delaware in which the chapter 15 proceedings are taking place. I hesitate to get into that issue and will assume that the alternative forum is the Ohio District Court. That is certainly the view of the expert witness Allan L. Gropper relied on by Cliffs.

(i) The cost of transferring the case or of declining the stay

64 Cliffs says it will result in substantial additional cost and delay to litigate the issues in Ontario. It says that both parties have teams of lawyers in Ohio who are intimately familiar with the case, the relevant documents, witnesses and issues. Cliffs had spent approximately U.S. $1 million on the Ohio litigation before it was dismissed. Essar Algoma has stated that it has a team of 12 attorneys who have spent more than 5,000 hours reviewing documents in the Ohio litigation and that its attorneys have reviewed more than 43,000 documents that Cliffs has produced.

65 Cliffs is concerned that if the matter is litigated in Ontario, both sides will have to educate Ontario lawyers about all of this. At one time, that would have been a major concern. However it is now possible and becoming commonplace in cross-border litigation for American lawyers to appear in an Ontario court, and *vice versa*. The recent Nortel trial was a perfect example of that in which on many days there were 10 to 20 U.S. lawyers in Toronto attending the trial.

66 Cliffs also says that as the Cliffs Contract is governed by Ohio law, there would be the added expense of proving Ohio law. That appears to me to be a minor expense. Essar Algoma has already provided an affidavit of an expert on Ohio law, which Cliffs accepted at least on one point during argument. An affidavit on Ohio contract law could not be relatively expensive in comparison to what has already been expended. Cliffs has also provided a copy of Ohio jury instructions for a civil breach of contract case. The concepts seem virtually identical to Ontario concepts.

67 This factor is essentially a neutral one.

(ii) The impact of a transfer on the conduct of the litigation or on related parallel proceedings

68 Cliffs says having an Ontario court hear the dispute would deprive it of an Ohio judge who is familiar with the issues. Judge Nugent is certainly far more familiar with the issues than an Ontario judge would be. However an Ontario judge, like any other judge hearing a trial or proceeding, is used to coming in cold and picking it up quickly.

69 Judge Nugent has not ruled on whether the Cliffs Contract can be terminated or on whether there were breaches of the contract by Essar Algoma that could be considered material breaches. He merely found on the summary judgment motion, that he dismissed, that there was no legally enforceable agreement between the parties to reduce the 2014 annual nomination to 3.3 million tons and that Essar Algoma therefore failed to meet its annual requirements by a margin of at least 500,000 tons. He did not deal with other defences that Essar Algoma was asserting and stated that he could not conclude that there was a breach entitling Cliffs to damages. Cliffs did not claim any

declaration that it had a right to terminate the Cliffs Contract. Cliffs says that if it can prove that there were material breaches, it would have the right to terminate the Cliffs Contract. These are issues yet to be dealt with.

70 So far as the timing of any trial or other proceeding is concerned, there is no evidence that the Ohio District Court would be in a better position to hear the case sooner than in this Court. Cliffs says it is ready to proceed to trial. Essar Algoma has said it needs more discovery. Both Cliffs and Essar Algoma say they want the matter determined as quickly as possible.

71 Whatever the situation, this Court can accommodate the parties quickly. The situation for Essar Algoma is critical, and the Monitor has stated in its sixth report that in developing and carrying out the SISP, which has tight timelines, Algoma needs certainty concerning the status of the Cliffs Contract and an expedited determination of the rights of the parties is linked to the development of the SISP. Whether those rights can be determined that quickly may be a question mark, but this Court is in at least as good a position as the Ohio court to deal with the issues quickly.

72 I see this factor as neutral or at best perhaps slightly favouring Cliffs.

(iii) The possibility of conflicting judgments

73 I do not see this as an issue. In argument, Essar Algoma acknowledged that it is bound by the finding made by Judge Nugent, to which I have already referred. It could hardly say otherwise, given the principle of *res judicata*. All other issues remain open.

(iv) Location of evidence

74 Cliffs says it will have to call evidence of witnesses in the U.S. regarding its advance planning and why Essar Algoma's actions were a problem to Cliffs. These witnesses would come from Cleveland.

75 However, Essar Algoma's witnesses are from Sault Ste. Marie. There is no evidence how many from each side will need to be called. It is a shorter trip from Cleveland to Toronto than from Sault Ste. Marie to Toronto, whether by air or car. In this day of international contracts, particularly between parties near the Canadian border, I do not see this factor as compelling. It is a neutral factor.

(v) Applicable law

76 Ohio law governs the Cliffs Contract. Cliffs says there is a risk an Ontario court will apply Ohio law incorrectly. I suppose it can be said that an Ohio judge would also apply it incorrectly. This might be a material factor if the law in question was markedly different from Ontario law with concepts unknown to Ontario law. It is clear from the record however that this is not the case. It was acknowledged in argument that Ohio law is not substantially different from Ontario law regarding material breach.

77 Cliffs cites the standard jury instructions in Ohio which defines material breach as follows:

> "Material breach" by plaintiff means a breach that violates a term essential to the purpose of the contract. Mere nominal, trifling, slight or technical departures

from the contract terms are not material breaches so long as they occur in good faith.

78 The jury instructions go on to say that some Ohio courts have utilized the following five factors listed in the Restatement of the Law, (2d) Contracts (1981) in deciding whether a breach is material:

(i) The extent to which the injured party will be deprived of the benefit which he reasonably expected;

(ii) The extent to which the injured party can be adequately compensated for the part of the benefit of which he will be deprived;

(iii) The extent to which the party failing to perform or to offer to perform will suffer forfeiture;

(iv) The likelihood that the party failing to perform or to offer to perform will cure his failure, taking account of all the circumstances including any reasonable assurances;

(v) The extent to which the behaviour of the party failing to perform or to offer to perform comports with standards of good faith and fair dealing.

(vi) The extent to which the behaviour of the party failing to perform or to offer to perform comports with standards of good faith and fair dealing.

79 Cliffs argues that the determination of whether a party failed to comport with standards of good faith and fair dealing is an inherently local reflection of local commercial mores and that the nature of an Ontario court's determination of standards of good faith and fair dealing would inevitably reflect Ontario values and standards rather than Ohio values and standards. I find this argument a stretch. There is no suggestion in the evidence that the values in Cleveland on such an issue would be different from the values in Sault Ste. Marie. In any event, there is nothing in the Ohio law that says that in a case involving parties undertaking a contract in Cleveland and Sault Ste. Marie, it is the Cleveland values rather than the Sault Ste. Marie values that are to be considered.

80 Ontario courts can and do often apply foreign law. In this case I do not consider the fact that the law to be applied is Ohio law much of a factor, if any.

(vi) Recognition and enforcement of an Ontario judgment

81 Cliffs takes the position that there is no jurisdiction in this Court to deal with the Essar Algoma claim against Cliffs because an injunction should not be ordered against a U.S. resident such as Cliffs that could not be enforced.

82 This argument assumes that Cliffs would ignore a decision of an Ontario court. Whether that is so is a question. Cliffs complied with an injunction ordered in Ontario in 2010 after it purported to terminate the Cliffs Contract. Cliffs has requested alternative relief if this Court assumes jurisdiction requiring a statement of claim to be delivered by Essar Algoma, which is some indication that it intends to appear and deal with the issue if it is to be dealt with in Ontario. If it does there could be

no issue of Ontario having jurisdiction that would not be recognized by a U.S. Court as Cliffs would have attorned to the jurisdiction.

83 Cliffs relies on a passage from Sharpe, *Injunctions and Specific Performance*, (loose-leaf ed. November 2015 Toronto: Canada Law Book), para1.1220 that refers to a reluctance of courts to make an order that cannot be enforced, as follows:

> Claims for injunctions against foreign parties present jurisdictional constraints which are not encountered in the case of claims for money judgments. In the case of a money claim, the courts need not limit assumed jurisdiction to cases where enforceability is ensured. Equity, however, acts *in personam* and the effectiveness of an equitable decree depends upon the control which may be exercised over the person of the defendant. If the defendant is physically present, it will be possible to require him or her to do, or permit, acts outside the jurisdiction. The courts have, however, conscientiously avoided making orders which cannot be enforced. The result is that the courts are reluctant to grant injunctions against parties not within the jurisdiction and the practical import of rules permitting service *ex juris* in respect of injunction claims is necessarily limited. Rules of court are typically limited to cases where it is sought to restrain the defendant from doing anything within the jurisdiction. As a practical matter the defendant "who is doing anything within the jurisdiction" will usually be physically present within the jurisdiction to allow ordinary service.

84 I have not been provided with any case however involving cross-border insolvencies in which orders in proceedings under the CCAA cannot be enforced in the United States in chapter 15 proceedings under the U.S. Bankruptcy Code or that deal with evidence as in this case regarding the enforceability of a non-monetary judgment in the United States.

85 Cliffs relies on an opinion of Allan L. Gropper, a highly regarded federal bankruptcy judge for the Southern District of New York from 2000 to 2015. In that opinion, Mr. Gropper stated that United States courts have the greatest respect for the orders and judgments of courts of other nations, particularly those of Canada and judgments for money are ordinarily enforced. He stated that while non-monetary judgments are less regularly enforced, in appropriate circumstances they may be enforced under the common law principle of comity. However, in order for a foreign order or judgment to be enforced, the foreign court must have personal jurisdiction over the defendant.[5]

86 I could hardly quarrel with an opinion on these matters by someone as eminent as Mr. Gropper. However, Mr. Gropper was instructed to assume that Cliffs does not carry on business in Canada, and that assumption is critical to his analysis. That assumption cannot stand in light of the findings that I have made regarding Cliffs carrying on business in Ontario. While Mr. Gropper opines that a U.S. court must scrutinize the basis on which a foreign court asserts jurisdiction over a defendant, and in light of international concepts of jurisdiction to adjudicate, there is no discussion of this issue if the foreign court such as this Court has found that the defendant has carried on business in Ontario under a contract made in Ontario.

87 Essar Algoma relies on an opinion of Ronald A. Brand, a professor of law at the University of Pittsburgh and highly qualified in the area of the recognition of foreign judgments. Professor Brand's opinion is that the fact that a Canadian judgment provides relief in the form of (a) a declaratory order concerning the rights and obligations of parties under and the status of a contract, and/or

(b) specific performance of contractual obligations, would not prevent the recognition and enforcement of that judgment in a court in the United States. Recognition is based on the principle of comity and derives from a U.S. case of *Hilton v. Guyot*, 159 U.S. 113 (1895). Professor Brand says that the principles of comity discussed in that case have made the U.S. one of the most liberal countries in the world in recognizing foreign judgments.

88 Cliffs relies on an opinion of Richard B. McQuade Jr., as U.S. District Court judge from 1986 to 1989 and before that an Ohio Common Pleas Court judge from 1978. Since 1998 he has served as a judge by assignment in both federal and Ohio states courts. His opinion is that an Ohio, Minnesota or Michigan court would not enforce an order of an Ontario court in the nature of specific performance. I must say that I prefer the opinion of Professor Brand for the reasons given by Professor Brand and his impressive credentials on the subject, credentials that I believe to be superior to those of Mr. McQuade.

89 Mr. McQuade states in his opinion that recognition of foreign judgments is based upon general principles of comity. He then goes on to state that the Uniform Foreign-Money Judgments Recognition Act that has been adopted in many states, including Ohio, Michigan and Minnesota, restricts the enforcement of foreign judgments to the recovery of money only. This, however, is not the whole picture. As Professor Brand points out, those state statutes are limited in scope to the recognition of foreign money judgments, but they all include a "savings clause" which specifically acknowledges that judgments other than money judgments may be recognized by applying traditional concepts of comity.

90 Mr. McQuade in his opinion stated that courts that adopted the Uniform Act have consistently denied enforcement to non-monetary judgments, and he cited one case *Sea Search Armada v. Republic of Columbia*, 821 F. Supp. 2d 268 as authority for that proposition. However, as explained by Professor Brand, that decision dealt with a version of the Uniform Foreign Money-Judgments Recognition Act that was in effect in Washington D.C. in 2011 that did not contain the savings clause that other states including Ohio, Michigan and Minnesota had adopted. A Washington D.C. statute was later passed in 2011 after the decision to expressly preserve the D.C. courts' discretion to recognize foreign non-money judgments under principles of comity or otherwise. Curiously, Mr. McQuade in a footnote to his opinion stated that a U.S. court may provide injunctive relief to enforce a foreign judgment it has recognized and that a U.S. court in doing so may take into account a number of factors typically taken into account in ordering injunctive relief. That footnote was contrary to his opinion stated in the body of his affidavit.[6]

91 There is also the issue as to what a U.S. court would consider in recognizing an injunctive order from this Court. In a recent article in 2014 by Judge Martin Glenn of the United States Bankruptcy Court for the Southern District of New York, Judge Glenn commented on the practice of comity between the U.S. and Canada. He stated:

> In *Hilton v. Guyot*, the Supreme Court held that if the foreign forum provides "a full and fair trial abroad before a court of competent jurisdiction, conducting the trial upon regular proceedings, after due citation or voluntary appearance of the defendant, and under a system of jurisprudence likely to secure an impartial administration of justice between the citizens of its own country and those of other countries, and there is nothing to show either prejudice in the court, or in the system of laws under which it is sitting," the judgment should be enforced and

> not "tried afresh." *Hilton*, 159 U.S. at 202-03. "[W]hen the foreign proceeding is in a sister common law jurisdiction with procedures akin to our own, comity should be extended with less hesitation, there being fewer concerns over the procedural safeguards employed in those foreign proceedings." *In re Bd. of Dirs. of Hopewell Int'l. Ins. Ltd., Inc.*, 238 B.R. 25, 66 (Bankr. S.D.N.Y. 1999), *aff'd*, 238 B.R. 699 (S.D.N.Y. 2002) (internal quotation marks and citations omitted). For example, the U.S. and Canada share the same common law traditions and fundamental principles of law. Canadian courts afford creditors a full and fair opportunity to be heard in a manner consistent with standards of U.S. due process. U.S. federal courts have repeatedly granted comity to Canadian proceedings.

92 Judge Glenn also referred to a reluctance to second guess a decision of a foreign court in taking jurisdiction if the defendant appeared in the foreign court to challenge its jurisdiction and failed to prevail. He stated:

> In deciding whether to enforce a foreign judgment, a court in the United States may scrutinize the basis for the assertion of jurisdiction by the foreign court. *See RESTATEMENT (THIRD) OF FOREIGN RELATIONS LAW* s. 482 cmt. c. ("*Lack of jurisdiction over defendant.* The most common ground for refusal to recognize or enforce a foreign judgment is lack of jurisdiction to adjudicate in respect of the judgment debtor. If the rendering court did not have jurisdiction over the defendant under the laws of its own state, the judgment is void and will not be recognized or enforced in any other state. Even if the rendering court had jurisdiction under the laws of its own state, a court in the United States asked to recognize a foreign judgment should scrutinize the basis for asserting jurisdiction in the light of international concepts of jurisdiction to adjudicate."). Whether jurisdiction was challenged in the foreign court is relevant but not necessarily decisive in deciding whether to enforce a foreign judgment, although a renewed challenge to jurisdiction is generally precluded. *Id.* ("If the defendant appeared in the foreign court to challenge the jurisdiction of the court and failed to prevail, it is not clear whether such determination will be considered *res judicata* by a court in the United States asked to recognize the resulting judgment."); *Id.* at s. 482 rn.3 ("[i]f the defendant challenged the jurisdiction of the rendering court in the first action and the challenge was unsuccessful or was not carried to conclusion . . . a renewed challenge to jurisdiction of the rendering court is generally precluded").

93 I recognize the reluctance expressed by Justice Sharpe in his text that our courts avoid making orders that cannot be enforced. However on the basis of the evidence before me, Cliffs has not established that an order made in this Court requiring Cliffs to perform the Cliffs Contract would not be enforced in those states where Cliffs has assets. I accept that there may be some risk as opinions are only opinions, but the risk on the basis of the evidence before me does not rise to the level that would render Ontario a *forum non conveniens* in this case.

(vii) Conclusion on forum non conveniens

94 Cliffs has not met its burden of showing that the alternative forum, in this case Ohio, is clearly more appropriate.

Is the relief inappropriate for a summary proceeding?

95 Cliffs takes the position that the relief Essar Algoma seeks is inappropriate for a summary proceeding and that there is no basis for Essar Algoma claiming urgency. This is not raised as a *forum non conveniens* point. It requests an order that Essar Algoma must deliver a statement of claim.

96 So far as the urgency is concerned, the Monitor has made clear that the issue needs to be quickly decided. I cannot find that Essar Algoma has purposely delayed the issue. In any event, Cliffs in argument took the position that it wanted the issue decided quickly.

97 Regarding the kind of hearing required to deal with the dispute, there is nothing in the record before me to say that Essar Algoma is demanding some summary procedure that would impair Cliffs' procedural rights in any material way. In argument, counsel for Essar Algoma said that what procedure will be adopted is for this Court on another day and that the parties will have to work together to come up with an appropriate procedure. It could be a full trial or less.

98 I would not at this stage order that Essar Algoma deliver a statement of claim. What the form of the process will take is yet to be decided. I agree with Cliffs that the procedural rights of the parties should be protected as much as possible as the circumstances will permit. Those circumstances, of course, include the fact that Essar Algoma filed under the CCAA shortly after Cliffs purported to terminate the Cliffs Contract and that the issue needs to be dealt with quickly for the sake of both parties. As well, the principles laid out in *Hryniak v. Mauldin*, 2014 SCC 7 and the need to be mindful of the most proportionate procedure for a case will need to be considered.

Conclusion

99 The motion of Cliffs is dismissed.

F.J.C. NEWBOULD J.

1 The power in section 11 is "subject to the restrictions set out in this Act." Cliffs argued that an inference should be drawn that because Essar Algoma withdrew its critical supplier motion, an inference should be drawn that it did so because it could not comply with the critical supplier tests in section 11(4). Thus the failure to be able to comply with section 11(4) should be read as a restriction in the Act preventing the use of section 11 by the applicants. I decline to make such an inference and in any event do not think a failure to fall into the language of section 11(4) which provides that a court *may* make an order can be read to be a restriction under section 11. It is commonplace in CCAA proceedings to make orders requiring supply without invoking section 11(4).

2 At the request of Cliffs, the claims procedure order signed on January 14, 2016 in this CCAA proceeding by agreement did not cover Cliffs' claims and the procedure to govern those claims is to await the determination of this motion.

3 It would be up to the Delaware Bankruptcy Court to determine if the claim should proceed in that Court or in the Ohio District Court.

4 Although Justice Dumas referred to a trustee and the Bankruptcy Court, the case was a CCAA case and the MME was not a bankrupt.

5 Mr. Gropper went on in his opinion to give his view ("it is submitted...") that a U.S. Court would not find that Cliffs has submitted to the jurisdiction of the Canadian courts. I have serious doubts as to whether an expert in foreign law should go beyond stating what the foreign law is and give an opinion on what the foreign court would do in a particular case. See my comments in *Nortel Networks Corp. (Re)* (2014), 20 C.B.R. (6th) 171 at paras. 103-104. In any event, his opinion was based on the assumption that Cliffs did not carry on business in Canada.

6 Mr. Gropper also referred, in a footnote to his statement that in appropriate circumstances a non-monetary may be enforced under the common law principle of comity, to the *Sea Search* case as authority that where the Uniform Act has been adopted, courts have consistently denied enforcement to non-monetary judgments. However Professor Brand's analysis is a complete answer to that case. I would note that while Mr. Gropper has extremely impressive credentials as a bankruptcy expert, his *curriculum vitae* does not list experience in dealing with state courts or the enforcement of foreign judgments under state legislation.

TAB 4

Para 24

Case Name:

Marine Drive Properties Ltd. (Re)

**IN THE MATTER OF Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36, as Amended
AND IN THE MATTER OF the Business Corporations Act, S.B.C. 2002, c. 57
AND IN THE MATTER OF Marine Drive Properties Ltd., Wyndansea Hotel Inc. and 0707624 B.C. Ltd.**

[2009] B.C.J. No. 1600

2009 BCSC 1083

56 C.B.R. (5th) 65

2009 CarswellBC 2105

180 A.C.W.S. (3d) 207

Docket: S090306

Registry: Vancouver

British Columbia Supreme Court
Vancouver, British Columbia

G.B. Butler J.

Heard: June 15, 2009.
Oral judgment: June 24, 2009.

(35 paras.)

Bankruptcy and insolvency law -- Companies' Creditors Arrangement Act matters -- Compromises and arrangements -- Costs of administration -- Upon application in Companies' Creditors Arrangement Act proceedings to determine the priority of a $500,000 administrative charge created on Jan. 15, 2009 but set aside on Feb. 10, 2009, the charge was to continue to secure the unpaid fees of the monitor and its counsel only -- The only possible remedy for a failure to give notice of the initial application was that the priority for the petitioning Marine Drive's legal counsel was to

be set aside -- It would be inequitable to retain that priority when it never should have been granted.

Application by multiple parties, collectively "Bancorp," to determine the priority of the $500,000 administrative charge created by the Jan. 15, 2009 initial order made in these proceedings under the Companies' Creditors Arrangement Act. The order was made following an ex parte hearing brought by the petitioners, Marine Drive Properties Ltd., Wyndansea Hotel Inc. and 0707624 B.C. Ltd. (collectively "Marine Drive"). The initial order provided for a stay of all proceedings, appointed a monitor, and created the administrative charge, which was granted super-priority over the existing mortgage security interests registered against marine Drive's real property. The initial order was set aside on Feb. 10, 2009, but not on a nunc pro tunc basis. The outstanding amounts claimed under the charge by Marine Drive, the monitor and counsel totalled $152,274. Bancorp argued there was a good possibility there would be a shortfall once all Marine Drive's assets were sold. The issues to be determined were: (1) was it too late for Bancorp and the other secured creditors to challenge the priority of the administrative charge; and (2) did the charge continue to secure the unpaid fees of the petitioners' counsel, the monitor and its counsel.

HELD: The charge continued to secure the unpaid fees of the monitor only, and its counsel. (1) It was not too late to consider Bancorp's application. The power of a judge to reconsider a ruling before the order was drawn up and entered was undoubted. As the order had not been entered, it was not too late for the court to exercise its discretion to reconsider the ruling in question, provided that it was done judicially. There was no impediment to reconsidering the effect of the ruling that the application ought not to have been brought on an ex parte basis. To decline to do so would leave an important issue unresolved. (2) In the circumstances, the only possible remedy for a failure to give notice was that the priority of the administrative charge for Marine Drive's legal counsel must be set aside. It would be inequitable for that priority to be retained when the circumstances were such that the priority never should have been granted. It would be anomalous for the unsuccessful party, marine Drive, to have all of its legal costs paid in circumstances where there was a possibility that the successful parties would not be able to recover their costs. With respect to the monitor, it did not defend the initial order, but simply performed the tasks assigned to it by the court. In the circumstances, the priority of the administrative charge for it and its counsel ought to be confirmed. The decision would ensure that insolvent companies and their counsel carefully considered whether the circumstances were such that the application for the initial order ought to be made on an ex parte basis. The parties advised they were in agreement as to how the administrative charge would be allocated among the assets of Marine Drive.

Statutes, Regulations and Rules Cited:

Business Corporations Act, SBC 2002, CHAPTER 57,

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

Counsel:

Counsel for Marine Drive Properties Ltd.: O. James.

Counsel for Counsel for Bancorp Financial Services Inc., Bancorp Balanced Mortgage Fund Ltd., Cooper Pacific Mortgage Investment Corporation and Liberty Holdings Excell Corp.: J. McLean.

Counsel for the Monitor: S. Dvorak.

Counsel for CareVest Capital Inc.: P. Vaartnou.

Oral Reasons for Judgment

1 **G.B. BUTLER J.** (orally, via telephone):-- This is an application brought by Bancorp Financial Services Inc., Bancorp Balanced Mortgage Fund Ltd., Cooper Pacific Mortgage Investment Corporation and Liberty Holdings Excell Corp. (collectively "Bancorp") to determine the priority, if any, of the $500,000 administrative charge (the "Administrative Charge") created by the initial order made in these proceedings on January 15, 2009 (the "Initial Order"). The Initial Order was granted pursuant to the ***Companies' Creditors Arrangement Act***, R.S.C. 1985, c. C-36 ["***CCAA***"] following an *ex parte* hearing brought by the petitioners, Marine Drive Properties Ltd., Wyndansea Hotel Inc. and 0707624 B.C. Ltd. (collectively "Marine Drive").

2 The Initial Order was generally in the form of the "Model Initial Order" used in British Columbia pursuant to the Practice Direction of November 9, 2006. It provided for a stay of all proceedings. It appointed Ernst & Young Inc. as monitor (the "Monitor") and created the Administrative Charge. Pursuant to the terms of the Initial Order, the Administrative Charge was granted super-priority. In other words, it was given priority over the existing mortgage security interests registered against Marine Drive's real property.

3 On January 29 and 30, 2009, I heard Bancorp's application to set aside the Initial Order. On February 10, 2009, I set aside the Initial Order (the "Second Order") but declined to do so on a *nunc pro tunc* basis. In arriving at that decision I found:

(a) The application for the Initial Order should not have been brought without notice to the respondents; and

(b) There were no circumstances that made it appropriate to continue the Initial Order.

4 My Reasons for Judgment in relation to the Second Order can be found at 2009 BCSC 145, 52 C.B.R. (5th) 47 (the "Reasons"). The facts are set out in those Reasons in some detail, so I do not need to repeat them here. The Second Order has not been entered given the dispute between the parties regarding the consequences that flow from my findings.

5 Counsel for Marine Drive and the Monitor took retainers from their clients ($15,000 and $10,000 respectively) which have been applied against their accounts. The outstanding amounts claimed under the Administrative Charge by counsel for Marine Drive, the Monitor and its counsel total $152,273.57. It was argued by Bancorp that there is a good possibility there will be a shortfall once all of Marine Drive's assets are sold. As a result, Bancorp, and the other secured creditors, may not recover the full amounts owing to them. Of course, if the Administrative Charge has priority over the secured lenders' mortgage charges, the amount of any shortfall will be increased.

6 The issues that need to be determined on this application are:

1. As the Initial Order was not set aside *nunc pro tunc*, is it too late for Bancorp and the other secured creditors to challenge the priority of the Administrative Charge?
2. Does the Administrative Charge continue to secure the unpaid fees of the petitioners' counsel, the Monitor and its counsel?

Issue 1: As the Initial Order was not set aside *nunc pro tunc*, is it too late for Bancorp and the other secured creditors to challenge the priority of the Administrative Charge?

7 In my Reasons I made the following comments that are relevant to this issue:

> 16 There are numerous contentious issues raised by these applications. The question of whether full and frank disclosure was made would require careful examination of the materials relied upon at the hearing on January 15, 2009, and careful review of the statements made by counsel. I do have serious concerns regarding the disclosure made at the time of the initial application. However, given the conclusions I have reached on the other issues, I have not undertaken that close review. ...
>
> ...
>
> 27 This application should not have been brought without notice to the respondents. Initial applications in ***CCAA*** proceedings should not be brought without notice merely because it is an application under that Act. The material before the court must be sufficient to indicate an emergent situation. Counsel must be careful to fairly present the situation to the court if the application is made on an *ex parte* basis.
>
> 28 As I have determined that there is no basis for an order under the ***CCAA***, I do not have to decide what remedy flows from the failure to give notice.
>
> ...
>
> 47 There are no circumstances present that make it appropriate to continue the Order. In addition, the Order should not have been sought on an *ex parte* basis. The Order will accordingly be set aside. As I have not found a failure to make full and frank disclosure on the part of the Petitioners, I decline to make the order effective *nunc pro tunc*.

8 Marine Drive and the Monitor argue that on two separate occasions, I made orders that gave the Administrative Charge priority over the registered mortgages of Bancorp and the other mortgagees. Most importantly, when I made the Second Order, I did so after hearing Bancorp's argument that the Initial Order should be set aside *nunc pro tunc*. I specifically declined to do that. The Second Order has not been appealed. Accordingly, Marine Drive and the Monitor say it is now too late for Bancorp and the other creditors to bring this application. They say that the present application is effectively "an appeal by stealth". Further they argue that Bancorp should not be permitted to set aside the Administrative Charge indirectly, when it failed to achieve that result directly.

9 I reject Marine Drive's submission that it is now too late to consider Bancorp's application. The power of a judge to reconsider a ruling before the order is drawn up and entered is undoubted: ***Clayton v. British American Securities Ltd.***, [1935] 1 D.L.R. 432, 49 B.C.R. 28 (C.A.) and ***Harrison v. Harrison***, 2007 BCCA 120, 64 B.C.L.R. (4th) 318. As the order has not been entered in this case, it is not too late for me to exercise my discretion to reconsider the ruling in question, provided that is done judicially.

10 Here, both parties have referred to authorities that are directly relevant to the issue raised on the present application. These authorities were not referred to at the time of the application for the Second Order. Further, it is evident from paragraph 28 of my Reasons that I specifically did not consider whether any remedy flowed from my finding that the application should not have been brought *ex parte*. In addition, the decision that the order should not be set aside *nunc pro tunc* was made solely because I did not make a finding that Marine Drive failed to make full and frank disclosure.

11 In these circumstances, there is no impediment to reconsidering the effect of the ruling that the application should not have been brought on an *ex parte* basis. Indeed, to decline to do so would leave an important issue unresolved. Whether any remedy flows from my finding that notice should have been given is an issue that should have been adjudicated upon at the time of the application for the Second Order.

Issue 2. Does the Administrative Charge continue to secure the unpaid fees of the petitioners' counsel, the Monitor and its counsel?

The Position of Bancorp

12 Bancorp argues that there is a fundamental rule that a party not be bound by an order granted on an application in respect of which it had no notice: ***Re Lochson Holdings Ltd. and Eaton Mechanical Inc.*** (1984), 10 D.L.R. (4th) 630, (*sub nom.* ***Lochson Holdings Ltd. v. Eaton Mechanical Inc.***) 55 B.C.L.R. 54 (C.A.) [***Lochson***]. Bancorp says that in the present case none of the secured creditors had notice of the application as a result of which it would be unfair and contrary to the rules of natural justice to permit the Administrative Charge to be granted priority over the mortgages. It also says that it is irrelevant whether the Initial Order was set aside *nunc pro tunc*. Bancorp says that so long as the Initial Order was set aside it can have no effect.

13 Bancorp also says it would be unjust to allow Marine Drive's counsel to recover 100% of its costs when it was the unsuccessful party. Almost half of those legal costs were incurred before the Initial Order was made and so there was no reliance on the Initial Order in respect of those costs. With regard to the balance of the costs, they were incurred in an unsuccessful effort to defend the Initial Order. Further, Bancorp says that it immediately put both the Monitor and Marine Drive's counsel on notice that it was applying to set aside the Initial Order, and that it would be prudent for the Monitor and counsel to keep costs to a minimum if they did not have retainers.

14 Bancorp's main argument is that if notice had been given, the Administrative Charge would never have been in place. It says there is no doubt that I would have arrived at the conclusion that Marine Drive could not meet the test under s. 11 of the ***CCAA***, as there were no circumstances present that made it appropriate to order a stay of proceedings.

The Position of Marine Drive and the Monitor

15 Marine Drive and the Monitor argue that in ***CCAA*** proceedings it is common for an initial order to provide for super-priority for an administrative charge. They note that the Model Initial Order in British Columbia includes such provisions. It is often the only way that a company can obtain the professional advisors needed to allow it to restructure. The ability of the court to make such an order is thus essential for the legislative scheme to be put into effect.

16 Marine Drive and the Monitor say that most of the authorities relied upon by Bancorp are rulings in receivership situations. They argue that there is a significant difference between a receivership and a ***CCAA*** restructuring. In the former, the property in question has to be safeguarded by the court, while in the latter situation it is the survival of the company being reorganized that is the focus of the court's concern. They note that in ***United Used Auto & Truck Parts Ltd. v. Aziz***, 2000 BCCA 146, (*sub nom.* ***United Used Auto & Truck Parts Ltd., Re***) 73 B.C.L.R. (3d) 236 [***United***], the court stated at para. 22:

> ... [T]he receivers' jurisdiction and the monitor's jurisdiction are analogous to the extent that they are both rooted in equity but they diverge to the extent that the monitors' jurisdiction serves a broader statutory objective under the ***CCAA***. In my opinion the jurisdiction under the ***CCAA*** cannot be restricted to the ***Kowal*** exceptions.

17 What the Court referred to in ***United*** as the "***Kowal*** exceptions", from ***Robert F. Kowal Investments Ltd. v. Deeder Electric Ltd.*** (1975), 21 C.B.R. (N.S.) 201 (Ont. C.A.) are the same as those set out in the ***Lochson*** case relied upon by Bancorp. The exceptions are:

(1) where the receiver has been appointed at the request of or with the consent or approval of the security holders;
(2) where the receiver has been appointed to preserve and realize assets for the benefit of all interested parties, including secured creditors, and properly incurs charges and expenses in so doing; and
(3) where the receiver has expended money for the necessary preservation and improvement of the property.

18 Marine Drive and the Monitor say that as a result of the decision in ***United***, the equitable jurisdiction of the court cannot be restricted in ***CCAA*** proceedings.

19 Marine Drive says that in this case it had insufficient cash flow to pay for the legal and professional advice required. In these circumstances, it argues that it is appropriate for the Administrative Charge to be granted super-priority.

20 In addition to these arguments, the Monitor and its counsel also argue that the priority of the Administrative Charge for the fees payable to them should be considered separately from the fees for Marine Drive's legal counsel. The Monitor was appointed by the court under the Initial Order and was required to perform its obligations and duties as an officer of the court. The Monitor required the assistance of counsel to carry out those duties. Once the Initial Order was made, the Monitor fulfilled its obligations and duties and should be paid for doing so. It notes that it did not defend the Initial Order but provided a balanced report to the court and the creditors. In these circumstances, the Monitor argues that it would be unfair to deny the priority granted by the Administrative Charge.

21 The leading authority in this area is ***Re Hunters Trailer & Marine Ltd.***, 2001 ABQB 546, 295 A.R. 113 [***Hunters***]. In that case, the initial order was granted *ex parte*. The stay was extended for an additional 30 days after the initial order. After the stay had been in place for two months, the secured lenders successfully applied to set aside the initial order and the stay. The secured creditors then challenged the priority of the administrative charge.

22 Chief Justice Wachowich reviewed the existing law regarding the jurisdiction of the court to grant super-priority for the administrative charge, including the decision of our Court of Appeal in ***United***. He stated as follows at para. 32:

> Having reviewed the jurisprudence on this issue, I am satisfied that the Court has the inherent or equitable jurisdiction to grant a super-priority for DIP financing and administrative charges, including the fees and disbursements of the professional advisors who guide a debtor company through the ***CCAA*** process. Hunters brought its initial ***CCAA*** application *ex parte* because it was insolvent and there was a threat of seizure by some of its major floor planners. If super-priority cannot be granted without the consent of secured creditors, the protection of the ***CCAA*** effectively would be denied a debtor company in many cases.

23 The secured creditors argued in ***Hunters*** that the fees and disbursements of professional advisors should only be confirmed where a successful arrangement is achieved. This argument was rejected by Wachowich C.J., who granted priority to the fees charged by the professional advisors for the work done prior to the initial order, as well as after that order was granted. This included the work done to defend the initial order. He stated as follows at paras. 34-36:

> It is preferable that priority for administrative costs and DIP financing be dealt with on notice to all interested parties. However, if the circumstances warrant, priority may be granted on the initial application, but on a limited basis only until the matter is considered on notice to those affected by the order. That is precisely what occurred in this case. Hunters brought an application on November 8th for an extension of the stay of proceedings. This application was made on notice to the secured creditors. If they had wanted to challenge the initial Order before that date, they could have done so on two days' notice.
>
> In my view, the services of both Reynolds and Gillespie were essential if Hunters was to have any possibility of arriving at an arrangement with its creditors which would allow Hunters to carry on its business. The priority assigned to the Administrative Charge in my Order of October 11, 2000 was granted as there was no other reasonable alternative to assure that the services of Reynolds and Gillespie would be available to Hunters. The Administrative Charge met the debtor company's urgent needs during the sorting-out period.
>
> I do not accept the argument advanced by the objecting creditors that it is only in the case of a successful arrangement under the CCAA that priority for the fees and disbursements of professional advisors should be confirmed. Professional advisors acting for a debtor company must act in a reasonable manner, but they

> are not guarantors of the success of restructuring. Nor is it unreasonable for the debtor company to defend a creditor's challenge to the initial CCAA order.

24 There is no doubt that the equitable jurisdiction of the court on an initial application in a ***CCAA*** proceeding is broad. This includes the jurisdiction to grant super-priority to administrative charges. This can be done in appropriate circumstances where the applicant has no reasonable alternative to ensure that it will have the services of the professional advisors needed to attempt to put an arrangement in place.

25 I agree with the reasoning and the conclusions arrived at in ***Hunters***. The priority for fees of professional advisors may be confirmed, even if a successful arrangement is not achieved through the ***CCAA*** process. Further, the charges that are incurred before the application for an initial order and the charges incurred to defend an initial order may be confirmed under the administrative charge even where no arrangement is made and the stay is ultimately set aside. If this were not the case, the ability of insolvent companies to take advantage of the ***CCAA*** would be limited. Only those companies which have sufficient cash flow to pay for or provide substantial retainers to their advisors would be in a position to apply for protection under the ***CCAA***.

26 I also agree that all of the circumstances must be examined to determine if it is appropriate to confirm the priority for the administrative charges. If the application for the initial order is made with notice to the creditors, then all of the circumstances that are likely to be relevant to this issue will be before the court. However, when the application for the initial order is made without notice, the court will have to consider, as it did in ***Hunters***, whether it was appropriate for the initial order application to have been made without notice.

27 In ***Hunters***, the court found that the application was brought *ex parte* for good reason: the company was insolvent and there was a threat of seizure by some of its major floor planners. If it had given notice it would have lost the possibility of arriving at an arrangement under the ***CCAA*** that would allow it to carry on business. The administrative charge was essential if the company was to have any possibility of arriving at an arrangement with its creditors.

28 In the present case, I must consider the circumstances to determine if the priority should be confirmed. Consideration of the circumstances will have to take into account the fact that the Monitor and its counsel are in a different position than Marine Drive and its counsel.

29 The situation in this case is very different from ***Hunters***. I found that there was no urgency to the application for the Initial Order and no need for it to have been brought on an *ex parte* basis. There was no imminent risk that steps would be taken by the secured creditors that would have the effect of putting Marine Drive out of business. In this case, Bancorp and the other secured creditors immediately applied to set aside the Initial Order and challenge the Administrative Charge.

30 I also found that there were no circumstances that made it appropriate to continue the Initial Order. As Bancorp has argued, given the facts in this case, that finding was equivalent to a conclusion that there were no circumstances present that supported the making of an order under s. 11 of the ***CCAA***. In other words, if notice had been given, the Initial Order would not have been made.

31 In these circumstances, I conclude that the only possible remedy for a failure to give notice is that the priority of the Administrative Charge for Marine Drive's legal counsel must be set aside. It would be inequitable for that priority to be retained when the circumstances are such that the priority never should have been granted. As Bancorp argued, it would be anomalous for the unsuc-

cessful party, Marine Drive, to have all of its legal costs paid in circumstances where there is a possibility that the successful parties will not be able to recover their costs. In summary, the circumstances that were present in ***Hunters*** are simply not present in this case.

32 The situation of the Monitor must be considered separately. The Monitor was appointed by the Initial Order and performed its work with the understanding that the professional fees charged for that work would be paid in accordance with the terms of the Initial Order. The report prepared by the Monitor was balanced and fair and provided useful information for the Court. As the Monitor argued, it did not defend the Initial Order; it simply performed the tasks assigned to it by the Court. In these circumstances, the priority of the Administrative Charge for the Monitor and its counsel should be confirmed.

33 The goal of the ***CCAA*** is to maintain the status quo of an insolvent company while it attempts to bring its creditors onside for a plan of arrangement. This is done so that the company can stay in business for the benefit of the company, its creditors and other stakeholders. This goal would be frustrated if monitors and their counsel found that they could not rely upon the security provided to them by the administrative charge in an initial order. The result of such a decision would be that insolvent companies would be unable to find professional advisors willing to take on the necessary work in circumstances where the application for the initial order had to be made on an *ex parte* basis.

34 The same consideration does not apply to the insolvent company and its solicitor. It is the company that has the obligation to determine whether it is appropriate in the circumstances for an order to be sought without notice to its creditors. Neither the company nor its counsel should receive the benefit of the Administrative Charge priority where there is no urgency or other reason for proceeding *ex parte*. This decision will not have the effect of interfering with the aim of the ***CCAA***. Rather, it will ensure that insolvent companies and their counsel carefully consider whether the circumstances are such that the application for the initial order should be made on an *ex parte* basis.

35 At the conclusion of the hearing of this application, counsel advised that they were in agreement as to how the Administrative Charge would be allocated among the assets of Marine Drive. Accordingly, I will leave the parties to work out the terms of the order regarding allocation of the Administrative Charge for the Monitor's fees, and the Monitor's counsel's fees, as well as the mechanics of collection of that charge. I will of course hear any application to settle issues that cannot be resolved.

G.B. BUTLER J.

cp/e/qlrds/qlmxb/qlaxw/qlaxr/qlana

TAB 5

Para 88

Case Name:

Nortel Networks Corp. (Re)

RE: IN THE MATTER OF the Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36, as Amended
AND IN THE MATTER OF a Plan of Compromise or Arrangement of 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

[2009] O.J. No. 2558

55 C.B.R. (5th) 68

75 C.C.P.B. 233

2009 CarswellOnt 3583

178 A.C.W.S. (3d) 305

2009 CanLII 31600

Court File No. 09-CL-7950

Ontario Superior Court of Justice
Commercial List

G.B. Morawetz J.

Heard: April 21, 2009.
Judgment: June 18, 2009.

(89 paras.)

Bankruptcy and insolvency law -- Creditors and claims -- Claims -- Priorities -- Unsecured claims -- Motions by unionized and non-unionized former employees for orders requiring Nortel to restore payments to the employees dismissed -- Nortel was granted protection under the Company's Credi-

tors Arrangement Act and was under financial pressure -- The employee claims were unsecured claims and therefore did not have any statutory priority -- Furthermore, the claims were based mostly on services that were provided pre-filing -- There was no reason to treat the unionized or non-unionized employees any differently than other unsecured creditors -- Nortel's resources were to be used to attempt restructuring -- Companies' Creditors Arrangement Act, s. 11.

Bankruptcy and insolvency law -- Companies' Creditors Arrangement Act (CCAA) matters -- Motions by unionized and non-unionized former employees for orders requiring Nortel to restore payments to the employees dismissed -- Nortel was granted protection under the Company's Creditors Arrangement Act and was under financial pressure -- The employee claims were unsecured claims and therefore did not have any statutory priority -- Furthermore, the claims were based mostly on services that were provided pre-filing -- There was no reason to treat the unionized or non-unionized employees any differently than other unsecured creditors -- Nortel's resources were to be used to attempt restructuring -- Companies' Creditors Arrangement Act, s. 11.

Motion by the union for an order requiring Nortel to recommence payments that was obligated to make under the collective agreement. Motion by former employees for an order requiring Nortel to pay termination pay, severance pay and other benefits. Nortel was granted protection under the Company's Creditors Arrangement Act in January 2009. At that time, Nortel ceased making payments of amounts that constituted unsecured claims, including termination and severance payments. The union took the position that Nortel was obligated to make the payments under the collective agreement. The former employees took the position that it would be inequitable to restore payments to unionized former employees and not non-unionized former employees. However, Nortel took the position that its financial pressure precluded it from paying all of the outstanding obligations.

HELD: Motions dismissed. The employee claims were unsecured claims and therefore did not have any statutory priority. Furthermore, the claims were based mostly on services that were provided pre-filing. As a result, there was no reason to treat the unionized or non-unionized employees any differently than other unsecured creditors and Nortel's resources were to be used to attempt restructuring.

Statutes, Regulations and Rules Cited:

Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36, s. 11, s. 11.3

Employment Standards Act, 2000, S.O. 2000, c. 41, s. 5

Labour Relations Act, 1995, S.O. 1995, c. 1, Schedule A,

Counsel:

Barry Wadsworth, for the CAW and George Borosh et al.

Susan Philpott and Mark Zigler, for the Nortel Networks Former Employees.

Lyndon Barnes and Adam Hirsh, for the Nortel Networks Board of Directors.

Alan Mersky and Mario Forte, for Nortel Networks et al.

Gavin H. Finlayson, for the Informal Nortel Noteholders Group.

Leanne Williams, for Flextronics Inc.

Joseph Pasquariello and Chris Armstrong, for Ernst & Young Inc., Monitor.

Janice Payne, for Recently Severed Canadian Nortel Employees ("RSCNE").

Gail Misra, for the CEP Union.

J. Davis-Sydor, for Brookfield Lepage Johnson Controls Facility Management Services.

Henry Juroviesky, for the Nortel Terminated Canadian Employees Steering Committee.

Alex MacFarlane, for the Official Unsecured Creditors Committee.

M. Starnino, for the Superintendent of Financial Services.

ENDORSEMENT

1 G.B. MORAWETZ J.:-- The process by which claims of employees, both unionized and non-unionized, have been addressed in restructurings initiated under the *Companies' Creditors Arrangement Act,* R.S.C. 1985, c. C-36 (the "CCAA") has been the subject of debate for a number of years. There is uncertainty and strong divergent views have been expressed. Notwithstanding that employee claims are ultimately addressed in many CCAA proceedings, there are few reported decisions which address a number of the issues being raised in these two motions. This lack of jurisprudence may reflect that the issues, for the most part, have been resolved through negotiation, as opposed to being determined by the court in the CCAA process - which includes motions for directions, the classification of creditors' claims, the holding and conduct of creditors' meetings and motions to sanction a plan of compromise or arrangement.

2 In this case, both unionized and non-unionized employee groups have brought motions for directions. This endorsement addresses both motions.

Union Motion

3 The first motion is brought by the National Automobile, Aerospace, Transportation and General Workers Union of Canada (CAW-Canada) and its Locals 27, 1525, 1530, 1535, 1837, 1839, 1905, and/or 1915 (the "Union") and by George Borosh on his own behalf and on behalf of all retirees of the Applicants who were formerly represented by the Union.

4 The Union requests an order directing the Applicants (also referred to as "Nortel") to recommence certain periodic and lump sum payments which the Applicants, or any of them, are obligated to make pursuant to the CAW collective agreement (the "Collective Agreement"). The Union also seeks an order requiring the Applicants to pay to those entitled persons the payments which should have been made to them under the Collective Agreement since January 14, 2009, the date of the CCAA filing and the date of the Initial Order.

5 The Union seeks continued payment of certain of these benefits including:

(a) retirement allowance payments ("RAP");
(b) voluntary retirement options ("VRO"); and

(c) termination and severance payments.

6 The amounts claimed by the Union are contractual entitlements under the Collective Agreement, which the Union submits are payable only after an individual's employment with the Applicants has ceased.

7 There are approximately 101 former Union members with claims to RAP. The current value of these RAP is approximately $2.3 million. There are approximately 180 former unionized retirees who claim similar benefits under other collective agreements.

8 There are approximately 7 persons who may assert claims to VRO as of the date of the Initial Order. These claims amount to approximately $202,000.

9 There are also approximately 600 persons who may claim termination and severance pay amounts. Five of those persons are former union members.

Former Employee Motion

10 The second motion is brought by Mr. Donald Sproule, Mr. David Archibald and Mr. Michael Campbell (collectively, the "Representatives") on behalf of former employees, including pensioners, of the Applicants or any person claiming an interest under or on behalf of such former employees or pensioners and surviving spouses in receipt of a Nortel pension, or group or class of them (collectively, the "Former Employees"). The Representatives seek an order varying the Initial Order by requiring the Applicants to pay termination pay, severance pay, vacation pay and an amount equivalent to the continuation of the benefit plans during the notice period, which are required to be paid to affected Former Employees in accordance with the *Employment Standards Act, 2000* S.O. 2000 c. 41 ("ESA") or any other relevant provincial employment legislation. The Representatives also seek an order varying the Initial Order by requiring the Applicants to recommence certain periodic and lump sum payments and to make payment of all periodic and lump sum payments which should have been paid since the Initial Order, which the Applicants are obligated to pay Former Employees in accordance with the statutory and contractual obligations entered into by Nortel and affected Former Employees, including the Transitional Retirement Allowance ("TRA") and any pension benefit payments Former Employees are entitled to receive in excess of the Nortel Networks Limited Managerial and Non-negotiated Pension Plan (the "Pension Plan"). TRA is similar to RAP, but is for non-unionized retirees. There are approximately 442 individuals who may claim the TRA. The current value of TRA obligations is approximately $18 million.

11 The TRA and the RAP are both unregistered benefits that run concurrently with other pension entitlements and operate as time-limited supplements.

12 In many respects, the motion of the Former Employees is not dissimilar to the CAW motion, such that the motion of the Former Employees can almost be described as a "Me too motion".

Background

13 On January 14, 2009, the Applicants were granted protection under the CCAA, pursuant to the Initial Order.

14 Upon commencement of the CCAA proceedings, the Applicants ceased making payments of amounts that constituted or would constitute unsecured claims against the Applicants. Included were payments for termination and severance, as well as amounts under various retirement and retirement transitioning programs.

15 The Initial Order provides:

(a) that Nortel is entitled but not required to pay, among other things, outstanding and future wages, salaries, vacation pay, employee benefits and pension plan payments;
(b) that Nortel is entitled to terminate the employment of or lay off any of its employees and deal with the consequences under a future plan of arrangement;
(c) that Nortel is entitled to vacate, abandon or quit the whole but not part of any lease agreement and repudiate agreements relating to leased properties (paragraph 11);
(d) for a stay of proceedings against Nortel;
(e) for a suspension of rights and remedies vis-à-vis Nortel;
(f) that during the stay period no person shall discontinue, repudiate, cease to perform any contract, agreement held by the company (paragraph 16);
(g) that those having agreements with Nortel for the supply of goods and/or services are restrained from, among other things, discontinuing, altering or terminating the supply of such goods or services. The proviso is that the goods or services supplied are to be paid for by Nortel in accordance with the normal payment practices.

Position of Union

16 The position of the CAW is that the Applicants' obligations to make the payments is to the CAW pursuant to the Collective Agreement. The obligation is not to the individual beneficiaries.

17 The Union also submits that the difference between the moving parties is that RAP, VRO and other payments are made pursuant to the Collective Agreement as between the Union and the Applicants and not as an outstanding debt payable to former employees.

18 The Union further submits that the Applicants are obligated to maintain the full measure of compensation under the Collective Agreement in exchange for the provision of services provided by the Union's members subsequent to the issuance of the Initial Order. As such, the failure to abide by the terms of the Collective Agreement, the Union submits, runs directly contrary to Section 11.3 of the CCAA as compensation paid to employees under a collective agreement can reasonably be interpreted as being payment for services within the meaning of this section.

19 Section 11.3 of the CCAA provides:

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

20 In order to fit within Section 11.3, services have to be provided after the date of the Initial Order.

21 The Union submits that persons owed severance pay are post-petition trade creditors in a bankruptcy, albeit in relation to specific circumstances. Thus, by analogy, persons owed severance pay are post-petition trade creditors in a CCAA proceeding. The Union relies on *Smokey River Coal Ltd. (Re)* 2001 ABCA 209 to support its proposition.

22 The Union further submits that when interpreting "compensation" for services performed under the Collective Agreement, it must include all of the monetary aspects of the Collective Agreement and not those specifically made to those actively employed on any particular given day.

23 The Union takes the position that Section 11.3 of the CCAA specifically contemplates that a supplier is entitled to payment for post-filing goods and services provided, and would undoubtedly refuse to continue supply in the event of receiving only partial payment. However, the Union contends that it does not have the ability to cease providing services due to the *Labour Relations Act, 1995*, S.O. 1995, c. 1. As such, the only alternative open to the Union is to seek an order to recommence the payments halted by the Initial Order.

24 The Union contends that Section 11.3 of the CCAA precludes the court from authorizing the Applicants to make selective determinations as to which parts of the Collective Agreement it will abide by. By failing to abide by the terms of the Collective Agreement, the Union contends that the Applicants have acted as if the contract has been amended to the extent that it is no longer bound by all of its terms and need merely address any loss through the plan of arrangement.

25 The Union submits that, with the exception of rectification to clarify the intent of the parties, the court has no jurisdiction at common law or in equity to alter the terms of the contract between parties and as the court cannot amend the terms of the Collective Agreement, the employer should not be allowed to act as though it had done so.

26 The Union submits that no other supplier of services would countenance, and the court does not have the jurisdiction to authorize, the recipient party to a contract unilaterally determining which provisions of the agreement it will or will not abide by while the contract is in operation.

27 The Union concludes that the Applicants must pay for the full measure of its bargain with the Union while the Collective Agreement remains in force and the court should direct the recommencement and repayment of those benefits that arise out of the Collective Agreement and which were suspended subsequently to the filing of the CCAA application on January 14, 2009.

Position of the Former Employees

28 Counsel to the Former Employees submits that the court has the discretion pursuant to Section 11 of the CCAA to order Nortel to recommence periodic and lump-sum payments to Former Employees in accordance with Nortel's statutory and contractual obligations. Further, the RAP payments which the Union seeks to enforce are not meaningfully different from those RAP benefits payable to other unionized retirees who belong to other unions nor from the TRA payable to non-unionized former employees. Accordingly, counsel submits that it would be inequitable to restore payments to one group of retirees and not others. Hence, the reference to the "Me too motion".

29 Counsel further submits that all employers and employees are bound by the minimum standards in the ESA and other applicable provincial employment legislation. Section 5 of the ESA expressly states that no employer can contract out or waive an employment standard in the ESA and that any such contracting out or waiver is void.

30 Counsel submits that each province has minimum standards employment legislation and regulations which govern employment relationships at the provincial level and that provincial laws such as the ESA continue to apply during CCAA proceedings.

31 Further, the Supreme Court of Canada has held that provincial laws in federally-regulated bankruptcy and insolvency proceedings continue to apply so long as the doctrine of paramountcy is not triggered: See *Crystalline Investments Ltd. v. Domgroup Ltd.*, [2004] 1 S.C.R. 60.

32 In this case, counsel further submits that there is no conflict between the provisions of the ESA and the CCAA and that paramountcy is not triggered and it follows that the ESA and other applicable employment legislation continues to apply during the Applicants' CCAA proceedings. As a result counsel submits that the Applicants are required to make payment to Former Employees for monies owing pursuant to the minimum employment standards as outlined in the ESA and other applicable provincial legislation.

Position of the Applicants

33 Counsel to the Applicants sets out the central purpose of the CCAA as being: "to facilitate the making of a compromise or arrangement between an insolvent debtor company and its creditors to the end that the company is able to continue in business". (*Pacific National Lease Holding Corp. (Re)*, [1992] B.C.J. No. 3070, aff'd by 1992, 15 C.B.R. (3d) 265), and that the stay is the primary procedural instrument used to achieve the purpose of the CCAA:

> ... if the attempt at a 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 Section 11 (*Pacific National Lease Holding Corp. (Re), supra*).

34 The Applicants go on to submit that the powers vested in the court under Section 11 to achieve these goals of the CCAA include:

(a) the ability to stay past debts; and
(b) the ability to require the continuance of present obligations to the debtor.

35 The corresponding protection extended to persons doing business with the debtor is that such persons (including employees) are not required to extend credit to the debtor corporation in the course of the CCAA proceedings. The protection afforded by Section 11.3 extends only to services provided after the Initial Order. Post-filing payments are only made for the purpose of ensuring the continued supply of services and that obligations in connection with past services are stayed. (See *Mirant Canada Energy Marketing Ltd. (Re)*, [2004] A.J. No. 331).

36 Furthermore, counsel to the Applicants submits that contractual obligations respecting post employment are obligations in respect of past services and are accordingly stayed.

37 Counsel to the Applicants also relies on the following statement from *Mirant, supra*, at paragraph 28:

> Thus, for me to find the decision of the Court of Appeal in Smokey River Coal analogous to Schaefer's situation, I would need to find that the obligation to pay severance pay to Schaefer was a clear contractual obligation that was necessary

> for Schaefer to continue his employment and not an obligation that arose from the cessation or termination of services. In my view, to find it to be the former would be to stretch the meaning of the obligation in the Letter Agreement to pay severance pay. It is an obligation that arises on the termination of services. It does not fall within a commercially reasonable contractual obligation essential for the continued supply of services. Only is his salary which he has been paid falls within that definition.

38 Counsel to the Applicants states that post-employment benefits have been consistently stayed under the CCAA and that post-employment benefits are properly regarded as pre-filing debts, which receive the same treatment as other unsecured creditors. The Applicants rely on *Syndicat nationale de l'amiante d'Asbestos inc. v. Jeffrey Mines Inc.* [2003] Q.J. No. 264 (C.A.) ("*Jeffrey Mine*") for the proposition that "the fact that these benefits are provided for in the collective agreement changes nothing".

39 Counsel to the Applicants submits that the Union seeks an order directing the Applicants to make payment of various post-employment benefits to former Nortel employees and that the Former Employees claim entitlement to similar treatment for all post-employment benefits, under the Collective Agreement or otherwise.

40 The Applicants take the position the Union's continuing collective representation role does not clothe unpaid benefits with any higher status, relying on the following from *Jeffrey Mine* at paras. 57 - 58:

> Within the framework of the restructuring plan, arrangements can be made respecting the amounts owing in this regard.
>
> The same is true in the case of the loss of certain fringe benefits sustained by persons who have not provided services to the debtor since the initial order. These persons became creditors of the debtor for the monetary value of the benefits lost further to Jeffrey Mines Inc.'s having ceased to pay premiums. The fact that these benefits are provided for in the collective agreements changes nothing.

41 In addition, the Applicants point to the following statement of the Quebec Court of Appeal in *Syndicat des employées et employés de CFAP-TV (TQS-Quebec), section locale 3946 du Syndicat canadien de la function publique c. TQS inc.*, 2008 QCCA 1429 at paras. 26-27:

> [Unofficial translation] Employees' rights are defined by the collective agreement that governs them and by certain legislative provisions. However, the resulting claims are just as much [at] risk as those of other creditors, in this case suppliers whose livelihood is also threatened by the financial precariousness of their debtor.
>
> The arguments of counsel for the Applicants are based on the erroneous premise that the employees are entitled to a privileged status. That is not what the CCAA provides nor is it what this court decided in *Syndicat national de l'amiante d'Asbestos inc. c. Mine Jeffrey inc.*

42 Collectively, RAP payment and TRA payments entail obligations of over $22 million. Counsel to the Applicants submits that there is no basis in principle to treat them differently. They are all stayed and there is no basis to treat any of these two unsecured obligations differently. The Applicants are attempting to restructure for the final benefit of all stakeholders and counsel submits that its collective resources must be used for such purposes.

Report of the Monitor

43 In its Seventh Report, the Monitor notes that at the time of the Initial Order, the Applicants employed approximately 6,000 employees and had approximately 11,700 retirees or their survivors receiving pension and/or benefits from retirement plans sponsored by the Applicants.

44 The Monitor goes on to report that the Applicants have continued to honour substantially all of the obligations to active employees. The Applicants have continued to make current service and special funding payments to their registered pension plans. All the health and welfare benefits for both active employees and retirees have been continued to be paid since the commencement of the CCAA proceedings.

45 The Monitor further reports that at the filing date, payments to former employees for termination and severance as well as the provisions of the health and dental benefits ceased. In addition, non-registered and unfunded retirement plan payments ceased.

46 More importantly, the Monitor reports that, as noted in previous Monitor's Reports, the Applicants' financial position is under pressure.

Discussion and Analysis

47 The acknowledged purpose of the CCAA is to facilitate the making of a compromise or arrangement between an insolvent debtor company and its creditors to the end that the company is able to continue in business. (See *Pacific National Lease Holding Corp. (Re),* [1992] B.C.J. No. 3070, aff'd by (1992), 15 C.B.R. (3d) 265, at para. 18 citing *Chef Ready Foods Ltd.* v. *Hongkong Bank of Canada* (1990), 4 C.B.R. (3d) 311 (B.C.C.A.) at 315). The primary procedural instrument used to achieve that goal is the ability of the court to issue a broad stay of proceedings under Section 11 of the CCAA.

48 The powers vested in the court under Section 11 of the CCAA to achieve these goals include the ability to stay past debts; and the ability to require the continuance of present obligations to the debtor. (*Woodwards Limited (Re)*, (1993), 17 C.B.R. (3d) 236 (S.C.).

49 The Applicants acknowledged that they were insolvent in affidavit material filed on the Initial Hearing. This position was accepted and is referenced in my endorsement of January 14, 2009. The Applicants are in the process of restructuring but no plan of compromise or arrangement has yet to be put forward.

50 The Monitor has reported that the Applicants are under financial pressure. Previous reports filed by the Monitor have provided considerable detail as to how the Applicants carry on operations and have provided specific information as to the interdependent relationship between Nortel entities in Canada, the United States, Europe, the Middle East and Asia.

51 In my view, in considering the impact of these motions, it is both necessary and appropriate to take into account the overall financial position of the Applicants. There are several reasons for doing so:

(a) The Applicants are not in a position to honour their obligations to all creditors.
(b) The Applicants are in default of contractual obligations to a number of creditors, including with respect to significant bond issues. The obligations owed to bondholders are unsecured.
(c) The Applicants are in default of certain obligations under the Collective Agreements.
(d) The Applicants are in default of certain obligations owed to the Former Employees.

52 It is also necessary to take into account that these motions have been brought prior to any determination of any creditor classifications. No claims procedure has been proposed. No meeting of creditors has been called and no plan of arrangement has been presented to the creditors for their consideration.

53 There is no doubt that the views of the Union and the Former Employees differ from that of the Applicants. The Union insists that the Applicants honour the Collective Agreement. The Former Employees want treatment that is consistent with that being provided to the Union. The record also establishes that the financial predicament faced by retirees and Former Employees is, in many cases, serious. The record references examples where individuals are largely dependent upon the employee benefits that, until recently, they were receiving.

54 However, the Applicants contend that since all of the employee obligations are unsecured it is improper to prefer retirees and the Former Employees over the other unsecured creditors of the Applicants and furthermore, the financial pressure facing the Applicants precludes them from paying all of these outstanding obligations.

55 Counsel to the Union contends that the Applicants must pay for the full measure of its bargain with the Union while the Collective Agreement remains in force and further that the court does not have the jurisdiction to authorize a party, in this case the Applicants, to unilaterally determine which provisions of the Collective Agreement they will abide by while the contract is in operation. Counsel further contends that Section 11.3 of the CCAA precludes the court from authorizing the Applicants to make selective determinations as to which parts of the Collective Agreement they will abide by and that by failing to abide by the terms of the Collective Agreement, the Applicants acted as if the Collective Agreement between themselves and the Union has been amended to the extent that the Applicants are no longer bound by all of its terms and need merely address any loss through the plan of arrangement.

56 The Union specifically contends that the court has no jurisdiction to alter the terms of the Collective Agreement.

57 In addressing these points, it is necessary to keep in mind that these CCAA proceedings are at a relatively early stage. It also must be kept in mind that the economic circumstances at Nortel are such that it cannot be considered to be carrying on "business as usual". As a result of the Applicants' insolvency, difficult choices will have to be made. These choices have to be made by all stakeholders.

58 The Applicants have breached the Collective Agreement and, as a consequence, the Union has certain claims.

59 However, the Applicants have also breached contractual agreements they have with Former Employees and other parties. These parties will also have claims as against the Applicants.

60 An overriding consideration is that the employee claims whether put forth by the Union or the Former Employees, are unsecured claims. These claims do not have any statutory priority.

61 In addition, there is nothing on the record which addresses the issue of how the claims of various parties will be treated in any plan of arrangement, nor is there any indication as to how the creditors will be classified. These issues are not before the court at this time.

62 What is before the court is whether the Applicants should be directed to recommence certain periodic and lump sum payments that they are obligated to make under the Collective Agreement as well as similar or equivalent payments to Former Employees.

63 It is necessary to consider the meaning of Section 11.3 and, in particular, whether the Section should be interpreted in the manner suggested by the Union.

64 Counsel to the Union submits that the ordinary meaning of "services" in section 11.3 includes work performed by employees subject to a collective agreement. Further, even if the ordinary meaning is plain, courts must consider the purpose and scheme of the legislation, and relevant legal norms. Counsel submits that the courts must consider the entire context. As a result, when interpreting "compensation" for services performed under a collective agreement, counsel to the Union submits it must include all of the monetary aspects of the agreement and not those made specifically to those actively employed on any particular given day.

65 No cases were cited in support of this interpretation.

66 I am unable to agree with the Union's argument. In my view, section 11.3 is an exception to the general stay provision authorized by section 11 provided for in the Initial Order. As such, it seems to me that section 11.3 should be narrowly construed. (See Ruth Sullivan, *Sullivan on the Construction of Statutes*, 5th ed. (Markham, Ont.: LexisNexis Canada Inc., 2008) at 483-485.) Section 11.3 applies to services provided after the date of the Initial Order. The ordinary meaning of "services" must be considered in the context of the phrase "services, ... provided after the order is made". On a plain reading, it contemplates, in my view, some activity on behalf of the service provider which is performed after the date of the Initial Order. The CCAA contemplates that during the reorganization process, pre-filing debts are not paid, absent exceptional circumstances and services provided after the date of the Initial Order will be paid for the purpose of ensuring the continued supply of services.

67 The flaw in the argument of the Union is that it equates the crystallization of a payment obligation under the Collective Agreement to a provision of a service within the meaning of s. 11.3. The triggering of the payment obligation may have arisen after the Initial Order but it does not follow that a service has been provided after the Initial Order. Section 11.3 contemplates, in my view, some current activity by a service provider post-filing that gives rise to a payment obligation post-filing. The distinction being that the claims of the Union for termination and severance pay are based, for the most part, on services that were provided pre-filing. Likewise, obligations for benefits arising from RAP and VRO are again based, for the most part, on services provided pre-filing. The exact time of when the payment obligation crystallized is not, in my view, the determining factor under section 11.3. Rather, the key factor is whether the employee performed services after the date of the Initial Order. If so, he or she is entitled to compensation benefits for such current service.

68 The interpretation urged by counsel to the Union with respect to this section is not warranted. In my view, section 11.3 does not require the Applicants to make payment, at this time, of the outstanding obligations under the Collective Agreement.

69 The Union also raised the issue as to whether the court has the jurisdiction to order a stay of the outstanding obligations under Section 11 of the CCAA.

70 The Union takes the position that, with the exception of rectification to clarify the intent of the parties, the court has no jurisdiction at common law or in equity to alter the terms of a contract between parties. The Union relies on *Bilodeau et al v. McLean*, [1924] 3 D.L.R. 410 (Man. C.A.); *Desener v. Myles,* [1963] S.J. No. 31 (Q.B.); *Hiesinger v. Bonice* [1984] A.J. No. 281; *Werchola v. KC5 Amusement Holdings Ltd.* 2002 SKQB 339 to support its position.

71 The Union extends this argument and submits that as the court cannot amend the terms of a collective agreement, the employer should not be allowed to act as though it had been.

72 As a general rule, counsel to the Union submits, there is in place a comprehensive regime for the regulation of labour relations with specialized labour-relations tribunals having exclusive jurisdiction to deal with legal and factual matters arising under labour legislation and no court should restrain any tribunal from proceeding to deal with such matters.

73 However, as is clear from the context, these cases referenced at [70] are dealing with the ordinary situation in which there is no issue of insolvency. In this case, we are dealing with a group of companies which are insolvent and which have been accorded the protection of the CCAA. In my view, this insolvency context is an important distinguishing factor. The insolvency context requires that the stay provisions provided in the CCAA and the Initial Order must be given meaningful interpretation.

74 There is authority for the proposition that, when exercising their authority under insolvency legislation, the courts may make, at the initial stage of a CCAA proceeding, orders regarding matters, but for the insolvent condition of the employer, would be dealt with pursuant to provincial labour legislation, and in most circumstances, by labour tribunals. In *Re: Pacific National Lease Holding Corp.* (1992) 15 C.B.R. (3d) 265 (B.C.C.A.), the issue involved the question whether a CCAA debtor company had to make statutory severance payments as was mandatory under the provincial employment standards legislation. MacFarlane J.A. stated at pp. 271-2:

> It appears to me that an order which treats creditors alike is in accord with the purpose of the CCAA. Without the provisions of that statute the petitioner companies might soon be in bankruptcy, and the priority which the employees now have would be lost. The process provided by the CCAA is an interim one. Generally, it suspends but does not determine the ultimate rights of any creditor. In the end it may result in the rights of employees being protected, but in the meantime it preserves the status quo and protects all creditors while a reorganization is being attempted.
>
> ...
>
> This case is not so much about the rights of employees as creditors, but the right of the court under the CCAA to serve not only the special interests of the direc-

> tors and officers of the company but the broader constituency referred to in *Chef Ready Foods Ltd., supra*. Such a decision may invariably conflict with provincial legislation, but the broad purpose of the CCAA must be served.

75 The *Jeffrey Mine* decision is also relevant. In my view, the *Jeffrey Mine* case does not appear to support the argument that the Collective Agreement is to be treated as being completely unaffected by CCAA proceedings. It seems to me that it is contemplated that rights under a collective agreement may be suspended during the CCAA proceedings. At paragraphs 60-62, the court said under the heading Recapitulation (in translation):

> The collective agreements continue to apply like any contract of successive performance not modified by mutual agreement after the initial order or not disclaimed (assuming that to be possible in the case of collective agreements). Neither the monitor nor the court can amend them unilaterally. That said, distinctions need to be made with regard to the prospect of the resulting debts.
>
> Thus, unionized employees kept on or recalled are entitled to be paid immediately by the monitor for any service provided after the date of the order (s. 11.3), in accordance with the terms of the original version of the applicable collective agreement by the union concerned. However, the obligations not honoured by Jeffrey Mine Inc. with regard to services provided prior to the order constitute debts of Jeffrey Mine Inc. for which the monitor cannot be held liable (s. 11.8 CCAA) and which the employees cannot demand to be paid immediately (s. 11.3 CCAA).
>
> Obligations that have not been met with regard to employees who were laid off permanently on October 7, 2002, or with regard to persons who were former employees of Jeffrey Mine Inc. on that date and that stem from the collective agreements or other commitments constitute debts of the debtor to be disposed of in the restructuring plan or, failing that, upon the bankruptcy of Jeffrey Mine Inc.

76 The issue of severance pay benefits was also referenced in *Communications, Energy, Paperworks, Local 721G v. Printwest Communications Ltd.* 2005 SKQB 331 at paras. 11 and 15. The application of the Union was rejected:

> ... The claims for severance pay arise from the collective bargaining agreement. But severance pay does not fall into the category of essential services provided during the organization period in order to enable Printwest to function.
>
> ...
>
> If the Union's request should be accepted, with the result that the claims for severance pay be dealt with outside the plan of compromise - and thereby be paid in full - such a result could not possibly be viewed as fair and reasonable with respect to other unsecured creditors, who will possibly receive only a small fraction of the amounts owing to them for goods and services provided to Printwest in good faith. Thus, the application of the Union in this respect must be rejected.

Disposition

77 At the commencement of an insolvency process, the situation is oftentimes fluid. An insolvent debtor is faced with many uncertainties. The statute is aimed at facilitating a plan of compromise or arrangement. This may require adjustments to the operations in a number of areas, one of which may be a downsizing of operations which may involve a reduction in the workforce. These adjustments may be painful but at the same time may be unavoidable. The alternative could very well be a bankruptcy which would leave former employees, both unionized and non-unionized, in the position of having unsecured claims against a bankrupt debtor. Depending on the status of secured claims, these unsecured claims may, subject to benefits arising from the recently enacted *Wage Earner Protection Program Act*, be worth next to nothing.

78 In the days ahead, the Applicants, former employees, both unionized and non-unionized may very well have arguments to make on issues involving claims processes (including the ability of the Applicants to compromise claims), classification, meeting of creditors and plan sanction. Nothing in this endorsement is intended to restrict the rights of any party to raise these issues.

79 The reorganization process under the CCAA can be both long and painful. Ultimately, however, for a plan to be sanctioned by the court, the application must meet the following three tests:

(i) there has to be strict compliance with all statutory requirements and adherence to previous orders of the court;
(ii) nothing has been done or purported to be done that is not authorized by the CCAA;
(iii) the plan is fair and reasonable. *Re: Sammi Atlas Inc.* (1998), 3 C.B.R. (4th) 171 (Ont. Gen. Div.)

80 At this stage of the Applicants' CCAA process, I see no basis in principle to treat either unionized or non-unionized employees differently than other unsecured creditors of the Applicants. Their claims are all stayed. The Applicants are attempting to restructure for the benefit of all stakeholders and their resources should be used for such a purpose.

81 It follows that the motion of the Union is dismissed.

82 The Applicants also raised the issue that the Union consistently requested the right to bargain on behalf of retirees who were once part of the Union and that the concession had not been granted. Consequently, the retirees' substantive rights are not part of the bargain between the unionized employees and the employer. Counsel to the Applicants submitted that the union may collectively alter the existing rights of any employee but it cannot negatively do so with respect to retirees' rights.

83 The Union countered that the rights gained by a member of the bargaining unit vest upon retirement, despite the fact that a collective agreement expires, and are enforceable through the grievance procedure.

84 Both parties cited *Dayco (Canada) Ltd. v. National Automobile, Aerospace and Agricultural Implement Workers Union of Canada (CAW-Canada)* [1993] 2 S.C.R. 230 in support of their respective positions.

85 In view of the fact that this motion has been dismissed for other reasons, it is not necessary for me to determine this specific issue arising out of the *Dayco* decision.

86 The motion of the Former Employees was characterized, as noted above, as a "Me too motion". It was based on the premise that, if the Union's motion was successful, it would only be equitable if the Former Employees also received benefits. The Former Employees do not have the benefit of any enhanced argument based on the Collective Agreement. Rather, the argument of the Former Employees is based on the position that the Applicants cannot contract out of the ESA or any other provincial equivalent. In my view, this is not a case of contracting out of the ESA. Rather, it is a case of whether immediate payout resulting from a breach of the ESA is required to be made. In my view, the analysis is not dissimilar from the Collective Agreement scenario. There is an acknowledgment of the applicability of the ESA, but during the stay period, the Former Employees cannot enforce the payment obligation. In the result, it follows that the motion of the Former Employees is also dismissed.

87 However, I am also mindful that the record, as I have previously noted, makes reference to a number of individuals that are severely impacted by the cessation of payments. There are no significant secured creditors of the Applicants, outside of certain charges provided for in the CCAA proceedings, and in view of the Applicants' declared assets, it is reasonable to expect that there will be a meaningful distribution to unsecured creditors, including retirees and Former Employees. The timing of such distribution may be extremely important to a number of retirees and Former Employees who have been severely impacted by the cessation of payments. In my view, it would be both helpful and equitable if a partial distribution could be made to affected employees on a timely basis.

88 In recognition of the circumstances that face certain retirees and Former Employees, the Monitor is directed to review the current financial circumstances of the Applicants and report back as to whether it is feasible to establish a process by which certain creditors, upon demonstrating hardship, could qualify for an unspecified partial distribution in advance of a general distribution to creditors. I would ask that the Monitor consider and report back to this court on this issue within 30 days.

89 This decision may very well have an incidental effect on the Collective Agreement and the provisions of the ESA, but it is one which arises from the stay. It does not, in my view, result from a repudiation of the Collective Agreement or a contracting out of the ESA. The stay which is being recognized is, in my view, necessary in the circumstances. To hold otherwise, would have the effect of frustrating the objectives of the CCAA to the detriment of all stakeholders.

G.B. MORAWETZ J.

TAB 6

Para 9

Case Name:

Nortel Networks Corp. (Re)

RE: IN THE MATTER OF the Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36, as Amended
AND IN THE MATTER OF a Plan of Compromise or Arrangement of 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

[2009] O.J. No. 3280

53 C.B.R. (5th) 196

2009 CarswellOnt 3028

2009 CanLII 26603

Court File No. 09-CL-7950

Ontario Superior Court of Justice
Commercial List

G.B. Morawetz J.

Heard: July 30, 2009.
Judgment: July 30, 2009.
Released: July 31, 2009.

(15 paras.)

Bankruptcy and insolvency law -- Companies' Creditors Arrangement Act (CCAA) matters -- Compromises and arrangements -- Claims -- International insolvencies -- Motion by Nortel Companies and others for court approval of call for claims process and mechanism for paying out claims by employees in financial hardship allowed.

Bankruptcy and insolvency law -- Proceedings -- Practice and procedure -- Stays -- Motion by Nortel Companies to extend CCAA stay allowed -- Companies working in good faith and with due diligence to reorganize extensive operations.

Motion by the Nortel Companies and the U.S. debtors for an order implementing a call for claims procedure, requiring most creditors to file their claims by September 30, 2009. The Companies, the Monitor and former employees also moved for an order approving a process for making immediate payments on claims by employees experiencing financial hardship. The Companies also moved for an extension of the CCAA stay period to October 30, 2009.

HELD: Motions allowed. The call for claims procedure would facilitate the moving parties in formulating a plan and reconciling the claims. The mechanism for paying out employee claims was approved. The stay was extended because the court was convinced the Companies were working in good faith and with due diligence to restructure their extensive operations.

Statutes, Regulations and Rules Cited:

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

Counsel:

Derrick Tay and Jennifer Stam, for Nortel Networks Corporation et al.

J.A. Carfagnini, C.G. Armstrong and G. Rubenstein, for Ernst & Young Inc., Monitor.

Arthur Jacques, T. McRae and J. Payne, for the Nortel Continuing Canadian Employees.

S. R. Orzy, for the Noteholders.

Lyndon Barnes and Adam Hirsh, for the Board of Directors of Nortel Networks Corporation and Nortel Networks Limited.

A. MacFarlane, for the Official Committee.

R. Sahni, for the Noteholders' Committee.

Robin B. Schwill, for the Nortel Networks U.K. Limited (in Administration).

Mark Zigler, for the Former Employees.

Tina Lie, for the Superintendent of Financial Services.

B. Wadsworth, for CAW-Canada.

ENDORSEMENT

1 **G.B. MORAWETZ J.**:-- The motion proceeded unopposed and resulted in two orders for the following reasons:

Claims Procedure Order

2 The Applicants and the U.S. Debtors wish to implement a "call for claims" procedure that will require most creditors of the Applicants and the U.S. Debtors to file their claims by September 30, 2009. The process will allow both the Applicants and the U.S. Debtors to begin the process of reconciling these claims. It should also provide the Applicants and the U.S. Debtors with more definitive information with respect to claims, which information can be used to assist in the formulation of a plan.

3 The Applicants prepared the proposed procedure order with a view to showing certain essential elements with the claims order that will shortly be sought in the Chapter 11 Proceedings.

4 The proposed procedure is described in both Mr. Doolittle's affidavit of July 24, 2009 and in the Sixteenth Report of the Monitor.

5 I am satisfied that it is appropriate to approve the Claims Procedure.

Employee Hardship, Canadian GSPA, Stay Extension Order

6 In response to the endorsement released on June 18, 2009, the Monitor, the Applicants and Koskie Minsky LLP, in its capacity as Representative Counsel for former employees, have considered the issue of hardship being experienced by certain former employees and have developed a mechanism for making immediate payment on account of the claims of those former employees who are experiencing financial hardship. The mechanism is summarized in both Mr. Doolittle's affidavit and in the Monitor's Sixteenth Report. The Eligibility Requirements and Procedure is also set out at page 115(a) of the Motion Record. The proposal has also been reviewed by the Official Committee, the Bondholders and by FSCO, with no party objecting.

7 It was acknowledged by counsel to the Monitor that further issues may arise out of the implementation of the mechanism and for this reason, among others, the Monitor indicated that it would report back to court on this issue by September 30, 2009.

8 Counsel to the CAW also brought to the court's attention that the Union may wish to have the eligibility criteria reviewed at that time.

9 I am satisfied that the proposed process is an appropriate response to the issue as raised in the June 18, 2009 endorsement and the process is approved, subject to further review, if any, after the Monitor reports back to court.

10 I am also satisfied that it is appropriate to approve the extension of the Canadian Group Supplier Protocol Agreement.

11 Finally, the Applicants seek an extension of the Stay Period to October 30, 2009.

12 As indicated in the Record, NNC is the ultimate parent of the Nortel companies, which operate world wide. The Applicants also have significant business operations. The restructuring of the Applicants will take a significant amount of time.

13 The progress to date has been described in various affidavits filed by the Applicants and in the Reports filed by the Monitor. The most recent affidavit of Mr. Doolittle and the Sixteenth Report also outline some of the upcoming steps that the Applicants intend to take in this process. The Monitor has also noted that, based on the key assumptions used in the preparation of the Applicants' July 12 Cash Flow Forecast, the Applicants will have sufficient cash resources available during the Forecast Period to permit the Applicants to make further progress in these proceedings. The Monitor supports the request for the extension.

14 Having reviewed the Record and having heard submissions, I am satisfied that the Applicants continue to work in good faith and with due diligence such that the request to extend the Stay Period to October 30, 2009 is warranted. The Stay Period is therefore extended to October 30, 2009.

15 Orders to give effect to the foregoing have been signed by me.

G.B. MORAWETZ J.

TAB 7

Para 206

Case Name:

Nortel Networks Corp. (Re)

IN THE MATTER OF the Companies' Creditors Arrangement Act, R.S.C. 1985, c. c-36, as Amended
AND IN THE MATTER OF a Plan of Compromise or Arrangement of Nortel Networks Corporation, Nortel Networks Limited, Nortel Networks Global Corporation, Nortel Networks International Corporation and nortel networks technology corporation
APPLICATION UNDER the Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36, as amended

[2015] O.J. No. 2440

2015 ONSC 2987

2015 CarswellOnt 7072

27 C.B.R. (6th) 175

254 A.C.W.S. (3d) 522

Court File No.: 09-CL-7950

Ontario Superior Court of Justice
Commercial List

F.J.C. Newbould J.

Heard: May 12-15, 20-22, 27-30, June 2, 5, 6, 16-20, 23, 24 and September 22-24, 2014.
Judgment: May 12, 2015.

(263 paras.)

Counsel:

Benjamin Zarnett, Peter Ruby, Jessica Kimmel, Graham D. Smith, Alan Mark, Julie Rosenthal, Joseph Pasquariello, Jennifer Stam, Ken Coleman, Jacob Pultman, Paul Keller, Laura Hall, R. Paul Steep, Elder C. Marques, Byron Shaw, Kenneth T. Rosenberg, Lily Harmer, Max Starnino, Karen Jones, Megan Shortreed, Mark Zigler, Ari Kaplan, Jeff Van Bakel, Barbara Walancik, Counsel for the Canadian Creditors' Committee.

Sheila Block, Andrew Gray, Scott A. Bomhof, Avi Luft, James Bromley, Lisa Schweitzer, Jeffrey Rosenthal, Howard Zelbo, Counsel for the U.S. Debtors.

Richard Swan, Tom Matz, Jonathan Bell, Gavin H. Finlayson, Kevin J. Zych, Andrew LeBlanc, Nick Bassett, Counsel for the Ad Hoc Group of Bondholders.

Matthew P. Gottlieb, Matthew Milne-Smith, James Doris, William Maguire, Neil Oxford, John Whiteoak, Tracy L. Wynne, Derek Adler, Counsel for the EMEA Debtors.

Michael E. Barrack, D.J. Miller, John L. Finnigan, Andrea McEwan, Rebecca (Lewis) Kennedy, Michael Shakra, Brian O'Connor, Eugene Chang, Counsel for the UKPC.

R. Shayne Kukulowicz, Goff Shaw, Abid Qureshi, David H. Botter, Counsel for the U.S. Unsecured Creditors' Committee.

Kenneth David Kraft, Karen B. Dine, John Salmas, David Crichlow, Counsel for Wilmington Trust, National Association, Trustee.

Brett Harrison, Counsel for The Bank of New York Mellon, Trustee.

John D. Marshall, Counsel for Law Debenture Trust Company of New York, Trustee.

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APPENDIX A.

Allocation of the proceeds of the line of business sales

(i) Mr. Kinrich
(ii) Mr. Malackowski and Mr. Huffard
(iii) Mr. Green

APPENDIX B

Residual IP proceeds allocation

(i) Mr. Kinrich's license approach to value
(ii) Mr. Malacko's contribution approach to value
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F.J.C. NEWBOULD J.:--

REASONS FOR JUDGMENT

Prologue

1 Until January 14, 2009, Nortel Networks Corporation ("NNC") was a publicly-traded Canadian company and the direct or indirect parent of more than 130 subsidiaries located in more than

100 countries, collectively known as the "Nortel Group" or "Nortel". It operated a global networking solutions and telecommunications business.

2 On January 14, 2009 most of the Nortel entities filed for bankruptcy protection. In Canada, the Canadian incorporated entities (the "Canadian Debtors") filed under the *Companies' Creditors Arrangement Act* ("CCAA"). In the United States, most of the U.S. incorporated entities (the "U.S. Debtors") filed under chapter 11 of the *U.S. Bankruptcy Code*. In England, most of the entities incorporated in Europe, the Middle East and Africa (the "EMEA[1] Debtors") were granted administration orders under the *UK Insolvency Act, 1986.*

3 The initial intent of Nortel was to downsize and carry on those portions of its telecommunications business that it thought could be profitable. However that plan quickly evaporated and in June, 2009 Nortel decided to liquidate its assets. It sold its business lines for approximately $3.285[2] billion of which approximately $2.85 billion is now available to be allocated. It then sold its residual intellectual property for $4.5 billion. These amounts totalling $7.3 billion are held in escrow (the "lockbox funds"). At issue in these proceedings is how to allocate the $7.3 billion among the Canadian Debtors, the U.S. Debtors and the EMEA Debtors.

4 The trial in this case was unique. It was a joint trial of the Ontario Superior Court of Justice (Commercial List) and the U.S. Bankruptcy Court for the District of Delaware[3]. It arose from the arrangements made by the parties as part of the process of selling assets, and from a Cross-border Insolvency Protocol (the "Protocol"). In short:

> **(i)** The parties agreed in an Interim Funding and Settlement Agreement before any of the Nortel assets were sold to put the proceeds of sale into escrow and then attempt to agree on a protocol for resolving how the proceeds were to be allocated. If no agreement was reached, the issues were to be tried by the Ontario and U.S. Courts pursuant to the Protocol.
>
> **(ii)** The parties could not agree on the allocation, nor could they agree on a protocol process. By orders of the Ontario and U.S. Courts, the allocation was directed to be determined in a joint trial pursuant to the Protocol. The EMEA Debtors were held to have attorned to the jurisdiction of these courts in the escrow agreements made with respect to the proceeds of the several sales that had occurred.[4]

5 The Protocol was approved early in the CCAA and chapter 15 proceedings by orders the Ontario and U.S. Courts.[5] This type of protocol has become standard in the last number of years to govern the administration of cross-border insolvency proceedings. The Protocol included it its purposes:

> Accordingly, this Protocol has been developed to promote the following mutually desirable goals and objectives in the Insolvency Proceedings:
>
> (a) harmonize and coordinate activities in the Insolvency Proceedings before the Courts;

(b) promote the orderly and efficient administration of the Insolvency Proceedings to, among other things, maximize the efficiency of the Insolvency Proceedings, reduce the costs associated therewith and avoid duplication of effort;

(c) honor the independence and integrity of the Courts and other courts and tribunals of the United States and Canada, respectively;

(d) promote international cooperation and respect for comity among the Courts, the Debtors, the Creditors Committee, the Estate Representatives (which include the Chapter 11 Representatives and the Canadian Representatives as such terms are defined below) and other creditors and interested parties in the Insolvency Proceedings;

(e) facilitate the fair, open and efficient administration of the Insolvency Proceedings for the benefit of all of the Debtors' creditors and other interested parties, wherever located; and

(f) implement a framework of general principles to address basic administrative issues arising out of the cross-border nature of the Insolvency Proceedings.

6 The Protocol contained a number of provisions regarding the independence of the Canadian and U.S. Courts and the exclusive jurisdiction of each Court in the determination of matters arising in the Canadian and U.S. proceedings respectively. Included in the Protocol were the following provisions:

> 7. The approval and implementation of this Protocol shall not divest nor diminish the U.S. Court's and the Canadian Court's respective independent jurisdiction over the subject matter of the U.S. Proceedings and the Canadian Proceedings, respectively...
>
> 8. The U.S. Court shall have sole and exclusive jurisdiction and power over the conduct of the U.S. Proceedings and the hearing and determination of matters arising in the U.S. Proceedings. The Canadian Court shall have sole and exclusive jurisdiction and power over the conduct of the Canadian Proceedings and the hearing and determination of matters arising in the Canadian Proceedings.

7 The Protocol provided in paragraph 12 for the harmonization and co-ordination of the administration of the two proceedings in Canada, including the holding of joint hearings of the two Courts and providing for discussions between the two judges. Included were the following:

> 12. To harmonize and coordinate the administration of the Insolvency Proceedings, the U.S. Court and the Canadian Court each may coordinate activities and consider whether it is appropriate to defer to the judgment of the other Court. In furtherance of the foregoing:

(a) The U.S. Court and the Canadian Court may communicate with one another, with or without counsel present, with respect to any procedural matter relating to the Insolvency Proceedings.

...

(d) The U.S. Court and the Canadian Court may conduct joint hearings (each a "Joint Hearing") with respect to any cross-border matter or the interpretation or implementation of this Protocol where both the U.S. Court and the Canadian Court consider such a Joint Hearing to be necessary or advisable, or as otherwise provided herein, to, among other things, facilitate or coordinate proper and efficient conduct of the Insolvency Proceedings or the resolution of any particular issue in the Insolvency Proceedings. With respect to any Joint Hearing, unless otherwise ordered, the following procedures will be followed:

(vi) The Judge of the U.S. Court and the Justice of the Canadian Court, shall be entitled to communicate with each other during or after any joint hearing, with or without counsel present, for the purposes of (1) determining whether consistent rulings can be made by both Courts; (2) coordinating the terms upon of the Courts' respective rulings; and (3) addressing any other procedural or administrative matters.

8 A joint hearing was held for this allocation dispute. The court rooms in Toronto and Wilmington were set up electronically so that lawyers and witnesses could and did appear in either courtroom and communicate with a lawyer, witness or the judge in the other courtroom through state of the art telecommunications services.

9 After the evidence was heard, written closing and reply briefs were filed by the parties and oral argument was made. It was agreed that at the conclusion of the case that each Court would release its decision at the same time. This judgment is being released at the same time as the opinion of Judge Gross in Wilmington.

10 Judge Gross in Wilmington and I have communicated with each other in accordance with the Protocol with a view to determining whether consistent rulings can be made by both Courts. We have come to the conclusion that a consistent ruling can and should be made by both Courts. We have come to this conclusion in the exercise of our independent and exclusive jurisdiction in each of our jurisdictions. These insolvency proceedings have now lasted over six years at unimaginable expense and they should if at all possible come to a final resolution. It is in all of the parties' interests for that to occur. Consistent decisions that we both agree with will facilitate such a resolution.

Nortel history and its matrix structure

11 NNC was the successor to a long line of technology companies headquartered in Canada dating back to the founding of Bell Telephone Company of Canada in 1883. Prior to being named Nortel, it was known as Northern Telecom. NNC's principal, direct operating subsidiary, also a Canadian company, was Nortel Networks Limited ("NNL"), which in turn was the direct or indirect parent of operating companies located around the world.[6]

12 From the mid-1980s, Nortel expanded substantially through the continued development of ground-breaking technology. The Nortel Group moved from developing and manufacturing traditional landline phone technology and equipment into digital, wireless and photonic technologies. At the same time, the Nortel Group expanded into Europe, Asia, Africa, the Middle East and Latin America.

13 At the time of its insolvency, Nortel had four main product groups (also known as Lines of Business):

* The "Carrier Networks" segment provided wireless networking solutions that enabled service providers and cable operators to supply mobile voice, data and multimedia communications to individuals and enterprises using mobile phone and other wireless devices. The Carrier Networks business also offered products providing local, toll, long distance and international gateway capabilities to telephone service providers as well as providing support to customers transitioning from one network to another.

* The "Enterprise Solutions" segment provided enterprise communications solutions addressing the headquarters, branch and home office needs of large and small businesses. The Enterprise Solutions segment's offerings included, among other things, Unified Communications, Ethernet routing and multiservice switching, IP and digital telephony (including phones), wireless LANs, security, IP and SIP contact centers, self-service solutions, messaging, conferencing and SIP-based multimedia solutions.

* The Metro Ethernet Networks ("MEN") segment provided carrier-grade Ethernet transport capabilities focused on meeting customers' needs for higher performance and lower cost emerging video-intensive applications. MEN included optical networking, carrier Ethernet switching products and multi-service switching products.

* The "Global Services" segment provided a broad range of services and solutions including network implementation services, network support services, network managed services (which related to the monitoring and management of customer networks and hosted solutions) and network application services.

14 The Nortel Group consists of more than 140 separate corporate entities located in 60 separate sovereign jurisdictions including Canada, the United States and the EMEA region, as well as the Caribbean and Latin America and Asia. NNC, the Nortel Group's ultimate parent holding company, was publicly listed and traded on both the Toronto Stock Exchange and the New York Stock Exchange.

15 One of NNC's direct subsidiaries is NNL, which was the Canadian operating company of the Nortel Group. NNL in turn owns 100% of the equity of each of NNI, which was the Nortel Group's operating company in the United States, NNUK, which was the Nortel Group's operating company in the United Kingdom, NN Ireland, which was the Nortel Group's operating company in Ireland, and 91.17% of the equity of NNSA, which was the Nortel Group's operating company in France.

16 The Nortel Group operated along business lines as a highly integrated multinational enterprise with a matrix structure that transcended geographic boundaries and legal entities organized around the world. Each entity, such as NNL, NNI, NNUK, NN Ireland and NNSA, was integrated into regional and product line management structures to share information and perform research and development ("R&D"), sales and other common functions across geographic boundaries and across legal entities. The matrix structure was designed to enable Nortel to function more efficiently, drawing on employees from different functional disciplines worldwide, allowing them to work together to develop products and attract and provide service to customers, fulfilling their demands globally.

17 As a result of Nortel's matrix structure, no single Nortel entity, either NNL or any of the other Canadian debtors in Canada, NNI or any of the other US debtors in the United States or NNUK or any of the other EMEA debtors, was able to provide the full line of Nortel products and services, including R&D capabilities, on a stand-alone basis. While Nortel ensured that all corporate entities complied with local laws regarding corporate governance, no corporate entity carried on business on its own.

18 R&D was the primary driver of Nortel's value and profit. Together with NNL, the principal companies that performed R&D were NNI, NNUK, NNSA and NN Ireland. These were known as Integrated Entities or, in transfer pricing terms, Residual Profit Entities ("RPEs") due to their participation from 2001 in a residual profit pool in connection with Nortel's transfer pricing arrangements[7]. Other operating companies performed sales and distribution functions and were known as Limited Risk Distributors or Entities ("LREs").

19 R&D was performed at labs around the world. The advanced technology primary research which was intended to develop novel, cutting edge intellectual property technologies was performed mostly in NNL laboratories in Ottawa, which also did R&D for various lines of business. From 2000 to 2009 NNL accounted on average for just under half of all R&D expenditures, more in the latter years than the earlier years. NNI accounted for 38 to 42% and EMEA accounted for 16 to 20% in the earlier years and 11.7 % from 2005 to 2009. The R&D was shared throughout the Nortel Group as needed by the lines of business and customer needs in the various regions and countries.

20 Because R&D was the primary driver of Nortel's value and profit, the residual profits of Nortel, after payment of fixed rates of return to all Nortel companies for sales and distribution functions, were paid to the RPEs under a Master Research and Development Agreement ("MRDA") in accordance with a residual profit split method ("RPSM") based on each RPE's expenditure on R&D relative to the R&D expenditure of all RPEs.

21 Under the MRDA, NNL was the legal owner of the Nortel intellectual property and each RPE other than NNL was granted an exclusive license by NNL to make and sell Nortel products in its territory using or embodying Nortel intellectual property developed by Nortel companies anywhere in the world and a non-exclusive license to do so in territories that were not exclusive to an RPE. What the ownership rights of NNL were and what the license rights were that were granted in the MRDA are highly contested. Also contested is the role that the MRDA should play in this allocation proceeding.

Bankruptcy filings

22 Beginning around 2001, the burst of the dot-com bubble had a severe effect on the global economy and on the telecommunications industry in particular, including Nortel. Market forces led

to a decline in Nortel's revenues and market share, and a decline in customer demand for Nortel's products. Subsequently, Nortel was faced with accounting issues which impacted Nortel's credit rating and its cost of financing and required Nortel to restate its financial statements for the fiscal years 2000 to 2005. The rating downgrades affected Nortel's access to capital markets and cost of financing for some years. The fortunes of Nortel improved for a few years but for various reasons, including the financial meltdown in the fall of 2008, Nortel saw its business decline in the two profitable lines of business that it was operating.

23 In light of the impact of the deteriorating market conditions and weakening customer commitments on Nortel's financial outlook, Nortel made the decision to commence formal bankruptcy and insolvency proceedings in Canada, the U.S. and England (respecting various EMEA entities) on January 14, 2009.

24 On January 14, 2009 NNC, NNL, the wholly owned subsidiary of NNC which was its operating subsidiary and a number of other Canadian corporations filed for protection under the CCAA. On the same date, Nortel Network Inc. ("NNI"), the principal US subsidiary of NNL, and a number of other US corporations filed for protection under chapter 11 of the US Bankruptcy Code and Nortel Networks UK Limited ("NNUK"), the principal UK subsidiary of NNL, and certain of their subsidiaries (the "EMEA Debtors") save the French subsidiary Nortel Networks S.A. ("NNSA") were granted administration orders under the *UK Insolvency Act, 1986.* On the following day, a liquidator of NNSA was appointed in France pursuant to Article 27 of the European Union's Council Regulation (EC) No 1346/2000 on Insolvency Proceedings in the Republic of France.

25 Subsequent to the filing date, certain other Nortel subsidiaries have filed for creditor protection or bankruptcy proceedings in the local jurisdiction in which they are located. Certain solvent indirect subsidiaries of NNUK are not in administration, but are represented in these proceedings by the Joint Administrators with respect to the allocation issues.

Decision to liquidate

26 The initial intent on filing was to attempt to restructure the business and downsize it by focusing on Nortel's legacy CDMA (Code Division Multiple Access) wireless business and a potential business based on LTE (Long-Term Evolution) wireless technology with all other Nortel business lines being sold. However, Nortel's major customers did not support this plan and advised they were not prepared to provide new contracts to Nortel for this purpose. As well, it became clear that it would not be possible for Nortel to obtain the funding that would have been required to restructure around a CDMA business.

27 In June 2009, management and the Debtor Estates collectively determined that the best means to maximize value for its creditors was to sell Nortel's lines of business and other assets and to commence a liquidating insolvency. No party in these proceedings has suggested that it was a viable option to restructure along geographic lines or for a country-specific entity to independently continue in Nortel's business.

Interim Funding and Settlement Agreement ("IFSA")

28 From the petition date of January 14, 2009, NNL incurred significant expenses to preserve the value of the business, including R&D expenses, and it was experiencing negative cash flow. It had not received any transfer pricing payments from its subsidiaries under the MRDA as a result of the insolvency proceedings.

29 It was evident that there would be significant issues among the parties as to whom the proceeds of the sale of Nortel's assets should be paid. The parties appreciated that if determining the allocation of proceeds from Nortel's assets were a precondition to their sale, sales would be substantially delayed, and the value of the assets would depreciate, resulting in less money for all creditors. Avoiding a dispute during the sale processes about how to allocate the proceeds allowed the parties to obtain the highest monetary value for the assets being sold.

30 On June 9, 2009, the US Debtors (excluding NN CALA, which had not yet filed for bankruptcy), the Canadian Debtors and the EMEA Debtors (excluding NNSA, which later acceded to the agreement) entered into the Interim Funding and Settlement Agreement ("IFSA") to address both interim funding of NNL as well as principles under which collaborative sales of Nortel's businesses and assets could take place.

31 The IFSA provided for a payment by NNI to NNL of $157 million in full settlement of any transfer pricing and other claims NNL might have had against NNI for the period from the petition date through September 30, 2009. The parties also agreed:

(a) to cooperate in the anticipated sales of the Nortel Group's assets;

(b) that their execution of sale documentation or the closing of a sale transaction would not be conditioned upon reaching agreement either on allocation of the sale proceeds or on a binding procedure for determining the allocation question;

(c) that the sale proceeds would be deposited into escrow, and that there would be no distribution out of escrow without either the agreement of all of the selling debtors or the determination of any dispute relating thereto by the relevant dispute resolver;

(d) that in order to facilitate the lines of business sales, the U.S. and EMEA Debtors would enter into appropriate license termination agreements which would provide for the termination of the license rights granted by NNL under the MRDA; termination or relinquishment of a license would be deemed a sale with the licensed participants each being deemed a seller; and

(e) that the agreement would not have any impact on the allocation of proceeds to any Debtor from any asset sale and would not prejudice a party's rights to seek its entitlement to the proceeds from any sale.

32 The US and Canadian Courts entered orders approving the IFSA following a joint hearing on June 29, 2009.

33 On December 23, 2009 the Canadian and U.S. Debtors signed a Final Canadian Funding and Settlement Agreement (the "FCFSA") under which NNI agreed to pay NNL $190.8 million in full and final settlement of all claims that NNL might have against NNI. Further, NNL granted NNI an allowed $2 billion unsecured claim in NNL's CCAA proceedings ranking pari passu with other pre-petition unsecured claims against NNL, with such claim not being subject to offset or reduction.

This claim had resulted from the tax authorities reviewing requests by the parties for approval of their transfer pricing arrangements. In 2009 NNL and NNI were advised that an agreement between the CRA and IRS sought a reallocation of income from NNL to NNI in the amount of U.S. $2 billion for the tax years ending 2001 to 2005. The tax authorities did not specify on what basis the $2 billion figure was calculated. The FCFSA, including the $2 billion admitted claim of NNI against NNL, was approved by the Canadian Court on January 21, 2010 and by the U.S. Court on the following day.

Asset sales

34 With the IFSA framework in place, the Debtor Estates embarked on a process that resulted in a series of sales of the various business lines, which occurred from mid-2009 through late 2010, with the last transaction closing in March 2011. The total proceeds were approximately $3.285 billion. There remains approximately $2.85 billion of that amount now available to be allocated.

35 In order to sell the lines of businesses separately, Nortel engaged in a "carve-out process" to identify the bundle of assets, rights and obligations that would have to be conveyed in each sale to enable the lines of business to function on a stand-alone basis.

36 An important aspect of the carve-out process was the identification of which IP rights, principally patent rights, needed to be conveyed. Each prospective purchaser of a business line wished to obtain as many patents as possible as part of each sale transaction and, conversely, the Nortel sellers wanted to ensure that the only patents transferred were those incorporated exclusively or principally in the business line in question so as to retain value within Nortel and not to jeopardize the ability to sell the other business lines that might require rights to the same patents.

37 Ultimately, those patents that were "predominantly used" in any given line of business were transferred to the purchaser of that line of business as part of the transaction. In the end, 2,700 patents were transferred as part of the business line sales.

38 For all other patents that were used in each line of business but not predominantly used, a non-exclusive license was granted to the purchaser for use of those patents in the operations of the particular business line being purchased.

39 By the time that all of the business sales were completed in March 2011, Nortel had no remaining operating businesses. What it did retain was a residual patent portfolio consisting of approximately 7000 patents and patent applications. These were principally patents and patent applications that were not used in any of the lines of business and therefore were not subject to licenses to the business sale purchasers. In addition, the residual IP portfolio included patents used by multiple lines of businesses and licensed to the purchasers of those lines of businesses.

40 On April 4, 2011, after significant negotiations with two prospective purchasers, certain Nortel entities (including NNC, NNL, NNI and NNUK) entered into a stalking horse asset sale agreement with a wholly owned subsidiary of Google Inc. with a purchase price of $900 million.

41 An auction was held at the end of June 2011, and the residual patent portfolio was ultimately sold to Rockstar Bidco, LP, a single purpose entity backed by a consortium of major technology companies (Apple, Microsoft, Ericsson, Blackberry, Sony and EMC), for $4.5 billion.

Position of the parties

42 In this case the Monitor is acting under what is now referred to as a "super monitor" order of October 3, 2012 in which the Monitor was authorized to exercise any powers which may be exercised by a board of directors of any of the applicants, which includes NNC and NNL. This order occurred after NNC and NNL were left without any board of directors or management and it was necessary for the Monitor to be appointed to advance the interests of NNL and NNC in this CCAA proceeding. While I will refer to the Monitor, I do so in recognition that the Monitor is advancing the position of the Canadian Debtors in this litigation.

43 The intellectual property of Nortel represented by far the largest portion of the assets sold. The Rockstar sale of the residual IP generated $4.5 billion. The lines of business generated $3.285 billion of which approximately $2.85 billion is now available. Intellectual property was a substantial part of the assets of the business lines that were sold, although the experts differed as to its value.

44 The parties and their experts for the most part relied on their interpretation of the MRDA in support of their allocation positions for the proceeds from intellectual property for both the Rockstar sale and the lines of business sales. Two parties, the UKPC (the UK pension claimants, being the trustee of the UK pension plan, and the board of the UK Pension Protection Fund) and the Canadian Creditors Committee[8] contended that the MRDA should not govern the allocation and that a pro rata allocation based on a *pari passu* distribution to all creditors should be used to allocate the lockbox funds.

45 It is necessary therefore to consider the MRDA and whether it should govern the allocation.

The MRDA

46 The parties look to the rights of the various Nortel entities to intellectual property under the MRDA as a central issue in this proceeding. What these rights are is contested. Many of its terms have been excruciatingly parsed. I will first deal with the meaning of the MRDA as an operating agreement. I will then deal with the issue as to whether it applies, or was intended to apply, to the allocation of the Nortel assets after the world-wide insolvency of Nortel.

47 The MRDA and its predecessor Cost Sharing Agreements[9] ("CSA") were developed for and driven by transfer pricing concepts. Transfer pricing is the act of assigning a monetary value, or price, to movements of resources or economic contributions that occur within a multinational enterprise across different taxing jurisdictions. Against the risk that companies attempt to use transfer pricing to increase operating income (and therefore taxable income) in jurisdictions with low income tax rates and correspondingly to decrease operating income in high-tax jurisdictions, tax authorities around the world have instituted regulations governing intercompany transfer pricing. These regulations centre on the arm's length principle. The arm's length principle necessitates that intercompany transactions be priced in a manner consistent with the way in which similarly situated uncontrolled parties bargaining at arm's length would price the transactions i.e., within an arm's length range.

48 Dr. Eden, a transfer pricing expert who testified on behalf of the U.S. Debtors, well described in her report the way in which transfer pricing agreements are made in light of the fact that governments have developed a dense regulatory framework for transfer pricing due to worries about the potentially negative impacts that transfer pricing can have on government tax and customs duty revenues. The setting of transfer pricing policies for corporate income tax purposes of a multinational enterprise (MNE) is a highly regulated, data-driven and fact-intensive activity dominated by professionals. The establishment of an MNE's transfer pricing policy typically involves not only

MNE group in-house staff, but also accountants, economists, lawyers, tax experts and other consultants. Moreover, an MNE's transfer pricing policy may involve the input of revenue authorities through an advance pricing agreement (APA) procedure.

49 All of this applied to Nortel and much evidence was given by tax people as to the process by which the MRDA was made and changed. Evidence was also given by some of them as to their view of the meaning of the agreement, the admissibility of which is contested.

(i) Governing law of the construction of the contract

50 The MRDA is by its terms to be construed in accordance with and governed by the law of Ontario. The same applied to the predecessor CSAs.

51 A number of authorities have been cited. A brief consideration of them is required in light of the various arguments made about the MRDA, particularly as it involves the principles of interpreting commercial contracts, what can be looked at when considering the factual matrix of the agreement and the use of recitals in an agreement in the interpretive process.

52 Winkler C.J.O. articulated the test for construing a commercial contract in *Salah v. Timothy's Coffees of the World Inc.* (2010), 74 B.L.R. (4th) 161 as follows:

> **16** The basic principles of commercial contractual interpretation may be summarized as follows. When interpreting a contract, the court aims to determine the intentions of the parties in accordance with the language used in the written document and presumes that the parties have intended what they have said. The court construes the contract as a whole, in a manner that gives meaning to all of its terms, and avoids an interpretation that would render one or more of its terms ineffective. In interpreting the contract, the court must have regard to the objective evidence of the "factual matrix" or context underlying the negotiation of the contract, but not the subjective evidence of the intention of the parties. The court should interpret the contract so as to accord with sound commercial principles and good business sense, and avoid commercial absurdity. If the court finds that the contract is ambiguous, it may then resort to extrinsic evidence to clear up the ambiguity.

53 In *Kentucky Fried Chicken v. Scott's Food Services Inc.* (1998), 41 B.L.R. (2d) 42 (Ont. C.A.) Goudge J.A. stated the following regarding the interpretation of a commercial agreement at para. 27

> Where, as here, the document to be construed is a negotiated commercial document, the court should avoid an interpretation that would result in a commercial absurdity. [*City of Toronto v. W.H. Hotel Ltd.* (1966), 56 D.L.R. (2d) 539 at 548 (S.C.C.)]. Rather, the document should be construed in accordance with sound commercial principles and good business sense; [*Scanlon v. Castlepoint Development Corporation et al.* (1992), 11 O.R. (3d) 744 at 770 (Ont.C.A.)]. Care must be taken, however, to do this objectively rather than from the perspective of one contracting party or the other, since what might make good business sense to one party would not necessarily do so for the other.

54 I take the principles in *Kentucky Fried Chicken* and in *Salah,* the latter adopted by Cronk J.A. in *Downey v. Ecore International Inc.* 2012 ONCA 480 and by Juriansz J.A. in *Ariston Realty Corp. v. Elcarim Inc.* 2014 ONCA 737, as the applicable principles governing this case. See also *Unique Broadband Systems Inc. (Re)* 2014 ONCA 538 at para. 88.[10]

55 The factual matrix of the contract is to be considered. What may be considered was expressed in *Kentucky Fried Chicken* as follows:

> **25** ...While the task of interpretation must begin with the words of the document and their ordinary meaning, the general context that gave birth to the document or its "factual matrix" will also provide the court with useful assistance. In the famous passage in *Reardon Smith Line Ltd. v. Yngvar Hansen-Tangen*, [1976] 1 W.L.R. 989 at 995-96 (H.L.) Lord Wilberforce said this:
>
>> No contracts are made in a vacuum: there is always a setting in which they have to be placed. The nature of what is legitimate to have regard to is usually described as "the surrounding circumstances" but this phrase is imprecise: it can be illustrated but hardly defined. In a commercial contract it is certainly right that the court should know the commercial purpose of the contract and this in turn presupposes knowledge of the genesis of the transaction, the background, the context, the market in which the parties are operating.
>
> **26** The scope of the surrounding circumstances to be considered will vary from case to case but generally will encompass those factors which assist the court "... to search for an interpretation which, from the whole of the contract, would appear to promote or advance the true intent of the parties at the time of entry into the contract." *Consolidated Bathurst Export Ltd. v. Mutual Boiler and Machinery Insurance Co.,* [1980] 1 S.C.R. 888 at 901.

56 More recently, Rothstein J. in *Sattva Capital Corp. v. Creston Moly Corp.* 2014 SCC 53 referred to the use of surrounding circumstances and cautioned as to the extent they can be considered:

> **57** While the surrounding circumstances will be considered in interpreting the terms of a contract, they must never be allowed to overwhelm the words of that agreement (*Hayes Forest Services*, at para. 14; and Hall, at p. 30). The goal of examining such evidence is to deepen a decision-maker's understanding of the mutual and objective intentions of the parties as expressed in the words of the contract. The interpretation of a written contractual provision must always be grounded in the text and read in light of the entire contract (Hall, at pp. 15 and 30-32). While the surrounding circumstances are relied upon in the interpretive process, courts cannot use them to deviate from the text such that the court effectively creates a new agreement (*Glaswegian Enterprises Inc. v. B.C. Tel Mobility Cellular Inc.* (1997), 101 B.C.A.C. 62).

> 58 The nature of the evidence that can be relied upon under the rubric of "surrounding circumstances" will necessarily vary from case to case. It does, however, have its limits. It should consist only of objective evidence of the background facts at the time of the execution of the contract (*King*, at paras. 66 and 70), that is, knowledge that was or reasonably ought to have been within the knowledge of both parties at or before the date of contracting. Subject to these requirements and the parol evidence rule discussed below, this includes, in the words of Lord Hoffmann, "absolutely anything which would have affected the way in which the language of the document would have been understood by a reasonable man" (*Investors Compensation Scheme*, at p. 114). Whether something was or reasonably ought to have been within the common knowledge of the parties at the time of execution of the contract is a question of fact.

57 It is clear that the factual matrix that can be considered may not include evidence of the subjective intent of a party or what a party believed a contract to mean. See *Sattva, supra*, at para. 59. It may also not include evidence of negotiations or create an ambiguity where none exists in an agreement. See also *Primo Poloniato Grandchildren's Trust (Trustee of) v. Browne* (2012), 115 O.R. (3d) 287 in which Feldman J.A. stated:

> 71 While the scope of the factual matrix is broad, it excludes evidence of negotiations, except perhaps in the most general terms, and evidence of a contracting party's subjective intentions: Geoff R. Hall, *Canadian Contractual Interpretation Law*, 2d ed. (Markham: LexisNexis, 2012), at p. 27. As the cases above suggest, the factual matrix includes only objective facts known to the parties at or before the date of the agreement, and what is common to both parties: Hall, p. 30. Hall goes on to state that while the factual matrix can "be used to clarify the parties' intentions as expressed in a written agreement, it cannot be used to contradict that intention, create an ambiguity which otherwise does not exist in the written document, or have the effect of making a new agreement": p. 31 (footnotes omitted). Ultimately, the words of the agreement are paramount.

58 The recitals in the MRDA are the subject of debate in this case. A clear statement of how recitals may be used in the interpretation of an agreement can be found in *Elliott Estate (Re)*, 1962 O.J. No. 164 (C.A.); aff'd [1963] S.C.R. 305. In that case, Kelly J.A. stated that a recital could be used only if there is an ambiguity in the operative parts of the agreement and the recital is clear. He stated:

> 11 I turn therefore to consider to what extent the recital may be used to overcome the patent deficiencies of clauses 6 and 7 and in fact of the whole operative parts of the agreement. In the first instance it must be borne in mind that a recital is not a necessary part of a document and its use in the interpretation of the document as a whole is strictly limited.
>
> > "The reciting Part of a Deed is not at all a necessary Part either in Law or Equity. It may be made use of to explain a Doubt of the Intention and Meaning of the Parties but it hath no Effect or Operation. But when it

> comes to limit the estate, there the Deed is to have its Effect according to what Limitations are therein set forth."

Per Holt, C.J., *Bath and Mountague's Case* (1693) 3 Cas. in Ch. 55 at 101; 22 E.R. 963 at 991. An oft quoted statement of the extent to which reference may be had to recitals is contained in the judgment of Lord Esher, M.R. in *Ex Parte Dawes. In Re Moon*, (1886) 17 Q.B.D. 275 at p. 286:

> "Now there are three rules applicable to the construction of such an instrument. If the recitals are clear and the operative part is ambiguous, the recitals govern the construction. If the recitals are ambiguous, and the operative part is clear, the operative part must prevail. If both the recitals and the operative part are clear, but they are inconsistent with each other, the operative part is to be preferred."

It is to be noted that the qualifying condition for the use of a recital in the interpretation of the operative parts is that there must be ambiguity in the operative parts; in such a case the preferred meaning to be given to the operative words should be that consistent with the intention expressed in the recital, provided that the words of the operative part are by themselves capable of such an interpretation. *MacKenzie v. Duke of Devonshire*, (1896) App. Cas. 400; *Ex Parte Dawes. In Re Moon, Supra*; *In re Sugden's Truts, Sugden v. Walker*, (1917) 2 Ch. 92. It is essential, however, that the construction to be placed upon the operative part in the light of the recital be a construction which the words themselves of the operative part are capable of bearing. Where, however, the operative parts of a document, due to the lack of appropriate words, are incapable of a construction which will fulfil the intention expressed in recitals, the recital may not be used for the purpose of reading into the operative clause a meaning which it is incapable of conveying when considered by itself.

59 It was held in *PUC v. Distribution Inc. v. Brascan Energy Marketing Inc.*, 2008 ONCA 176, that an elevation of a recital to a mutual promise or operative provision was an error.

60 *Eli Lilly & Co. v. Novopharm Ltd.*, [1998] 2 S.C.R. 129 at para. 57, in which Iacobucci J. in discussing the meaning of an agreement referred to the recitals, was referred to in argument. Iacobucci J. did not discuss the principles to be used in considering recitals. *Sistem v. Kyrgyz Republic,* 2012 ONSC 4983, has also been referred to in argument, a decision in which I did not refer to the principles to be used in considering recitals in interpreting contracts. I consider the decision in *Sistem* to be consistent with the principles enunciated by Kelly J.A. in *Elliott Estate.* I do not see either *Eli Lilly* or *Sistem* establishing any different criteria for the use of recitals from *Elliott Estate.*

61 I turn now to the interpretation of the MRDA and the rights accorded in it keeping these interpretive principles in mind.

(ii) Position of the parties

62 The essential differences in allocation positions advanced by the parties flow from the different manner in which each characterizes the terms of the MRDA, the interests held by the parties in Nortel's IP, and the applicability of terms of the MRDA to the value ascribed to various assets.

63 The Monitor, supported by the CCC, contends that under the MRDA, NNL owned the IP and the interests of NNI and the other participants to the MRDA were restricted to certain exclusive and non-exclusive license rights granted to them by NNL pursuant to the terms of the MRDA. The Monitor says that the license rights were not unlimited, as they did not cover all rights in the IP in question, but rather covered only a subset (albeit a substantial subset) of the IP rights, on certain terms, all of which have valuation implications. In particular, the Monitor says that the license rights granted to NNI and the other licensed participants were not all rights to the IP but were subject to "field of use" restrictions that gave the licensees the right to use the IP to make, use or sell "Products" as defined in the MRDA, which meant products, software or services that were made or sold by, or for, any of the licensees. This meant that the Products must have been created or marketed by or for the Nortel Group. No product that was part of a third party's business rather than the business of Nortel could fall within the definition of Products. While the license gave the licensees the right to sublicense, this could not permit the licensees to sublicense what they did not have.

64 The Monitor's position, supported by the CCC, is that what was sold in the Rockstar sale of IP was the ownership of residual patents and patent applications owned by NNL. The purchasers would not have bought the residual IP to make Nortel products, and that as the license rights held by NNI and the other licensees would not have permitted them to sublicense to the Rockstar consortium the right to use the IP for the Rockstar consortium's own purposes, the proceeds of the Rockstar sale belong to NNL.

65 The position of NNI, supported by the other U.S. interests, asserts that each of NNI and the other licensees held all of the rights and all of the value in the IP in their respective exclusive territories as defined in the MRDA. The U.S. Debtors assert that the license rights NNI held were not subject to any field of use or scope restriction or limitation, resulting in an assertion that all of the economic value in the IP in the exclusive territory belonged to the licensee. They contend that the legal title held in the IP under the MRDA was a purely "bare" legal title with no monetary value. They also rely on a right to sue for damages in the U.S. for infringement of NN Technology by others.

66 The position of the EMEA debtors is that each of the parties to the MRDA jointly owned all of the IP in proportion to their financial contributions to research and development, and that all share in the sale proceeds attributable to IP in those same proportions. The joint ownership is said to arise independent of, but recognized in, the MRDA.

(iii) Analysis

(a) The meaning of the exclusive license

67 The agreement is headed MASTER R&D AGREEMENT. It was entered into on December 22, 2004 with an effective date of January 1, 2001 and states that it confirms and formalizes the operating arrangements of the participants as and from that date. It provided that NNL was the legal owner of the NN Technology (the IP), and it contained grants of licenses from NNL to the other participants, referred to as the Licensed Participants. Each Licensed Participant was given an exclusive license for its territory and a non-exclusive license for those parts of the world other than Can-

ada and where the Licensed Participants had their exclusive territory. The exclusive territory for NNI was the U.S. and Puerto Rico, for NNUK was the United Kingdom, for NNSA was France and for Nortel Ireland was the Republic of Ireland.

68 At its core, so far as the ownership and licensing of the IP is concerned are articles 4(a) and 5(a) and (b). The original language remained in substance but was amended from time to time. These articles as amended are as follows:

Article 4 -- Legal Title to NN Technology

(a) Except as otherwise specifically agreed, legal title to any and all NN Technology whether now in existence or hereafter acquired, or developed pursuant to the terms of this Agreement, shall be vested in NNL. In consideration therefor, NNL agrees to enter into an Exclusive License and a Non-Exclusive License with each of the Licensed Participants as set forth in Article 5.

Article 5 -- Grant of Exclusive Licenses by NNL

(a) To the extent of its legal right to do so, and subject to the rights of relevant third parties, NNL hereby:

(i) continues to grant to each Licensed Participant an exclusive, royalty-free license, including the right to sublicense, which except as hereinafter provided shall be in perpetuity, rights to make, have made, use, lease, license, offer to sell, and sell Products using or embodying NN Technology in and for the Exclusive Territory designated for that Licensed Participant, and all rights to patents, industrial designs (or equivalent) and copyrights, and applications therefor, and technical know-how, as necessary or appropriate in connection therewith ("Exclusive License"); and

(ii) grants to each Licensed Participant, as of January 1, 2009 (the "Non-Exclusive License Effective Date"), a non-exclusive, royalty-free license, including the right to sublicense, which except as hereinafter provided shall be in perpetuity, rights to make, have made, use, lease, license, offer to sell, and sell Products using or embodying NN Technology in and for the Non-Exclusive Territory, and all rights to patents, industrial designs (or equivalent) and copyrights, and applications therefor, and technical know-how, as necessary or appropriate in connection therewith ("Non-Exclusive License").

69 To support their differing interpretations of these provisions, the parties augment to some extent their arguments by reference to other provisions in the MRDA. It will be necessary to deal with these. As can be seen from article 5(i), NNL "continues to grant", a reflection of the fact that prior to the MRDA, the parties were governed by Cost Sharing Agreements (CSAs)[11]. Recitals to the MRDA make this clear:

WHEREAS legal title to all NN Technology is held in the name of NNL;

> WHEREAS each Licensed Participant held and enjoyed equitable and beneficial ownership of certain exclusive rights under NT Technology for a Specified Territory pursuant to the Amended Research and Development Cost Sharing Agreement entered into on January 1, 1992, and it is the intent of NNL and the Licensed Participants that the Licensed Participants continue, as of the effective date of this Agreement, to hold and enjoy such rights;

70 In considering the various interpretations of the MRDA put forward by the parties, it is helpful to compare those provisions with the earlier CSA provisions. Under the CSA, the parties split the costs of R&D by a certain formula. That agreement did not purport to split profits in any way. However, the tax authorities made it clear that they no longer would permit a cost sharing arrangement at Nortel and instead wanted an arrangement whereby profits would be shared among the participants by a residual profit split method (RPSM) that allocated profits according to the amount each participant spent on R&D. Relevant recitals in the MRDA that were not contained in the previous CSA are:

> WHEREAS each Participant bears the full entrepreneurial risks and benefits for the Nortel Networks business;
>
> WHEREAS each Participant has performed, in the past, and intends to continue to perform R&D Activity with respect to the Nortel Products;
>
> WHEREAS each Participant desires to avoid the duplication of R&D Activity;
>
> WHEREAS each Participant believes that it is appropriate that each Participant should benefit from its contribution to R&D activity commensurate with the value of its contribution to that R&D activity in the context of the manner in which the Nortel Networks business is conducted and that the residual profit split methodology (RPSM) is the best arm's length measure, in the circumstances of NNL and the Participants, of such contributions with reference to such benefits;
>
> WHEREAS this Agreement reflects the Participants' intent and agreement since January 1, 2001 to enter a license arrangement with the Licensed Participants, and the Participants have operated from January 1, 2001 in accordance with the terms set forth herein;
>
> WHEREAS Participants acknowledge that as a result of a collective review by the Canadian Customs and Revenue Agency, the US Internal Revenue Service, and the UK Inland Revenue regarding the application of the RPSM, the calculation of the RPSM as set forth in Amended Schedule A may be amended which amendments would require the consent of the Participants;

71 These recitals and the RPSM method contained in the MRDA were driven by transfer pricing considerations. The language, for example, that each Participant (NNL and the Licensed Participants) bears the full entrepreneurial risks and benefits for the Nortel Networks business was not in the prior CSA and was part of the rationalization adopted to support a RPSM.

72 The MRDA provided in article 2 that each Participant would perform R&D at a level consistent with past practices and share the results of its R&D with the other participants. Article 3 provided payment for the R&D as follows:

Article 3 -- R&D Activity Payments

(a) For and as a consequence of the performance of R&D Activity, each Participant shall be entitled to receive a payment in an amount equal to the allocation determined under the RPSM (the "R&D Allocation") as the measure of the benefit to which it is entitled commensurate with its performance of, and contribution to, R&D Activity.

(b) Each Participant hereby accepts and agrees to make the payment determined under the RPSM in Amended Schedule A[12] as representing such Participant's share of the R&D Allocation.

(c) The R&D Allocation will be computed pursuant Amended Schedule A which sets forth the basis of the RPSM as originally proposed to the Revenue Authorities. The Participants understand that the RPSM is the subject of review, discussions and negotiations with the Revenue Authorities. The Participants agree to amend this Agreement and to adjust the RPSM to the extent necessary to reflect any negotiated determination with the Revenue Authorities as to the final R&D Allocation.

73 The U.S. Debtors and EMEA take the position that the legal title that is vested in NNL under article 4 of the MRDA is bare legal title given to NNL for administrative convenience to enable it to administer all NN Technology and that the licensed participants own the equitable and beneficial interest in the NN Technology. It draws on the recital that provides:

> WHEREAS each Licensed Participant held and enjoyed equitable and beneficial ownership of certain exclusive rights under NT Technology[13] for a Specified Territory pursuant to the Amended Research and Development Cost Sharing Agreement entered into on January 1, 1992, and it is the intent of NNL and the Licensed Participants that the Licensed Participants continue, as of the effective date of this Agreement, to hold and enjoy such rights;

74 I do not see this recital as clearly stating that a Licensed Participant has equitable and beneficial ownership of the NT Technology. It states that a Licensed Participant held equitable and beneficial ownership of "certain exclusive rights under NT Technology" and would continue to have such rights. The recital does not say what the "certain exclusive rights" were and it is just as consistent with those rights being license rights rather than ownership rights in the technology. As well, having equitable and beneficial ownership of certain exclusive rights "<u>under</u> NT Technology" would seem to be something different from having equitable and beneficial ownership of certain exclusive rights "of" or "in" the NT Technology.

75 In the CSA referred to in the recital, the language used is as follows:

ARTICLE 4

LEGAL TITLE TO
NT TECHNOLOGY

> The Parties hereto acknowledge that, except as otherwise specifically agreed, legal title to all NT Technology whether now in existence or developed pursuant to the terms of this Cost Sharing Agreement, except patents owned by Participant [Northern Telecom Inc., now NNI] on January 1, 1980, shall be vested in Northern Telecom [now NNL]. With respect to patentable inventions and copyrightable property encompassed by NT Technology, Northern Telecom shall have the exclusive right but not the obligation to file and prosecute applications in its name for patent or copyright protection in every country of the world. Participant shall execute or cause to be executed such documents reasonably requested by Northern Telecom as may be necessary or desirable to give effect to the foregoing. (Underlining added).

76 The exception in this provision for patents owned by Northern Telecom Inc., now NNI, suggests that the legal title vested in Northern Telecom (now NNL) was ownership rather than bare legal title. Otherwise there would have been no purpose in excluding the patents owned by Northern Telecom Inc. It would not have been necessary.

77 In article 6 of the CSA, dealing with confidential information, it is stated:

> Participant acknowledges that Northern Telecom is the legal owner of the NT Technology developed pursuant to this Cost Sharing Agreement and that the NT Technology is proprietary and constitutes a trade secret. Participant shall hold the NT Technology in confidence and only make use of or disclose it as permitted by this Cost Sharing Agreement.

78 This provision refers to Northern Telecom being the "legal owner". This is consistent with the language of article 4 of the CSA. If, as stated in the recital to the MRDA, it was the intent of NNL and the Licensed Participants that the Licensed Participants would continue under the MRDA to hold and enjoy such rights as they held under the CSA, those rights would not include legal ownership of the NN Technology.

79 NNI also relies on language in Schedule A of the MRDA to assert its beneficial ownership of the NN Technology. It provides in part:

Calculation of Arm's Length R&D
Allocation to each Participant

> The purpose of this section is to provide a brief summary of Nortel's transfer pricing policy and to provide clarity as to how each Participant is to be compensated under this Agreement.
>
> The current transfer pricing methodology is the residual profit split method ("RPSM") which was adopted by the Participants at the request of the tax authorities as the most appropriate method for determining the arm's length compensation to each of the Participants for the R&D Activity to be provided pursuant to the Master R&D Agreement. The RPSM acknowledges the fact that the key

> profit driver in the Nortel business is the development and maintenance of rapidly depreciating intellectual property ("IP").
>
> Accordingly, the R&D Allocation provided to Participants under the RPSM reflects the fact that the Participants bear the full entrepreneurial risk of the Nortel business such as the risks attendant with the substantial and continuous development and ownership of the NN Technology. Mathematically, the RPSM accords the Participants all the upside risk in the Nortel business as well as the downside risk. (Underlining added).

80 Schedule A is part of the MRDA. I do not, however, read it as granting rights. The rights are granted in the operative provisions of the MRDA. Schedule A states at the outset that its purpose is to give a brief summary of Nortel's transfer pricing policy and to provide clarity as to how each participant is to be compensated. Schedule A provides in some detail how the residual profit is to be calculated and split amongst the Participants. Stating that Participants bear risks such as risks attendant with the development and ownership of the NN Technology does not state that ownership of the technology is being granted. What the Licensed Participants were granted in the MRDA were license rights.

81 Various dictionary definitions were resorted to in arguing what the meaning of "legal title" to the NN Technology was that was vested in NNL under article 4 of the MRDA. In the end, I do not think it necessary to get into that debate. NNL had ownership of NN Technology to the extent that NN Technology was not licensed to the Licensed Participants. Rights in inventions were assigned by the inventors to NNL and NNL applied for the patents and was named as owner of them. It was NNL who granted licenses to the Licensed Participants. NNUK, for example, did not provide a license to NNI for IP developed by NNUK. It was NNL that did so. Although NNL had the exclusive right to the NN Technology in Canada under the MRDA, the MRDA did not grant any license to NNL. That was recognition that it was NNL that owned the NN Technology.

82 A licensee does not enjoy property rights. Its rights are contractual. A licence is merely a permission to do that which would otherwise amount to trespass. See *Euro-Excellence Inc. v. Kraft Canada Inc.*, [2007] S.C.R. 20 at para. 27. A licensee's rights are not necessarily equivalent to those of the patentee; rather, they are limited to, and qualified by, the express terms of the license. See *Eli Lilly & Co. v. Novopharm Ltd.*, [1998] 2 S.C.R. 129 at para. 49. It is the determination of what those license rights were that were granted to the Licensed Participants in the MRDA that is important because it is those license rights that were given up by Licensed Participants to permit the business line sales and the sale of the residual IP to Rockstar.

83 The grant of the exclusive license in the MRDA in article 5(i) is:

> ...NNL hereby:
>
> (i) continues to grant to each Licensed Participant an exclusive, royalty-free license, including the right to sublicense, which except as hereinafter provided shall be in perpetuity, rights to make, have made, use, lease, license, offer to sell, and sell Products using or embodying NN Technology in and for the Exclusive Territory designated for that Licensed Participant, and all rights to patents, industrial designs (or equivalent) and copyrights, and applications therefor, and technical

> know-how, as necessary or appropriate in connection therewith (Exclusive License") (Underlining added);

84 The license is not a license of NN Technology, but rather a license "to make... and sell Products using or embodying NN Technology". Thus the MRDA definition of "Products" is of central importance and the Monitor says that "Products" is defined to mean products, software or services that were made or sold by, or for, NNL and the Licensed Participants. The Monitor contends that products not made for NNL or the Licensed Participants, such as products that would be made by the Rockstar consortium members or their licensees are not covered by the license.

85 The definition of "Products" at Article 1(g) of the MRDA is:

> "Products" shall mean all products, software and services designed, developed, manufactured or marketed, or proposed to be designed, developed, manufactured or marketed, at any time by, or for, any of the Participants, and all components, parts, sub-assemblies, features, software associated with or incorporated in any of the foregoing, and all improvements, upgrades, updates, enhancements or other derivatives associated with or incorporated in any of the foregoing. (Underlining added).

86 The U.S. Debtors parse the language of the license grant and contend that the Licensed Participants obtained all of the rights to the NN Technology. They break down the grant of the exclusive license into four clauses as follows:

> NNL hereby:
>
> continues to grant to each Licensed Participant an exclusive, royalty-free license, including
>
> the right to sublicense, which except as hereinafter provided shall be in perpetuity,
>
> rights to make, have made, use, lease, license, offer to sell, and sell Products using or embodying NN Technology in and for the Exclusive Territory designated for that Licensed Participant, and
>
> all rights to patents, industrial designs (or equivalent) and copyrights, and applications therefor, and technical know-how, as necessary or appropriate in connection therewith ("Exclusivc License").

87 The U.S. Debtors stated in their opening brief that the opening grant of an exclusive, royalty-free license in the first clause is not limited by the word "including". They say the word "including" does not create a limitation, that the word "including" follows the words "exclusive, royalty-free license" and thus the words that follow cannot, and do not purport to, limit the broad exclusive licenses granted to the licensed participants under the MRDA. In effect they argue that the opening words before the word "including" created a complete grant of a license without reserve.

88 I cannot accept that argument. The words "continues to grant an exclusive, royalty-free license", on their own, do not say what the license is, or what it is for, or for how long. Given that a

licensee's rights are limited to, and qualified by, the express terms of the license (*Eli Lilly & Co* at para. 49), a license grant of uncertain scope, such as proposed by the U.S. Debtors, would have no meaning. Moreover, the words "in and for the Exclusive Territory designated for that Licensed Participant" appear after "including". On the U.S. Debtors' reading of the license, the territorial limitation would only apply to the license to make Products, and would not apply to a broad exclusive license that they say is already created before one gets to the word "including". It would also mean that the words "in perpetuity" which follow the reference to a sublicense would not apply to the broad exclusive license, which is inconsistent with what the U.S. Debtors say is the case.

89 There would be no commercial purpose in the MRDA granting a broad unrestrictive license and then providing more specific grants in the license that are restricted. For example, the third clause restricts the licensee to selling Products, which contains terms of limitation.

90 The U.S. Debtors also contend that the third clause permits NNI or any other Licensed Participant to make or have made for it Products using NN Technology and that the sublicense rights contained in the second clause are not so limited to Products using NN Technology. I cannot accept that contention. A sublicense could not sublicense more than the licensee had under its license and the second clause could not purport to do so. This argument of the U.S. Debtors relies on its argument that the first clause was a broad unrestrictive grant of a license, which argument I cannot accept.

91 The U.S. Debtors contend that the fourth clause is a free-standing or "catch-all" license grant of all rights to patents etc. unconnected to the license to make, use or sell Products. The language of this provision is:

> all rights to patents, industrial designs (or equivalent) and copyrights, and applications therefor, and technical know-how, as necessary or appropriate in connection therewith ("Exclusive License");

92 The U.S. Debtors say that the concluding words "in connection therewith" refer to the preceding words "technical know-how". The contention of the U.S. Debtors is that this last clause is like the first clause, being a separate grant not limited by the right to make, use or sell Products. The Monitor says that these all of these words in the clause relate to the license to make, use or sell Products and that the words "in connection therewith" do not relate only to the reference to technical know-how.

93 I must say that I find it difficult to accept that the concluding words "in connection therewith" modify only the words "technical know-how". There would be no need for a comma after the words technical know-how". Those words, even if only applicable to the last clause, could apply equally to "industrial designs (or equivalent)" and "applications therefor".

94 I do not find persuasive at all the attempt of the U.S. Debtors to parse the language of the grant of license as they have done. On their reading, there are several different grants of license. Yet at the end of the paragraph are the words "Exclusive License" in parenthesis. There is only one license and the words should be read together harmoniously.

95 The U.S. Debtors make the point that what they refer to as the last clause in the license grant would be superfluous on the reading of the Monitor. That is because the definition of Products and NN Technology includes patents and the other things contained in that last clause. The U.S. Debtors say that because in interpreting a contract one should strive to give meaning to all of its terms, the

last clause should be read as providing rights different from the rights to make, use or sell Products. While this argument on its face has a certain attractiveness, I do not think it right in this case.

96 The grant of license rights in article 5 is one grant. It does not in the paragraph expressly spell out the definition of Product or NN Technology. The draftsman may have thought it prudent to include the final clause. The words "in connection therewith" must be given some meaning and I do not accept the meaning given to them by the U.S. Debtors. I read the words as relating to the grant of a license to make, use and sell Products employing NN Technology, which in my view was the intent of the entire license granted in clause 5(i).

97 The Monitor refers to a statement of Lord Hoffman, no stranger to contract interpretation and a legal giant of his day, in *Beaufort Developments (NI) Ltd. v. Gilbert-Ash NI Ltd,* [1999] A.C. 266 at 274 (H.L.) that arguments of redundancy should be treated with caution. He stated:

> I think, my Lords, that the argument from redundancy is seldom an entirely secure one. The fact is that even in legal documents (or, some might say, especially in legal documents) people often use superfluous words. Sometimes the draftsmanship is clumsy; more often the cause is a lawyer's desire to be certain that every conceivable point has been covered. One has only to read the covenants in a traditional lease to realise that draftsmen lack inhibition about using too many words.

98 In *Long v Delta Catalytic Industrial Services Inc.*, [1998] 6 W.W.R. 792, Fruman J. (as she then was) said much the same thing:

> Some might argue that this interpretation makes the provision redundant...That may well be the case, but it won't be the first time that a repetitive provision has been inserted into an agreement.

99 Redundancy could also be laid at the feet of the U.S. Debtors in their interpretation of the license grant. If their reading is correct, all of the second, third and fourth clauses would be redundant as the first clause was an unrestricted grant of a license. I think in this case redundancy arguments are just that, arguments that do not deal with the commercial purpose of the agreement.

100 An addendum to the MRDA dated December 14, 2007 with effect from January 1, 2006 was made to adopt changes to the terms of the MRDA that had been reflected in the financial statements of the Participants. The first two recitals of this addendum stated:

> Whereas each Participant holds and enjoys equitable and beneficial ownership of NN Technology as defined in the Prior Agreement,
>
> Whereas this Addendum continues each Participant's rights and obligations in the NN Technology,

101 The reason for this addendum was stated in the third recital

> Whereas given changes in the Nortel business, NNL and certain other Participants are seeking governmental approval of modifications to the RPSM.

102 This was the first of two addenda that changed the way of calculating the residual profit split each year from an amortized 30% spend of each Participant each year on R&D to a five year rolling average spend by each Participant on R&D. The operative parts of this addendum did not change the operative terms of the prior MRDA relating to the licence rights granted to the participants. I do not read the first two recitals that "each Participant holds and enjoys equitable and beneficial ownership of NN Technology as defined in the Prior Agreement" and the addendum "continues each Participant's rights ... in the NN Technology" as changing anything with respect to those rights in the prior MRDA. It is how the prior MRDA defines the rights of the participants that is important.

103 Confidentiality provisions are contained in the MRDA. The Monitor contends that because under article 6(a) the licensed participants owe a duty of confidentiality to NNL regarding the NN Technology but NNL does not owe such a duty to the Licensed Participants is an indication of the ownership by NNL of the NN Technology. The U.S. Debtors contend that because exceptions to the duty of confidentiality in article 6(d) give the right to the Licensed Participants to communicate to suppliers, customers and third persons licensing rights to use the NN Technology that they must have been given the authority to license to such third parties.

104 I think too much is made by each side of these confidentiality provisions. There is something perhaps in each side's argument, but I would not read article 6 as expanding on or limiting the ownership or license rights of the NN Technology. That was not its purpose. Regarding article 6(d)(iii), it begs the question as to whom the rights were given to license to third parties, and in light of the evidence of sub-licensing prior to the MRDA, to which I will refer in dealing with surrounding circumstances or the factual matrix, it is clear that NNL was a party to all such sub-licensing and NNI alone never sub-licensed.

105 The U.S. debtors contend that what was intended by IPCo comfortably falls within the definition of a Product and that therefore what was sold to Rockstar embodied rights that NNI had. They contend:

> IPCo was a licensing service business that the Participants proposed to be developed and indeed were actively developing, and which indisputably embodied the entirety of the Patent Portfolio sold to Rockstar, fits comfortably within the plain meaning of a "service" and thus the definition of "Products".

106 I do not agree. IPCo was considered for a time after the insolvency filings in January 2009. It could not be considered to have been part of the operating arrangements of Nortel while it carried on its business or intended to be governed by the MRDA. IPCo was not intended to be a "licensing service" business. The evidence of Sharon Hamilton, which I accept, is that the proposed business of IPCo was to use threatened or actual litigation against technology companies making their own products which arguably used or embodied NN Technology, in an attempt to encourage them to take and pay for a license to NN Technology. That was not a business contemplated in any meaningful way at any time that the MRDA or its predecessor was negotiated or signed.

107 The economic analysis prepared by Horst Frisch in 2002 as part of its work in devising the RPSM for the MRDA referred to Nortel customers choosing Nortel products and services because Nortel is committed to using its R&D resources in providing full pro-active service and support to its customers. A functional analysis for the years 2000 to 2004 sent by Nortel to the tax authorities in 2004 said the same thing. It also stated:

> "Nortel's networking solutions generally bring together diverse networking products from its various product families, and related services, to create either a customized or "off the shelf" solution for customers. Nortel's business consists of the design, development, manufacture, assembly, marketing, sale, licensing, servicing and support of these networking solutions".

108 The definition of Products in the MRDA is:

> "**Products**" shall mean all products, software and services designed, developed, manufactured or marketed, or proposed to be designed, developed, manufactured or marketed, at any time by, or for, any of the Participants, and all components, parts, sub-assemblies, features, software associated with or incorporated in any of the foregoing, and all improvements, upgrades, updates, enhancements or other derivatives associated with or incorporated in any of the foregoing.

109 Taken this definition, the license to NNI and the other participants was to "make, use..., license...sell" Products using or embodying NN Technology by, or for, the Participants. The Monitor contends that giving someone else (i.e. not any of the Participants) the right to use or embody NN Technology in their own products are not "services" within the Products definition in the MRDA. The Monitor contends that on the U.S. Debtors' reading of the word "services" in the MRDA, NNI could have provided a "service" to competitors of Nortel by permitting them to use in the U.S. the entirety of Nortel's patent pool to make their own products to compete with Nortel. The plain reading of the MRDA and common sense are contrary to this interpretation.

110 I agree with the Monitor's interpretation of the MRDA. At the time the MRDA was being considered, Nortel was not in a business of licensing its services to others for the business of others. It was providing a service to its customers to support the technology being acquired by its customers. The MRDA must be read in that context. What was contemplated for a relatively short period of time after the world wide insolvency of the Nortel Group was simply not in the cards prior to that time.

(b) The right to sue for infringement

111 The U.S. Debtors contend that the right to sue is central to their rights as exclusive licensee in the U.S. The right to sue is contained under Article 4 which is headed Legal Title to NN Technology. The right is not contained in the exclusive or non-exclusive licenses under article 5. I cannot read this right to sue as being part of the licenses granted to the licensed participants in article 5. Articles 4 (a) and (e) are relevant, and provide:

> (a) Except as otherwise specifically agreed, legal title to any and all NN Technology whether now in existence or hereafter acquired, or developed pursuant to the terms of this Agreement, shall be vested in NNL. In consideration therefor, NNL agrees to enter into an Exclusive License and a Non-Exclusive License with each of the Licensed Participants as set forth in Article 5.

(e) Licensed Participants have the right to assert actions and recover damages or other remedies in their respective Territories for infringement or misappropriation of NN Technology by others.

112 This right was not contained in the prior CSA. It first appeared in the MRDA.

113 This right in sub-article 4 (e) does not state that the Licensed Participants have the exclusive right to bring action in their territories. The exclusive rights which the Licensed Participants have are contained in the exclusive license rights in article 5. There is no provision in the MRDA that precluded NNL from suing for patent infringement in a territory in which Licensed Participants had exclusive license rights. Indeed, the limited practice in the U.S. before the MRDA was signed was that both NNL and NNI were named as plaintiffs in infringement actions. To the extent those actions can be considered to be part of the factual matrix, it explains why the right to sue granted to NNI was not an exclusive right.

114 The right to sue for damages given to the Licensed Participants in their exclusive territories would obviously require a Licensed Participant to establish that it had been damaged. If the suit involved a breach of rights which the Licensed Participant had under its license, damages could presumably be proven. However, if the suit involved a breach of rights which the Licensed Participant did not have under its license, damages could not be proven.

115 If a Licensed Participant were the only plaintiff, which does not appear to have ever been the case, presumably it would be open to a defendant to contend that the Licensed Participant had not suffered any damages as what was being done by the defendant was not something that the Licensed Participants could have done under its license. That defence would not likely be run if both NNL and the Licensed Participant such as NNI were plaintiffs.

116 The Licensed Participants were not given any right to sue for damages for patent infringement in non-exclusive territories. This right was held by NNL.

(iv) Surrounding circumstances or the factual matrix

117 What may be looked at in constructing an agreement is objective evidence of the background facts at the time of the execution of the contract. It may not include evidence of the subjective intent of a party or what a party believed a contract to mean. Whether something was or reasonably ought to have been within the common knowledge of the parties at the time of execution of the contract is a question of fact.

118 There is an issue regarding the timing of the evidence that may be looked at. The exclusive licence to the Licensed Participants was contained in the 1985 CSA between Northern Telecom Limited [now NNL] and Northern Telecom Inc. [now NNI] signed in December 1984 and continued with no substantive changes in the 1992 CSA and in the MRDA and its later addenda. I would not, however, limit the time of the surrounding circumstances to the time that the CSAs were signed. The MRDA was made on December 22, 2004 effective January 1, 2001. Thereafter, while there were a number of changes to the MRDA in various addenda, no changes of substance were made to the operative provisions regarding the rights of the participants in NN Technology. I think the surrounding circumstances to the time of the signing of the MRDA in December 2004 can be looked at. Although there were some modifications to the MRDA after that, none involved any substantive change to the rights of NNL or to the exclusive licenses given to the Licensed Participants.

119 There was a great deal of evidence led by the U.S. and EMEA interests as to the subjective views of the witnesses, mostly tax personnel, regarding the rights of the parties under the CSA or MRDA or what the witnesses understood the language to mean, or in one case as to the witness's understanding of what others understood the documents to mean. Apart from the latter being inadmissible hearsay, all of this evidence was not admissible as it amounted to subjective views as to the meaning of an agreement. Nor was it admissible under the factual matrix rule permitting objective surrounding circumstances at the time of the execution of the agreement to be considered, and I do not consider it[14]. For example, what Mr. Henderson thought about the rights under the CSA license, that he copied from an earlier version of the CSA, or what others thought the MRDA meant or what they thought the intent of it was is not to be taken into account. See *Sattva*, *supra*, at para. 59.

120 I think it right to point out that not all of the evidence was one way. For example, the evidence of Angela De Wilton, the director of Intellectual Property in the Nortel IP law group and the director of IP strategy, was that Nortel was the owner of the patents and not just for administrative reasons. This evidence, elicited on cross-examination, also suffers from it being her subjective view of the rights of the parties under the MRDA. There were other witnesses who said much the same thing, such as Mr. Binning, the Executive Vice-President and CFO of NNC and NNL from November, 2007 to March, 2010 who said on his cross-examination that he understood that NNL owned the IP. This evidence suffers from the same problem of being a subjective view of the rights of the parties. The point is that that not all witnesses agreed with the subjective views of other witnesses.

121 There was also some evidence led of a prior draft of the MRDA and the views of an outside tax lawyer at Oslers who acted for NNL as to the particular draft language. This evidence is also inadmissible as being a prior draft and as constituting that particular lawyer's subjective views as to what the MRDA should contain.

122 A great deal of evidence, including evidence of statements made to tax authorities, had to do with economic theories of transfer pricing. As the transfer pricing principles changed from a cost sharing approach to a residual profit sharing approach, the economic theories and statements to tax authorities changed. One thing that did not change from the CSA approach to the RPSM approach was the language of the license grant from NNL to the other participants. It is that language that must be considered.

(a) 1996 APA

123 The 1992 CSA between Northern Telecom Limited (now NNL) and Northern Telecom Inc. (now NNI) was made with effect from January 1, 1992 but was not drafted until 1996 after the negotiations with the CCRA in Canada and the IRS is the U.S. in the advance pricing agreement process, so as to reflect the terms of the APA made with each of those tax authorities.

124 The U.S. Debtors say that the APA makes clear that NNI was entitled to all of the benefits of the NN Technology in the U.S., including all sub-licensing rights. I think they draw too long a bow. The APA between Northern Telecom and the CCRA was an agreement which by its terms was to "establish a cost sharing methodology which will result in the allocation of expenses to NNI by [NNL] for R&D done by [NNL] and its subsidiaries...which will constitute reasonable amounts in the circumstances for the purposes of section 69 of the Income Tax Act". The concern of the tax authorities was that the costs of R&D be properly allocated between NNL and NNI. The purpose of

the APA was not to agree how the income of NNL and NNI was to be shared or allocated, but how to apply R&D expenditures to whatever the income was for each of NNL and NNI.

125 Article 1.1 of the APA stated that the allocation of R&D expenses was to be determined in accordance with the cost sharing methodology described in appendix A. Appendix A is headed Cost Sharing Methodology. It contains detailed formulae to determine how R&D is to be allocated. At the outset, it has a section headed Understandings. The first understanding is that all benefit derived from R&D expenses is recognized either in the selling of a finished product to an unrelated customer or from the licensing of the technology resulting from the R&D expense (the "Benefit") within a defined geographical market by a Cost Sharing Participant ("CSP"). It goes on to state that "[NNL], as a CSP, "is entitled to all Benefits in all geographical markets except for the part(s) thereof granted to another CSP" and "NNI is also a CSP and its geographical market is the united States of America and the Commonwealth of Puerto Rico".

126 This statement that NNL is entitled to all Benefits in all geographical markets except for the part(s) thereof granted to another CSP is somewhat unclear. It could refer to all Benefits except for parts thereof granted to another CSP, or to all geographical markets except for those parts granted to another CSP. The former would seem to make sense because there would be no purpose in stating that NNL was entitled to all benefits in all geographical markets except those granted to another CSP as the following sentence states that the geographical market of NNI is the U.S. and Puerto Rico. If as I read it the understanding was that NNL was entitled to all benefits except for those granted to a CSP, the document begs the question as to what benefits were granted to NNI, which is the issue in this case.

127 It is understandable, as Mr. Henderson testified, that the parties needed to wait until the APA was settled with the tax authorities before the 1992 CSA was settled as the APA stated that it was to apply to the taxation years 1992 to 1999. That does not mean, however, that the parties needed to know how revenue was to be allocated by the APA. The purpose of the APA was to obtain an agreement from the revenue authorities how to allocate R&D costs, not revenues. This is borne out by Mr. Henderson's admissions on cross-examination that the 1992 CSA just adopted the license language of the 1985 CSA and that all operative provisions were the same.

(b) Sub-licences

128 Both sides refer to the evidence of sub-licensing as refuting the case of the other. In this I think they are incorrect. Not a great deal is clear from this evidence.

129 The reply closing argument of the U.S. Debtors contains a list of "Sublicenses Involving NNI". None were made only by NNI. Many were made by NNL and NNI and others were made by NNL on behalf of itself and its subsidiaries.

130 The sublicenses made by NNL and NNI recited that NNL has granted to NNI "certain rights to license said patents" in the U.S. In the body of the agreement it provides that NNL and NNI "to the extent of their legal right to do so" grants a license to the licensee for the countries and jurisdictions in which Nortel now or in the future holds the Nortel patent. What rights had been licensed to NNI is not stated in the sublicense. Some sublicenses provided that the royalties were payable to NNI, with NNI having the right to direct some or all of the payments to NNL. Others, being a majority of them, provided for the royalties to be payable to NNL with NNL having the right to direct some or all of the payments to NNI. In the case of cross-license agreements, the roy-

alties were payable to NNL and there was no provision for NNL to direct some or all of the payments to NNI.

131 In agreements made by Nortel, defined as NNL on behalf of itself and its subsidiaries, regarding U.S. patents, it was stated that Nortel was the owner of the patents and that Nortel granted world-wide license rights for the patents. Other agreements involving other patents made by Nortel, also defined as NNL on behalf of itself and its subsidiaries, recited that Nortel was the owner of the patents. The effect of the language in this form of agreement is that the patents are owned by Nortel on behalf itself and its subsidiaries, which supports the position of EMEA that all patents were jointly owned by the MREs.

132 The U.S. Debtors point to some evidence of certain Nortel tax personnel to explain the forms of sublicensing agreements used by Nortel. One is an e-mail exchange in 2002 involving two different views from two different tax persons, in which subjective views as to what the license in the CSAs from NNL to the other participants meant and what the theory of the sublicensing agreements was. The other is an e-mail in 2000 from someone professing not to be an expert in tax and passing on his understanding of what the tax people's view was. Apart from the latter being hearsay and inadmissible, this e-mail evidence contains subjective views of the extent of the license in the CSAs from Nortel to the other participants in the CSAs and is inadmissible.

133 Nortel's IP team prepared a presentation after the sale of the business lines in connection with the stalking horse bid process for the residual intellectual property. The presentation reviewed the history of Nortel's portfolio including its past licensing activities. It stated that Nortel previously had a small licensing group which was not a core focus of the company. There were virtually no assertions against major players, customers or partners and they focused on smaller companies with limited ability to fight back. They had earned approximately $37 million per year in royalty income. The licensing operations ceased in 2007 for budgetary reasons but in 2008 Nortel made a decision to restart the licensing organization. Mr. Binning, the Executive Vice-President and CFO of NNC and NNL from November 2007 to March 10, 2010 said that during that time Nortel was not in the license business. I take it from this evidence that for a business as large as the Nortel business, it would appear that sublicensing was an insignificant business for Nortel prior to its bankruptcy.

134 If one follows the money from the sublicenses, the evidence is that the royalties were split on the basis of the MRDA participant's contributions to R&D. The royalties were incorporated into the RPSM calculations even although they were not mentioned in Schedule A to the MRDA. Why this was done was not made clear by Mr. Stephens who gave the evidence of this happening. With one exception, we were not pointed to any evidence as to what was done with any royalties received prior to 2006, which is perhaps a more germane period as being prior to the signing of the MRDA. In 2004 a settlement of $35 million with Foundary Networks, Inc. was split on the basis of the RPSM.

135 In sum, there were no sublicenses when the license was granted by NNL to NNI at the time of the 1985 CSA. There were a number after that which do not indicate any clear pattern of what sublicense rights either NNL or the other participants were recognized to have. Sublicensing was a very insignificant part of the Nortel business prior to its insolvency.

(c) Representations to tax authorities

136 I have already discussed the 1996 APA process.

137 In connection with the switch from a CSA approach to a RPSM approach, Horst Frisch, a leading firm of transfer pricing economists, was retained to advise Nortel. Horst Frisch prepared a report dated March 14, 2002 titled Economic Analysis of Nortel Networks' Intercompany Transactions and this report was given to the tax authorities.

138 The U.S. interests point to a statement at page 10 of the report that stated from an economic standpoint, each participant could be considered to "own" the NT Technology. The paragraph in question made clear that what was being discussed was the situation under the CSA that existed up to the end of 1999. It stated:

> Prior to 2000 Nortel shared it global R&D expenses pursuant to its R&D cost sharing arrangement ("R&D CSA"), which dates back to the mid-1970's (with several amendments). Under the arrangement, each cost sharing participant ("CSP") had the right to use the intangible property developed pursuant to the R&D cost sharing arrangement (i.e., the NT Technology") in its respective market. From an economic standpoint, each R&D cost sharing participant could be considered to "own" the NT technology as it related to its specific region.

139 What is meant by "from an economic standpoint" each participant could be considered to "own" the NT technology as it related to its specific region is not clear. The OECD Guidelines and transfer pricing regulations in the U.S. and Canada all define intangible property to include licenses or rights to use assets. The statement of Horst Frisch that each participant had the right to use the IP and from an economic standpoint could be considered to "own" the NT technology could well have referred to owning the license rights held by each participant rather than referring to the underlying NT technology. The U.S. Debtors in their opening brief acknowledged case law to the effect that the rights an exclusive licensee holds are referred to as beneficial ownership.

140 Horst Frisch was clearly not talking about legal rights, nor were they discussing particular language in the CSA. Even had they purported to give their views as to what legal rights the parties had under the CSA or the MRDA, which they were not, those views would not have been admissible. Horst Frisch was discussing economic theory.

141 A few pages further in the report, when Horst Frisch were discussing what would occur under the RPSM method of allocating profits under the MRDA, they stated that the economic theory underlying the CSA was not applicable to the RPSM of allocating profits. The report stated:

> As noted above, under the prior R&D CSA the CSP which ultimately made the sale to a third party in its exclusive territory was deemed to have economic ownership of the NT Technology since the third party sale attracted an R&D allocation under the CSA.
>
> In the absence of the R&D CSA, with the two exceptions noted above, each old CSP will incur R&D expense which should entitle it to share in Nortel's global profits or losses. We have not attempted to attach these R&D expenses to the manufacturing or the distribution operation of the old CSPs since there will no longer be a formula by which global R&D expenses are shared (i.e., a third party sale will not attract an R&D allocation so it is not reasonable to assume that only the selling entity will continue to own the valuable intangibles). The amount of

> R&D performed is not necessarily correlated with third party sales or manufacturing activity. Rather, each entity will perform and pay for its own R&D expenses, and has the ability to sell Nortel products worldwide and share in global profits or losses.

142 What Horst Frisch were saying was that the economic theory of the participant in a third party sale in its territory "owning" the intangibles would not apply to such a sale under the MRDA. Perhaps implicitly they were saying that the economic "ownership" of the intangibles would be owned by all of the participants in accordance with their R&D spend under the MRDA, although this is not expressly stated. If so, from an economic point of view, it would be more consistent with the position of EMEA rather than the U.S. or Canadian interests.[15]

143 After the APAs were applied for in 2002, the tax authorities visited various Nortel sites. They then posed a number of questions. In September 2003 Nortel send a 45 page response to these questions. One of the questions was to update the authorities on any developments since the APA submission was made and whether any changes to the proposed transfer pricing methodology were anticipated. One of the responses of Nortel had to do with restructuring charges. The U.S. interests point to a statement that the residual entities are the owners of the intangible property. The context is important to see what was being said. Included was the following:

> In 2000 and later years, the telecommunications industry experienced a decline in demand unlike any other substantial industry in modem history. For that reason, there does not appear to be any precedent for analyzing the above issues. Accordingly, a reliance on basic economic principles was deemed necessary.
>
> In an arm's length situation, it was determined that the residual entities would agree to reimburse the distribution entities for a portion of their restructuring charges rather than have those entities become insolvent and forced into receivership. Generally, the underlying economic rationale for this argument is this: the residual entities, as the owners of the intangible property, as well as the manufacturers of the tangible goods, would recognize that its distribution network is critically necessary for their long-term survival. Should members of the distribution network become insolvent/cease operations, the residual entities' ability to offer their products for sale may be severely impacted. Therefore, it is in their best economic interests to ensure that a strong global distribution network exists.

144 This is a discussion of economic theory. It cannot be construed as a discussion of legal principles or the meaning of the MRDA. The reference to being owners of the intangible property could well be a reference to license rights rather than the underlying intangibles, as license rights are intangible property.

145 Dr. Timothy Reichert, a transfer pricing expert called by the Monitor, made the following statement about economic ownership as considered in transfer pricing, a statement not contradicted by any witness:

> A central concept in transfer pricing is that of "economic ownership" (referred to, alternatively, as "beneficial ownership," and simply "ownership"). Economic ownership is not a reference to ownership in a legal sense, but rather refers to a

> party's right to benefit from an income stream attributable to a defined undertaking or activity.

146 This statement cannot be disregarded. An economic right to an income stream attributable to a defined undertaking or activity requires one to know what is the defined undertaking or activity. The economic statements made to the taxing authorities did not purport to define the precise limits to the license granted by NNL to the participants under either the CSA or the MRDA. As seen, the statements made to the taxing authorities did not at all make clear what rights were being referred to and in particular, whether the "economic or beneficial ownership" was in the underlying NN Technology or in the license rights to that technology. They cannot be taken as statements that under the MRDA the licensees legally owned the NN Technology.

147 To the contrary, Mr. Weisz, the Leader of International Tax at NNI who was involved in Nortel's transfer pricing policies, and who was asked by Mr. Dolittle, the VP of Tax for Nortel to become involved in the APA process that had stalled, told the IRS during that process that it was NNL that was the legal owner of the IP.

148 It must also be recognized that the APA process with the tax authorities was to arrive at an agreement with them regarding the Nortel operating business. It was an operating business with profits and losses that the tax authorities were interested in. This was the case both for the APA processes for both the CSA and MRDA. There were no discussions with the tax authorities as to what would happen on the insolvency of the entire business of Nortel. The discussion of the economic theory of economic or beneficial ownership must be considered in that light. They were not discussing such a theory in so far as it might apply to the situation of a cessation of business as occurred with Nortel.

149 The issue in this case has to do with the breadth of the licenses granted to the Licensed Participants and whether that included the right to sublicense the residual patent portfolio that was eventually sold to Rockstar. However at the time of the APA processes, sublicensing was a miniscule part of the business of Nortel and not surprisingly I have been pointed to no presentation to the tax authorities that discussed this issue. It was not on the Nortel radar.

150 The MRDA was provided to the tax authorities. They also had the prior CSA. The U.S. interests do not say that NNI rights were obtained other than in the CSA and then the MRDA. The tax authorities had these agreements and were able to read them, and were in as good a position as anyone to form their own view of what the agreements did or did not do. It cannot be suggested that the tax authorities did not understand transfer pricing. It was their business to know it.

151 There is evidence relied on by the EMEA debtors to support their position that the proceeds of the sale of the residual IP should be allocated in accordance with the relative expenditure on R&D by NNL and the licensed participants. After the APS application was filed by Nortel with the tax authorities in 2002, planning for a June 19, 2002 joint meeting with the three tax authorities took place in earnest, including the preparation of answers to questions Nortel anticipated might be raised by the tax authorities. In preparation for the meeting, Nortel engaged advisors from Deloitte & Touche LLP, KPMG LLP, Horst Frisch, and Sutherland Asbill & Brennan LLP to assist. Mr. O'Connor of Deloitte's prepared the following answer to an anticipated question regarding the sale of any IPCo, an answer that was circulated and agreed before the meeting:

> [Q:] How does Nortel propose to account for any future sale of intellectual property developed prior to or during the term of the APA? Which entities are considered the legal owner of IP and which are considered the economic owners?
>
> [A:] Proceeds from the sale of IP will be allocated to residual profit split participants on the basis of their economic ownership of the IP -- that is, on the basis of their share of total R&D capital stock in the year of sale.

152 The document was taken to the joint meeting. There is no evidence one way or the other as to whether the question was asked. While the question does not deal with what would happen if all of the Nortel IP was sold on a world-wide insolvency of Nortel, it is evidence that at the time of the APA process, Nortel was prepared to say that any sale of IP would be split in accordance with the RPSM in the year of the sale.

(d) Avoiding permanent establishment status in the U.S.

153 The U.S. interests contend that it was important to NNI not to be considered a U.S. resident for U.S. tax purposes and thus not have "permanent establishment" in the U.S. It is contended that it was this concern that drove separate legal entities to be set up for each country and for the license to be exclusive to the Participants for their territory so that the Participants would be the only ones dealing with customers in that territory.

154 Taken that as the situation, I do not see that it gets very far. There is no question that the exclusive license gave NNI the exclusive right to sell Nortel products in the U.S. The important issue in this case is what rights NNI had to sub-license and whether it was restricted to Nortel "Products" as defined in the MRDA. Sub-licensing was a miniscule part of the business of Nortel and there is no evidence at all that sublicensing issues drove the setting up of companies in different jurisdictions.

(e) Patent litigation

155 I have previously referred to the patent litigation that had taken place prior to the MRDA. Both NNL and NNI were plaintiffs in the actions in the U.S. Why that was so does not really matter. It explains why the right given to licensed participants to sue in their territories for damages for patent infringement was not an exclusive right.

156 As to what was done with the proceeds of patent litigation, there was a settlement in October, 2004 of an action commenced by NNL and NNI against Foundary Networks, Inc. $35 million was paid for past infringement and for future royalties under a license agreement. The entire payment was treated as royalty income and allocated to NNL and the Licensed Participants in accordance with the RPSM in the MRDA.

(f) Conclusion of factual matrix evidence

157 I do not consider the surrounding circumstance or factual matrix evidence to provide much clear assistance in construing the meaning of the terms in the MRDA. Even if it did, I would be required to be guided by the dictates of *Sattva* that while the surrounding circumstances will be considered in interpreting a contract and the goal of examining such evidence is to deepen a decision-maker's understanding of the mutual and objective intentions of the parties as expressed in the

words of the contract, they must never be allowed to overwhelm the words of the contract and the interpretation of a contract must always be grounded in the text. While the surrounding circumstances are relied upon in the interpretive process, courts cannot use them to deviate from the text such that the court effectively creates a new agreement.

(v) Commercial reasonableness

158 The U.S. interests and EMEA say that the Monitor's interpretation of the MRDA is commercially unreasonable. They contend that no party at arm's length would agree to spend large amounts to develop patents but only one party would be entitled to all of the proceeds from the sale of those patents.

159 It must be remembered that the MRDA and its predecessor CSA were drafted to come to terms with the tax authorities. The parties to the negotiations were Nortel on the one hand and the tax authorities on the other. The resulting CSA and then MRDA were operating agreements premised on cost sharing under the CSA and profit or loss sharing under the MRDA. The tax authorities were interested in the tax that each Nortel entity would pay each year. The tax authorities dealt in only limited periods of time. The 1992 CSA was settled with the tax authorities only in 1996, yet in 1999 they made it clear they wanted Nortel to abandon the CSA agreement and instead change to a RPS method of transfer pricing.

160 Nortel and the tax authorities were not negotiating on what would happen if Nortel stopped operating or in the event of a world-wide insolvency of Nortel. More particularly, they were not negotiating on how the proceeds of the sale of the entire Nortel world-wide patent portfolio would be allocated amongst the various Nortel companies in the event of the insolvency of Nortel. That was not discussed. This is not surprising because, as Dr. Eden testified, transfer pricing rules were developed only in connection with ongoing entities for purposes of determining their corporate tax.

161 The issue of commercial reasonableness must be considered in the context of who was involved in the preparation of the MRDA. It was not the technology people. Mr. Brian McFadden, the Chief Technology Officer of Nortel at the time the MRDA was drafted and signed, was not consulted about its terms and never heard of the MRDA while at Nortel. Ms. Angela de Wilton, the Nortel Director of Intellectual Property had no recollection of ever seeing the MRDA. In order to make the argument that it would have been commercially unreasonable for a Nortel company to agree to do R&D leading to patents and not be paid for the patents on the sale of the business, one would think that the people responsible for the R&D would have at least known of the agreement and its terms. The fact that they did not indicates that a trade-off of R&D for future receipts on a sale of the business was not on the radar screen at all so far as the operating people were concerned. The language of the MRDA was all tax driven.

162 So far as what was on the radar of the tax people at Nortel at the time the terms of the MRDA were settled, in so far as the quid pro quo for doing R&D was concerned, the MRDA expressly provided in Article 2(c) that any compensation for R&D was to be based solely on the RPSM allocation. It stated:

> (c) All costs incurred directly or indirectly by each Participant for R&D Activity shall be borne exclusively by it. Any reimbursement for costs including any other compensation shall be provided to such Participant for its R&D Activity solely as provided in Article 3 below.

163 Article 3 that the annual sharing of profits or losses under the residual profit split method was what was to be received for each participants R&D that year. It stated:

Article 3 -- R&D Activity Payments

(a) For and as a consequence of the performance of R&D Activity, each Participant shall be entitled to receive a payment in an amount equal to the allocation determined under the RPSM (the "R&D Allocation") as the measure of the benefit to which it is entitled commensurate with its performance of, and contribution to, R&D Activity.

164 In the context of what the parties were dealing with in the MRDA, I do not see how it can be said that it was commercially unreasonable for them to agree that in return for doing R&D each year, they would share only in the profits or losses in accordance with the RPSM allocation. That is all they had in mind. While Nortel had suffered losses by 2004 when the MRDA was signed, there is no evidence that Nortel expected to have only losses in the future. To the contrary, the operating people at Nortel expected that Nortel would return to profitability.

165 Mr. Henderson testified that a bankruptcy or insolvency of Nortel was not in their minds at the time the RPSM in the MRDA was created. The fact that they did not consider or provide what was to happen to the proceeds if all of the IP was sold after a world-wide insolvency does not make the agreement commercially unreasonable. The time for considering whether an agreement properly interpreted is commercially reasonable or unreasonable is surely the time when it was agreed, not in hindsight.

166 The U.S. Debtors called Dr. Catherine Tucker, a transfer pricing expert, whose evidence was to the effect that under the Monitor's interpretation of the MRDA, the Licensed Participants would lack appropriate incentives to undertake expensive and speculative R&D for the next potential generation of products. I do not think her evidence helpful. It is really an inadmissible subjective view as to how the MRDA license should be interpreted.

167 There is no basis for Professor Tucker's assumption that the MRDA was intended to create incentives for the Licensed Participants to make forward-looking innovations. The fact that Mr. McFadden, the Chief Technology Officer of Nortel at the time of the MRDA, was not consulted about the MRDA and knew nothing about it belies any such assumption. Professor Tucker's assumption also ignores the way in which R&D was carried out at Nortel.

168 The majority of Nortel R&D was directed by the various Business Lines, which had to prepare annual R&D plans for approval. The remaining R&D, the advanced technology research (the "leap from one S-curve to the next" that Professor Tucker describes), was coordinated by the Chief Technology Officer. The evidence of Mr. McFadden was that all advanced technology programs were based in Ottawa and were operated by NNL. While product development R&D groups within each of Nortel's lines of business reported directly to the heads of their business units, the advanced technology programs personnel within each line of business reported directly to the CTO's office at NNL. The R&D was not the bailiwick of any Licensed Participant.

(vi) Conclusions on the meaning of the MRDA

169 I interpret the MRDA, and find, that under it, and while Nortel operated as a going concern business, NNL had all ownership interests of the NN Technology subject to grants, being (i) the

grant to each Licensed Participant of a non-exclusive right to assert actions and recover damages in their territory under article 4(e) and (ii) the grant of exclusive and non-exclusive licenses to the Licensed Participants under article 5(a).

170 The licenses under article 5(a) were not licenses of all rights to the NN Technology but were subject to field of use restrictions that gave the Licensed Participants the right to use the NN Technology to make, use or sell Products as defined in the MRDA, which meant products, software or services that were made or sold by, or for, any of the Licensed Participants. The Products must have been created or marketed by or for the Nortel Group. No product that was part of a third party's business rather than the business of Nortel fell within the definition of Products. The business considered by IPCo was not covered by the licenses. The Licensed Participants' rights to sublicense were subject to these restrictions.

Applicability of the MRDA to the allocation issues

171 Nortel Networks UK Pension Trust Limited and the Board of the UK Pension Protection Fund (the "UKPC") contend that the MRDA was never intended to provide an answer to the question of how to allocate among the bankrupt estates the proceeds of the sale of the Nortel Group's assets following the world-wide insolvency of Nortel.

172 I agree. The MRDA was an operating agreement and was not intended to, nor did it, deal with the disposal of all of Nortel's assets in a situation in which no revenue was being earned and no profit or losses were occurring. The MRDA provided in its opening line that it was an agreement "confirming and formalizing the operating arrangements" of the parties.

173 There is a provision in schedule A to the MRDA added in the third addendum effective January 1, 2006 but signed by the parties late in late December 2008 or early January 2009 that indicates that sales of property were not intended to be dealt with under the MRDA. That schedule A provided that in dealing with the calculations of the Nortel earnings/losses to be used in the RPSM calculation, there was to be deducted "gain/loss on the sale of business". A gain or loss would normally be taken into account on the particular company's statement of profit and loss and the Participants decided they did not want any such gain or loss to influence the calculation of profits or losses for the purposes of calculating the allocation of profits or losses in the RPSM calculation. Mr. Orlando testified that the sale of a business was seen to be a non-operating activity. This provision is an indication that the MRDA was not intended to deal with the sale of any assets, let alone the world-wide assets of the Nortel Group.

174 The MRDA and its predecessor Cost Sharing Agreements ("CSAs") were developed for and driven by transfer pricing concepts. They were drafted to come to terms with the tax authorities. The MRDA expressly provided in a recital that the calculation of the RPSM might have to be adjusted as a result of its review by the tax authorities. The MRDA was drafted by tax lawyers and tax advisors. The primary external counsel involved, and lead drafter of the MRDA, Giovanna Sparagna, testified that the MRDA is "primarily focused on transfer pricing," which is "part of tax law," and it is "primarily [a] tax law document[]." The MRDA was signed on behalf of NNL by John Doolittle, Nortel's Vice-President of Tax. All parties acknowledge that the MRDA was a tax-driven document designed to implement Nortel's transfer pricing policies.

175 Following the insolvency proceedings on January 14, 2009, no transfer pricing payments were made under the MRDA. The two special cash payments made by NNI to NNL were made un-

der different agreements, being the IFSA dated June 9, 2009 and the FCFSA dated December 23, 2009.

176 Dr. Eden, who testified on behalf of the U.S. Debtors, testified that transfer pricing was only for ongoing businesses. She also testified that she saw the MRDA as a transfer pricing document and that the RPSM method contained in it was only used for corporate income tax purposes. She and other transfer pricing experts such as Dr. Richard Cooper, Dr. Steven Felgran and Dr. Timothy Reichert testified to the effect that transfer pricing does not address entitlement to the proceeds of the sale of assets on insolvency.

177 I accept that the MRDA was a transfer pricing document created for tax purposes. The licenses were a part of it. The licenses granted under it were never dealt with separately from the MRDA. Their only purpose was to support the intended tax treatment resulting from the MRDA.

178 It can perhaps be argued that under article 9 of the MRDA the rights of NNL under article 4 and of the Licensed Participants under article 5 continued on the expiry or termination of the agreement, indicating a purpose other than tax that survives the insolvency of the Nortel enterprise. I would not construe those provisions that way.

179 The relevant provisions of article 9 of the MRDA provide:

Article 9 -- Duration and Continuing Rights and Obligations

(a) This Agreement shall be effective from January 1, 2001 until December 31, 2004, provided however that this Agreement will automatically renew for additional and unlimited one-year terms until terminated by the mutual written consent of all Participants.

(b) Upon the expiry or termination of this Agreement as provided herein, each Licensed Participant shall be deemed to have acquired a fully paid up license permitting it to continue to exercise the rights granted to it herein, and, in particular, the rights granted to it in Article 5 as though this Agreement had continued.

(c) The provisions of Article 4 (Legal Title to NN Technology) with respect to NN Technology acquired or developed pursuant to this Agreement from the Effective Date of this Agreement up to and including its expiry or termination date, Article 6 (relating to confidentiality) and Article 7 (relating to liability) shall survive notwithstanding the expiry of this Agreement, or any termination of this Agreement for any cause whatsoever.

180 Under article 9, the MRDA automatically renewed after 2004 unless terminated by mutual consent of all parties to it. If terminated, the Licensed Participants were to be deemed to have acquired a fully paid up license "permitting it to continue to exercise the rights granted to it herein... as though this Agreement had continued". This provision by its terms contemplated the business of the Licensed Participants continuing to operate. It did not contemplate a situation in which all of the Licensed Participants liquidated their assets and went out of business.

181 The CSAs contained a similar provision regarding the rights of the Licensed Participants on termination to a fully paid up license. At the end of 1999, the tax authorities did not want to re-

new the APAs and they encouraged Nortel to adopt a RPSM. In December, 2001, Nortel's CSAs for R&D were terminated effective January 1, 2001. In spite of the termination of these agreements, Nortel continued to operate and it was only on December 22, 2004 after negotiations with the tax authorities that the MRDA was executed with an effective date of January 1, 2001. The MRDA stated that it confirmed and formalized the operating arrangements of the Participants as and from that date. That is, the license rights under the CSAs continued to be used in accordance with the terms of the CSAs, and Nortel's tax advisors told that to the tax authorities on April 26, 2004. This was contemporaneous with the MRDA being settled.

182 One can see from this that the purpose of continuing rights under article 9 of the MRDA after a termination was to permit the Participants to continue operating, during which a new agreement would have to be negotiated. Nortel was a multi-national enterprise that had to live with tax authorities where it operated and could not live without a transfer pricing agreement of some kind. As previously discussed, there was no thought at the time of the MRDA being settled that Nortel was not going to return to profitability.

183 Article 11(a) of the MRDA provided that any Participant that was not a party to an APA with the tax authorities could elect to withdraw from the MRDA. Article 11(c)(iv) of the MRDA provided that it was a defaulting event if one of the Participants became insolvent, in which case the Participant automatically was terminated from participation in the agreement. A fourth addendum was made to the MRDA effective December 31, 2008 and signed in early January 2009. It was headed Standstill Provision and provided that in the event of an occurrence of an event described at Section (sic) 11(c)(iv), i.e. if a Participant became insolvent, (i) no Participant effected by such insolvency shall be automatically terminated from participating in the agreement, (ii) no Participant shall elect to withdraw from the agreement under Article 11(a), and (iii) NNL would have the right in its sole discretion to terminate participation in the MRDA of any Participant affected by such event, i.e. of a defaulting Participant by reason of its insolvency.

184 This provision did not contain provisions expressed to apply in the event of a world-wide insolvency of all of the Nortel companies. It contained provisions of a standstill nature dealing with a situation in which one Participant became insolvent. It was obviously designed to prevent a Participant from declaring insolvency and then trying to take positions contrary to other Participants and to prevent the other Participants in such an event trying to take positions contrary to other Participants. I do not read this provision as an indication that in the event of a world-wide insolvency of all of the Nortel companies with no operations, the agreement was to continue to govern the affairs of a non-operating enterprise. Had that been the parties' intention, they could have said so in the addendum. They did not.

185 I conclude that the circumstances surrounding the creation of the MRDA lead to no other result but that the construct of legal title to the NN Technology being in NNL in return for NNL granting exclusive licenses to the Licensed Participants was only for the purpose of supporting the proposed method to split profits or losses on a tax efficient basis while Nortel operated as a going concern business. The agreement in its application was intended to apply only to Nortel while it operated and not to deal with rights after Nortel and its subsidiaries stopped operating its businesses.

EMEA position on ownership of the Nortel IP

186 The EMEA Debtors' position is different from the position of the Canadian and U.S. Debtors. They say that the Participants, or RPEs, have joint ownership of all Nortel IP under common

law principles by reason of the IP belonging to the RPEs that employed the inventors. They say that the MRDA recognizes that joint ownership and that the joint ownership should be the basis for allocating the proceeds of the sale of the Nortel residual IP.

187 The basic premise of the EMEA Debtors' argument is that the Participants or RPEs were joint owners of all Nortel IP by reason of law. They argue that under Canadian law, the inventor is the first owner of an invention and is the legal title holder entitled to apply for any related patent. However, where the inventor is employed to invent, as the Nortel Group's researchers were, then the employer by operation of law beneficially owns any resulting IP. While the employee inventor who is listed on the patent application holds legal title, the employer is the beneficial owner. Given the integrated nature of Nortel and its R&D created in multiple jurisdictions, the EMEA Debtors argue that each participant beneficially owned not the IP created in its jurisdiction, but rather a share of the indivisible pool of the Nortel Group's IP.

188 Canadian and U.K. law appears to support the principle that where an employee creates an invention as part of his or her employment, the employer is the beneficial owner of the patent.[16] U.S. law is otherwise. Under U.S. law, unless there is agreement to the contrary, it is the inventor and not the employer who is the owner of his or her invention until he or she assigns it[17].

189 All Nortel employees, whether employed by NNL or a subsidiary, were required to assign directly or indirectly to NNL any intellectual property which they generated during the course of their employment. At least 98% of the patents and patent applications sold to Rockstar had been assigned by the inventors to NNL.

190 The EMEA Debtors say that while the inventors assigned their rights to NNL, the subsidiaries that employed the inventors did not. Thus they say that NNUK, the employer of inventors in the U.K., continued to have beneficial ownership of the patents for inventions created by its employees. I do not accept that. NNUK was required under article 4 (b) of the MRDA to execute such documents as NNL reasonably required to give effect to article 4 (a), which provided for legal title to NN Technology to be vested in NNL. In light of that obligation, NNUK is in no position now to say that the assignment of the IP from its employees to NNL was ineffective.

191 This argument of the EMEA Debtors would not apply to NNI in the U.S. as under U.S. law NNI did not have any such common law rights to IP developed by its employees who assigned their rights to NNL. Nor would it apply to patents invented by employees of NNL who assigned their rights to NNL. The EMEA Debtors' argument, if accepted, would mean that NNUK would only have rights to the IP developed by its employees and would have no joint ownership interest in the IP developed by employees of NNL, NNI, NNSA or Nortel.

192 I cannot accept the joint ownership theory of the Nortel IP or use that theory as a basis for allocating the proceeds of sale of the Nortel IP assets.

Appropriate method to allocate the proceeds of sale

193 While the Monitor on behalf of the Canadian Debtors and the U.S. Debtors take diametrically different views as to their rights under the MRDA, they each look to the MRDA and the rights they say were given to them as the basis of their allocation positions. I have not accepted their position that they obtained rights under the MRDA that determine their right to the proceeds of the sale of Nortel's assets.

194 Nor have I accepted the position of the EMEA Debtors that the RPEs have joint ownership of all Nortel IP under common law principles recognized in the MRDA and that such joint ownership should be the basis for allocating the proceeds of the sale of the Nortel residual IP.

195 Without the MRDA to govern the allocation, and without the joint ownership theory of the EMEA Debtors, the issue becomes one of deciding what metric should be used to allocate the proceeds of sale.

196 In so far as the IP is concerned, while the patents were registered in the name of NNL, I would not for that reason hold that NNL is entitled to the proceeds of the IP sales. The patents and application rights to apply for patents were held in the name of IP for administrative purposes. It was best practices in a multi-national enterprise to have all patents assigned to one company, in this case to NNL, as explained by Ms. Anderson and Ms. De Walton, and made management of the portfolio much easier. While these witnesses expressed subjective views that it was NNL who owned the patents, these views are not determinative, as acknowledged in the Monitor's reply brief at paras 65-66.

197 This was not one corporation and one set of employees inventing IP that led to patents. Nortel was a highly integrated multi-national enterprise with all RPEs doing R&D that led to patents being granted. It was R&D that drove Nortel's business. R&D and the intellectual property created from it was the primary driver of Nortel's value and profits. All parties agree on that. It would unjustly enrich NNL to deprive all of the other RPEs of the work that they did in creating the IP just because the patents were registered in NNL's name.

198 Canadian law permits recovery for unjust enrichment whenever a plaintiff can establish three elements: an enrichment of or benefit to the defendant, a corresponding deprivation of the plaintiff, and the absence of a juristic reason for the enrichment: *Kerr v. Baranow*, 2011 SCC 10 at para. 32.

199 U.S. law provides that unjust enrichment occurs where a party obtains a benefit which, under the circumstances and in light of the relationship between the parties, it would be inequitable to retain: *Counihan v. Allstate Ins. Co.*, 194 F.3d 357, 361 (2d Cir. 1999). It requires the retention of a benefit to the loss of another or the retention of money or property of another against the fundamental principles of justice or equity and good conscience. It is not available if there is a contract that governs the relationship between the parties that gives rise to the claim: *Kuroda v. SPJS Holdings, L.L.C.*, 971 A.2d 872, 891(Del. Ch. 2009).

200 On either test, I find that NNL would be unjustly enriched by being entitled to all of the proceeds of the sale of Nortel IP at the expense of the other RPEs who contributed to the creation of that IP just because the patents were registered in NNL's name. It would be inequitable. There would be no juristic reason for the enrichment as the MRDA as I have interpreted it does not deal with the allocation rights of the parties in this world-wide insolvency of Nortel.

201 It would also unjustly enrich NNI if it were to be allocated the amount from the IP sales that it claims based principally on its revenues, which is the basis of the claim by the U.S. Debtors. NNI was able to sell Nortel products based on the R&D and resulting IP performed by other RPEs.

202 This is an unprecedented case involving insolvencies of many corporations and bankrupt estates in different jurisdictions. The intangible assets that were sold, being by far the largest type of asset sold, were not separately located in any one jurisdiction or owned separately in different juris-

dictions. They were created by all of the RPEs located in different jurisdictions. Nortel was organized along global product lines and global R&D projects pursuant to a horizontally integrated matrix structure and no one entity or region was able to provide the full line of Nortel products and services. R&D took place in various labs around the world in a collaborative fashion. R&D was organized around a particular project, not particular geographical locations or legal entities, and was managed on a global basis. The fact that Nortel ensured that legal entities were properly created and advised in the various countries in which it operated in order to meet local legal requirements does not mean that Nortel operated a separate business in each country. It did not.

203 Nortel's matrix structure also allowed Nortel to draw on employees from different functional disciplines worldwide (*e.g.* sales, R&D, operations, finance, general and administrative, etc.), regardless of region or country according to need. Individuals could be part of a team with horizontal responsibility without removing them from their respective position vertically (or departmentally) within the Nortel group.[18]

204 In these circumstances, what principles should be applied to determine the allocation of the proceeds of the asset sales? In my view, doing what is just in the unique circumstances of this case should govern the allocation.

205 A court has wide powers in a CCAA proceeding to do what is just in the circumstances. Section 11(1) provides that a court may make any order it considers appropriate in the circumstances. Although this section was provided by an amendment that came into force after Nortel filed under the CCAA, and therefore by the amendment the new section does not apply to Nortel, it has been held that the provision merely reflects past jurisdiction. In *Century Services*, Deschamps J. stated:

> **65** I agree with Justice Georgina R. Jackson and Professor Janis Sarra that the most appropriate approach is a hierarchical one in which courts rely first on an interpretation of the provisions of the *CCAA* text before turning to inherent or equitable jurisdiction to anchor measures taken in a *CCAA* proceeding (see G.R. Jackson and J. Sarra, "Selecting the Judicial Tool to get the Job Done: An Examination of Statutory Interpretation, Discretionary Power and Inherent Jurisdiction in Insolvency Matters", in J.P. Sarra, ed., *Annual Review of Insolvency Law 2007* (2008), 41, at p. 42). The authors conclude that when given an appropriately purposive and liberal interpretation, the *CCAA* will be sufficient in most instances to ground measures necessary to achieve its objectives (p. 94).
>
> **67** The initial grant of authority under the *CCAA* empowered a court "where an application is made under this Act in respect of a company ... on the application of any person interested in the matter ..., subject to this Act, [to] make an order under this section" (*CCAA*, s. 11(1)). The plain language of the statute was very broad.
>
> **68** In this regard, though not strictly applicable to the case at bar, I note that Parliament has in recent amendments changed the wording contained in s. 11(1), making explicit the discretionary authority of the court under the *CCAA*. Thus in s. 11 of the *CCAA* as currently enacted, a court may, "subject to the restrictions set out in this Act, ... make any order that it considers appropriate in the circum-

stances" (S.C. 2005, c. 47, s. 128). Parliament appears to have endorsed the broad reading of *CCAA* authority developed by the jurisprudence. (underlining added)

206 This Court has a broad inherent jurisdiction to make orders as required to fill in gaps or lacunae not covered by specific provisions in the CCAA. As a superior court of general jurisdiction, the Superior Court of Justice has all of the powers that are necessary to do justice between the parties. Except where provided specifically to the contrary, the Court's jurisdiction is unlimited and unrestricted in substantive law in civil matters. See *80 Wellesley St. East Ltd. v. Fundy Bay Builders Ltd. et al.*, [1972] 2 O.R.280 (C.A.) at para. 9. See also *TCR Holding Corp. v. Ontario*, 2010 ONCA 233 at para. 26, *Beach v. Moffatt* (2005), 75 O.R. (3d) 383 (C.A.) at para. 8, *J.M. v. W.B.* (2004), 71 O.R. (3d) 171 (C.A.) at para. 43 and *McVan General Contracting Ltd. v. Arthur* (2002), 61 O.R. (3d) 240 (C.A.) at para. 56.

207 In *Century Services Inc. v. Canada (Attorney General)*, 2010 SCC 60 at paras. 57-61, it was recognized by the Supreme Court and stated by Justice Deschamps that the CCAA is skeletal in nature and does not contain a comprehensive code that lays out all that is permitted, that the incremental exercise of judicial discretion with respect to the CCAA has been adapted and has evolved to meet contemporary business and social needs and that when large companies encounter difficulty and reorganizations become increasingly complex, CCAA courts have been called upon to innovate accordingly.

208 In this case, insolvency practitioners, academics, international bodies, and others have watched as Nortel's early success in maximizing the value of its global assets through cooperation has disintegrated into value-erosive adversarial and territorial litigation described by many as scorched earth litigation.[19] The costs have well exceeded $1 billion. A global solution in this unprecedented situation is required and perforce, as this situation has not been faced before, it will by its nature involve innovation. Our courts have such jurisdiction.

209 It is a fundamental tenet of insolvency law that all debts shall be paid *pari passu* and all unsecured creditors receive equal treatment. See *Shoppers Trust Co. (Liquidator of) v. Shoppers Trust Co.* (2005), 74 O.R. (3d) 652 (C.A.) at para. 25, per Blair J.A., *Indalex Ltd. (Re)* (2009), 55 C.B.R. (5th) 64 (Ont. S.C.), at para. 16 per Morawetz J. and my comments in *Nortel Networks Corp. (Re)* (2014), 121 O.R. (3d) 228 at para.12. A pro rata allocation in this case goes partway towards such a result.

210 According to the various protocols, the task in this proceeding is to determine the amount that is to be allocated to each of the Canadian, U.S. and EMEA Debtors' Estates. I do not read the protocols or the IFSA as precluding a pro rata allocation. While payment to the Selling Debtors is to be made from the $7.3 billion in the lockbox funds, neither the protocols nor the IFSA determine how the allocation is to be made.

211 Directing a pro rata allocation will constitute an allocation as required. Once the lockbox funds have been allocated, it will be up to each Nortel Estate acting under the supervision of its presiding court to administer claims in accordance with its applicable law. A pro rata allocation can be achieved by directing an allocation of the lockbox funds to each Debtor Estate based on the percentage that the claims against that Estate bear to the total claims against all of the Debtor Estates.

212 It is argued that a pro rata allocation would constitute an impermissible substantive consolidation of the Estates, or as put by the U.S. Debtors, an impermissible "global substantive con-

solidation". I do not agree. A pro rata allocation in this case would not constitute a substantive consolidation and, even if it did, it would in my view be permissible within established case law.

213 In a liquidation or reorganization of a corporate group, the doctrine of substantive consolidation has emerged in order to provide a mechanism whereby the court may treat the separate legal entities belonging to the corporate group as one. In particular, substantive consolidation allows for the combination of the assets and liabilities of two or more members of the group, extinguishes inter-company debt and creates a single fund from which all claims against the consolidated debtors are satisfied. In effect, under substantive consolidation, claims of creditors against separate debtors instantly become claims against a single entity.

214 A pro rata allocation in this case would not constitute a substantive consolidation, either actual or deemed, for a number of reasons. First, and most importantly, the lockbox funds are largely due to the sale of IP and no one Debtor Estate has any right to these funds. It cannot be said that these funds in whole or in part belonged to any one Estate or that they constituted separate assets of two or more Estates that would be combined. Put another way, there would be no "wealth transfer" as advocated by the bondholders. The IFSA, made on behalf of 38 Nortel debtor entities in Canada, the U.S. and EMEA, recognized that the funds would be put into a single fund undifferentiated as to the Debtor Estates and then allocated to them on some basis to be agreed or determined in this litigation. Second, the various entities in the various Estates are not being treated as one entity and the creditors of each entity will not become creditors of a single entity. Each entity remains separate and with its own creditors and its own cash on hand and will be administered separately. The inter-company claims are not eliminated.

215 Even if it could be said that a pro rata allocation involved substantive consolidation, which it cannot, I do not see case law precluding it in the unique circumstances of this case international case. Even in domestic cases, CCAA plans involving substantive consolidation are not unknown.

216 In Canada, neither the CCAA nor the BIA contains express provisions authorizing substantive consolidation. Similarly, the U.S. Bankruptcy Code does not explicitly permit substantive consolidation. However, courts in both jurisdictions have rendered consolidating orders on the basis of their equitable jurisdiction. See *See* M. MacNaughton and M. Azoumanidis, *Substantive Consolidation in the Insolvency of Corporate Groups: A Comparative Analysis, Annual Review of Insolvency Law, 2007*, J. Sarra, ed. (Carswell: 2008).[20]

217 In *Rescue! The Companies' Creditors Arrangement Act*, by Dr. Janis Sarra, Carswell 2007, the grounds for permitting substantive consolidation were described as follows at page 242:

> The court will allow a consolidated plan of arrangement or compromise to be filed for two or more related companies in appropriate circumstances. For example, in *PSINet Ltd.* the Court allowed consolidation of proceedings for four companies that were intertwined and essentially operated as one business. The Court found the filing of a consolidated plan avoided complex issues regarding the allocation of the proceeds realized from the sale of the assets, and that although consolidation by its nature would benefit some creditors and prejudice others, the prejudice had been ameliorated by concessions made by the parent corporation, which was also the major creditor. Other cases of consolidated proceedings such as Philip Services Canadian Airlines, Air Canada and Stelco, all proceeded without issues in respect of consolidation.

> Generally, the courts will determine whether to consolidate proceedings by assessing whether the benefits will outweigh the prejudice to particular creditors if the proceedings are consolidated. In particular, the court will examine whether the assets and liabilities are so intertwined that it is difficult to separate them for purposes of dealing with different entities. The court will also consider whether consolidation is fair and reasonable in the circumstances of the case.

218 In *Re Lehndorff General Partner Ltd.* (1993), 17 C.B.R. 3d 24, Justice Farley held that a consolidated plan was appropriate, noting that there was significant intertwining of the debtor companies, including multiple instances of inter-company debt, cross-default provisions and guarantees and the existence and operation of a centralized cash-management system. All of these features were present in Nortel.

219 In *Re PSINet Ltd.* (2002), 33 C.B.R. 4th 284, Justice Farley noted that a plan of arrangement based on substantive consolidation avoided the "complex and likely litigious issues" that could result from the allocation of the proceeds of the sale of substantially all of the debtor companies' assets. He also noted that the consolidated plan reflected the intertwined nature of the debtors and their operation. In that case, Farley J. stated that the overall effect of a consolidation was required:

> In the circumstances of this case, the filing of a consolidated plan is appropriate given the intertwining elements discussed above. See *Northland Properties Ltd., Re*, 69 C.B.R. (N.S.) 266 (B.C.S.C.), affirmed (B.C.C.A.), *supra*, at p. 202; *Lehndorff General Partner Ltd., Re*, 17 C.B.R. (3d) 24 (Ont. Gen. Div. [Commercial List]) at p. 31. While consolidation by its very nature will benefit some creditors and prejudice others, it is appropriate to look at the overall general effect.

220 In *Northland Properties*, a case involving a proposed plan for several companies that operated as a single entity, Justice Trainor considered the tests for permitting a substantive consolidation. He looked to U.S. law for guidance and began his analysis by adopting the balancing test articulated in *Re Baker and Getty Fin. Services Inc.,* U.S. Bankruptcy Court, N.D. Ohio (1987) 78 B.R. 139:

> The propriety of ordering substantive consolidation is determined by a balancing of interests. The relevant enquiry asks whether "the creditors will suffer greater prejudice in the absence of consolidation than the debtors (and any objecting creditors) will suffer from its imposition".

221 Trainor J. then went on to list seven factors which had been developed to assist in the balancing of interests. Those factors were:

1. difficulty in segregating assets;
2. presence of consolidated financial statements;
3. profitability of consolidation at a single location;

4. commingling of assets and business functions;

5. unity of interests in ownership;

6. existence of intercorporate loan guarantees; and

7. transfer of assets without observance of corporate formalities.

222 In considering these factors, it is clear beyond peradventure that Nortel has had significant difficulty in determining the ownership of its principle assets, namely the $7.3 billion representing the proceeds of the sales of the lines of business and the residual patent portfolio. This amount constitutes over 80% of the total assets of all of the Nortel entities[21]. This issue has taken several years of litigation and untoward costs in the parties attempting to establish an entitlement to it. As the MRDA does not govern how the sales proceeds are to be allocated, there is no one right way to separate them. It cannot be said that there is no question which entity is entitled to the sale proceeds or in what amount. It is clear that these assets are in the language of Dr. Janis Serra "so intertwined that it is difficult to separate them for purposes of dealing with different entities".

223 Moreover, the evidence in this case is clear and uncontested that Nortel (a) had fully integrated and interdependent operations; (b) had intercompany guarantees for its primary indebtedness; (c) operated a consolidated treasury system in which generated cash was used throughout the Nortel Group as required; (d) disseminated consolidated financial information throughout its entire history, save for the year before its bankruptcy; and (e) created IP through integrated R&D activates that were global in scope.

224 When consolidation occurs, some creditors may be prejudiced if they would have had a greater recovery of so many cents on the dollar against their debtor if there had been no consolidation. Conversely, other creditors may be benefitted by consolidation if they would have had a lesser recovery against their debtor if there had been no consolidation. In this case, even if a pro rata allocation amounted to a consolidation, the issue would be moot because it cannot be said that without consolidation one class of creditors, including the bondholders, would necessarily have had a greater recovery than with consolidation. The reason for this is that there has been no recognized measurable right in any one of the selling Debtor Estates to all or a fixed portion of the proceeds of sale.

225 The bondholders who hold bonds with covenants of both NNL and NNI contend that they would be unduly prejudiced by a pro rata allocation of the lockbox funds as they are entitled to look to both NNL and NNI for payment of their claims and if one of these companies did not have sufficient funds to pay the bonds in full, they could look to the other. I agree that they are entitled to claim against both companies and this will be recognized in the pro rata allocation that will be ordered.

226 The bondholders have the legal right to be paid in full on their bonds. But so do all of the other creditors. Like the pensioners and other creditors, the bondholders are not secured. Because of a shortfall in funds, all of these creditors cannot be paid in full. The issue is how the pain is to be shared.

227 The total cash on hand in the U.S. Debtors' and Canadian Debtors' Estates as of June 2014 was a little over 25% of the face amount of the outstanding bonds. Without an allocation from the lockbox funds of a sufficient amount to enable NNL and NNI to pay the bonds in full, the bond-

holders could not be paid in full. The bondholders, however, have no covenants in their bonds requiring the lockbox funds to be allocated in any manner, and specifically, no right to have lockbox funds allocated to NNL or NNI. Nor do NNL or NNI have any such rights. The lockbox funds are not the property of any one of NNL or NNI or any other RPE.

228 The bondholders are like other creditors in this regard. The other creditors of the Canadian Debtors could likewise argue that they will be prejudiced if the argument of the Monitor that all of the IP proceeds should be paid to NNL as the owner of the IP is not accepted. But the prejudice to be considered is not this kind of prejudice, but prejudice to legal rights. Neither the bondholders nor the other creditors of the Canadian Debtors have any legal right to have the lockbox funds allocated in a way that will benefit them.

229 The bondholders with covenants of NNL and NNI contend that their expectations will be disregarded by a pro rata allocation and that it will harm the bond markets if they are not somehow paid in full. I think this argument is overblown in this case and in any event not supported by any evidence of their expectations.

230 The evidence of Peter Currie, the CFO of NNC and NNL from 2005-2007, which is not contested, was that until the early to mid-2000s, Nortel's public debt was issued by NNL without guarantee from any other Nortel entity. In 2006, while Nortel's credit rating was still adversely affected by various factors, NNL issued notes having an aggregate principal amount of US$2 billion, which notes were conditionally guaranteed by NNI. NNI was a conditional guarantor in large part because at that time it carried certain hard assets on its balance sheet and because Nortel could obtain slightly better debt terms given that NNI was domiciled in the same place as the ultimate lenders, that is, the United States.

231 Thus it is quite clear from the evidence that when Nortel went to the bond market in 2006 and 2007 to raise funds, Nortel believed that it required the covenant of NNI in order to get the financing on terms and at a cost that Nortel wanted. However, prior to the Nortel insolvency in January, 2009, the market place did not differentiate in any material way the bonds that were guaranteed by NNI and the bonds not carrying a NNI guarantee.

232 From June, 2006 to December, 2008, Moody's and DBRS issued nine credit ratings for Nortel that did not distinguish between Nortel bonds guaranteed by NNI and those that were not. The UCC's expert witness Robert Kilimnik[22] agreed on his deposition that if a guarantee is a risk differentiator from DBRS's point of view, and there were a series of bonds with a guarantee and a series of bonds without a guarantee, he would expect them to be rated differently. This is an indication that the market did not differentiate between the NNC bonds guaranteed by NNI from those that were not guaranteed.

233 Another indication is the evidence of the Nortel bond spreads compared to U.S. government bonds contained in Ex. 58. The chart demonstrates that that Nortel bonds that carried an NNI guarantee traded at higher or equal spreads to Nortel bonds that did not carry an NNI guarantee. Mr. Kilimnik, an experienced bond trader, said on his deposition testimony was that bonds with a lower spread are considered less risky in the marketplace and that if guarantees were recognized by creditors as reducing the risk of issuances by the same company, he would have expected to see that expectation reflected in spread comparisons.

234 Mr. Paviter Binning, the Executive Vice-President and CFO of NNC from 2007 to March 2010 and an impressive witness to be sure, agreed with that conclusion of Mr. Kilimnik and testi-

fied that the data implied that the market was giving no value to the guarantees. He also testified that in his experience, investors generally looked to the overall quality of the company and that the guarantees were neither here nor there. He agreed that part of the reason why the guarantees may have had no meaning for the market was that the bonds were sub-investment grade in the first place. His evidence, which I accept, means that after the bonds were issued, the guarantees by NNI did not have a material effect on the marketplace.

235 John McConnell, a professor of business (finance) at Purdue University, delivered a report and testified on behalf the unsecured creditor's committee of NNI in response to a report of Leif M. Clark and Jay L. Westbrook, the latter of whom did not testify at the trial. Professor McConnell's report contained data from the date that the Nortel Group filed for protection on January 14, 2009 to January 2014 which indicated that the bonds not guaranteed by NNI traded at prices below the bonds guaranteed by NNI.

236 I do not see this data as relevant. Counsel for the bondholders in his opening asserted that the expectations of bondholders that are relevant are the expectations pre-petition and not post-petition.

237 If the expectations of those who purchased bonds post-petition were relevant, there was no evidence at all from such purchasers. Professor McConnell spoke to no bondholder and on cross-examination admitted that he had no way of knowing what factors went into the purchase and/or sale of any of the Nortel bonds by any of the current bondholders in the market post-filing. No bondholder testified or gave any evidence of expectations in acquiring bonds.

238 The evidence of Professor McConnell is based entirely on the fact that after the insolvency filings, bonds without a NNI guarantee traded at a lower price than those with a NNI guarantee. There are two points that can be made. The first is that his conclusion is an inference drawn from the trading price of the bonds after the insolvency as to what motivated those purchasers of the bonds after the insolvency. Second, there was no analysis of Professor McConnell that would lead to the conclusion that his inference of bondholder purchaser expectations could apply to purchasers of bonds prior to the onset of insolvency. He said he could not do such an analysis because before insolvency the bonds had different attributes which would not permit him to draw inferences as to the effect of guarantees. Be that as it may, I would not accept the inference drawn by Professor McConnell regarding the effect of the guarantees on a purchaser of bonds. I prefer the evidence of Mr. Binning to which I have referred.[23]

239 Moreover, the evidence is clear that bonds trade on a much different basis after insolvency. Mr. Binning testified that prior to the threat of insolvency, the bonds traded on a yield to maturity basis, meaning that bondholders take all of the payments that would be expected to be made if the bond is held to maturity, and then calculate a percentage yield based upon the price paid for the bonds. Once insolvency or financial distress is anticipated, Mr. Binning testified that bonds trade in the hands of distressed investors who trade not on a yield to maturity basis but in a classic arbitrage market based upon price and expectations of future price and what they think they can make on the bonds during insolvency. He advised the board of Nortel on September 30, 2008, three and a half months before the Nortel filing, that RBC had advised that approximately 50% of the bonds had traded into the hands of distressed investors.

240 Professor McConnell also testified that as new information came into the marketplace about the likely recoveries, that would be reflected in the price of the bonds. That is another way of

saying that distressed investors have bet on the future outcome of this case. This is reflected in the volumes and trading prices of the bonds at various times between January 14, 2009 and June, 2014, including (i) in the immediate aftermath of the Filing Date when the bonds were trading at very low prices, (ii) during the prolonged three-day auction resulting in the residual IP sale to Rockstar at the beginning of July 2011 as purchasers placed bets on bond price increases and recoveries following the completion of that sale; and (iii) in reaction to Delaware Bankruptcy Court Judge Walrath's September 2011 decision in *In re Washington Mutual* holding that post-petition interest must be awarded at the federal judgment rate and not at the rates in the various bonds.

241 The bondholders group that at the time of the trial held a majority of the unsecured guaranteed bonds purchased the vast majority of their holdings after the filing date of January 14, 2009 and at a significant discount to par. Certain members purchased when the bonds were trading at as low as 30 cents on the dollar and others received smaller, but still substantial, discounts. This can be seen in exhibits 59 and 60. The vast majority of their collective holdings were acquired in the period between July 31, 2009, at or around the time when Nortel began to liquidate its assets, and July 18, 2011, at or around the time of the Residual IP Sale.

242 The creditor expectations of the current bondholders, who acquired their bonds post-petition, even if known or supported by evidence, is not something I would take into account in this case. I infer from the evidence that any such expectations would have been based on their views as to litigation outcomes and should not be the basis of any decision by the courts.

243 In considering potential prejudice to the bondholders in the event of a pro rata allocation, consideration must be given to what the bondholders would gain. The bonds provide access to the assets of the issuer and guarantor. They do not provide any right to assets of any other entity in the Nortel Group. The 2006, 2007 and 2008 offering memoranda for the guaranteed bonds set out risks associated with the bonds, including the following notice regarding the lack of access to other Nortel entities:

> The Issuers' subsidiaries are separate and distinct legal entities and any subsidiary that is not a Guarantor will have no obligation, contingent or otherwise, to pay amounts due under the Notes or the Guarantees or to make any funds available to pay those amounts, whether by dividend, distribution, loan or other payment.

244 The offering memoranda also contained the following risk that investors would face in the event of insolvency of Nortel entities and the lack of access to the assets of those entities:

> In the event of a bankruptcy, liquidation or reorganization of any direct or indirect non-guarantor subsidiary of NNC, all of the creditors of that subsidiary (including trade creditors and creditors holding secured or unsecured indebtedness or guarantees issued by that subsidiary) and third parties having the benefit of liens (including statutory liens) against that subsidiary's assets will generally be entitled to payment of their claims from the assets of such non-guarantor subsidiary before any of those assets are made available for distribution to any Issuer that is a shareholder of such subsidiary. As a result, the Notes and the Guarantees are effectively junior to the obligations of non-guarantor subsidiaries.

245 Whereas the investors who acquired their bonds pursuant to the offering memoranda were specifically made aware that in the situation in which Nortel now finds itself, they would not have

access to assets of other Nortel entities that had not guaranteed the bonds, the effect of a pro rata allocation is to provide the current bondholders with such access. The lockbox funds represent the proceeds of sale of all of the assets of all of the 38 entities under the IFSA. Creditors holding guarantees have access under a pro rata allocation to not only the assets of the principal obligor and guarantor corporations, but the proceeds of sale of all the assets of the selling debtors. This is access to more pools of asserts than that for which the holder of a guarantee bargained.

246 While the current bondholders may have thought, or bet on an outcome, that NNL or NNI would likely achieve a win in this litigation that would provide those two companies with sufficient assets to pay the bonds in full and with post-filing interest, there was no guarantee at all that this would be achieved. The bonds contained no covenants that required the assets of NNL or NNI to be maintained at a certain level and no covenants that required the lockbox funds to be allocated in any manner. Mr. Binning had advised the Nortel board in September, 2008 that there were no maintenance covenants in the bonds, meaning that Nortel did not have to live up to any debt servicing ration . He testified that what the guarantees under these bonds essentially gave the bondholders was access to the assets in Canada and in the US without a great degree of comfort as to what those assets would be from time to time. I accept that evidence.

247 As to the effect of a pro rata allocation on the ability of issuers to issue bonds in the future, Professor McConnell on his cross-examination said that he had no opinion on that subject and that he had not tried to quantify what effect a pro rata allocation would have on the capital markets. Thus there is no evidence that a pro rata allocation in this case will detrimentally affect the capital markets and the ability of issuers to issue bonds in the future. Professor McConnell's statement that he had no opinion on the subject is perhaps not too surprising taken the highly unusual facts surrounding the Nortel insolvency and the difficulty of determining ownership of the IP that was sold.

248 It is said that the $2 billion claim of NNI against NNL that was approved by both courts is an impediment to a pro rata allocation. I do not think that is the case. The $2 billion claim will be treated as one of the unsecured liabilities of NNL.

249 The same principles that apply to the US$ 2 billion claim by NNI against NNL will apply to the admitted claim of NNUK and Nortel Networks SpA against NNL pursuant to the Agreement Settling EMEA Canadian Claims and Related Claims dated July 9, 2014, and to the claim of the UKPC for GDP339.75 million recognized in my judgment of December 9, 2014.

Appropriate pro rata allocation method

250 The allocation each Debtor Estate will be entitled to receive from the lockbox funds is the percentage that all accepted claims against that Estate bear to the total claims against all Debtor Estates.

251 In determining what the claims against a Debtor Estates are, a claim that can be made against more than one Debtor Estate can only be calculated and recognized once. The one that is known is the bondholder claim for $4 billion, referred to as the claim on cross-over bonds. All but one of such bond issues was issued by NNC or NNL and guaranteed by NNI. One bond issue for $150 million was issued by NNCC, a subsidiary of NNI, and guaranteed by NNL[24]. The claims on the bonds in determining the claims are to be made on the Debtor Estate of the issuer. If a claim on a guaranteed bond is not paid in full by the issuer Debtor Estate, a claim for the shortfall can be recognized by the Debtor Estate that guaranteed the bond, but that shortfall claim will not be taken into account in determining the claims against the Debtor Estates.

252 One of the known claims is the claim of the UKPC for the approximately GDP2.2 billion deficit in the NNUK pension plan. If the UKPC makes a claim for this amount against NNUK and also against other EMEA Debtors, those claims against the other EMEA Debtors will not be taken into account in determining the claims against the Debtor Estates. The claim may be taken into account only once in the pro rata allocation.

253 I understand that for the Canadian Debtors and the U.S. Debtors, the claims for the most part are generally known although there are some claims still unresolved, such as the SNMPRI claim. The U.K. Administrator has not yet instituted a claims procedure, apparently awaiting a determination of this allocation proceeding. In my view, the process should be undertaken now and I expect this will happen.

254 Interim distributions have been proposed. In my view, this would be especially important for the predominantly elderly pensioner population and disabled employees who have endured hardship as a result of the loss of their benefits but also for other creditors who have waited more than five years for a distribution on their claims. An interim distribution should be made if possible.

255 Briefs should now be filed by those parties supporting an interim distribution with full details of what is requested. Opposing briefs would of course be required. The procedures and timing could be discussed at a 9:30 am appointment.

Allocation on a basis other than pro rata

256 The evidence on this subject was complex and varied dramatically from party to party. To wit:

(a) The Monitor on behalf of the Canadian Debtors contended for an allocation of $6.034 billion to thc Canadian Debtors, $1.001 billion to the U.S. Debtors and $300.7 million to the EMEA Debtors.[25]

(b) The U.S. Debtors contended for an allocation of $0.77 billion to the Canadian Debtors, $5.3 billion to the U.S. Debtors and $1.23 billion to the EMEA Debtors.

(c) The EMEA Debtors contended for an allocation of $2.32 billion to the Canadian Debtors, $3.636 billion to the U.S. Debtors and $1.325 billion to the EMEA Debtors.

257 I have given consideration to the valuation issues. To a great extent, they are dependent on the various interpretations of the MRDA asserted by the parties. For that reason I would not use any of the valuations for the purpose of the pro rata allocation as I have found that the MRDA does not govern the allocation. However, my views and findings on the valuations are set out in Appendix A for the business line sales and Appendix B for the residual IP sale to Rockstar.

Conclusion

258 A judgment is to go that the lockbox funds are to be allocated on a pro rata allocation basis with the following principles to govern:

(1) Each Debtor Estate is to be allocated that percentage of the lockbox funds that the total allowed claims against that Estate bear to the total allowed claims against all Debtor Estates.

(2) In determining what the claims are against the Debtor Estates, a claim that can be made against more than one Debtor Estate can only be calculated and recognized once in accordance with these reasons for judgment. Claims on bonds are to be made on the Debtor Estate of the issuer. A claim for any shortfall can be recognized by the Debtor Estate that guaranteed the bond, but that shortfall claim will not be taken into account in determining the claims against the Debtor Estates. If the UKPC makes a claim against more than one Debtor Estate, such additional claims will not be taken into account in determining the claims against the Debtor Estates.

(3) Intercompany claims against a Debtor Estate are to be included in the determination of the claims against that Estate.

(4) Cash on hand in any Debtor Estate will not be taken into account in the pro rata allocation. Each Debtor Estate with cash on hand will continue to hold that cash and deal with it in accordance with its administration.

(5) An interim distribution may be allowed upon further submissions. Briefs in favour of and opposed to an interim distribution are to be filed on a time-line to be considered at a 9:30 am appointment.

(6) Proposed schedules for expediting any remaining claims procedures are to be provided without delay.

Epilogue

259 I cannot leave these reasons without commenting on the persons who made this unique case possible.

260 First, to the technical staff who provided the facilities to permit this trial to be conducted in two different countries at the same time, I say it was a job more than well done. It was outstanding and we are indebted to you all. Judge Gross and I have no idea how it was all set up and operated, but I know he is as grateful for the facilities as I am. Thank you.

261 Second, to the reporters and their staff, it was also a job more than well done. Apart from the instantaneous real time reporting that permitted all parties to see the evidence as it was being given, we were blessed with draft transcripts being electronically sent to us shortly after the evidence concluded each day and final transcripts later that evening.

262 Third, to the lawyers. We were blessed with outstanding counsel on both sides of the border. In a case such as this with the amount at stake, one can understand the pressures on counsel and how those pressures could get in the way of a smooth preparation and presentation of the case. From what I could see, all acted in a professional manner that does them credit. Without that, the case could not have proceeded as well as it did. Their staff should also be congratulated for the smooth way in which the case was electronically presented. It was a marvel.

263 Finally, I want to thank Judge Gross for his courtesies and good humour. It has been a pleasure to work with him. Without such a good relationship and the trust that we developed for each other, this trial and its conclusion would not have been possible.

F.J.C. NEWBOULD J.

* * * * *

APPENDIX A

Allocation of the proceeds of the line of business sales

[1] The experts for the various parties differ on the way that the proceeds of the sales of the LOB should be allocated amongst the Canadian estate, the U.S. estate and the EMEA estate.

[2] Mr. Kinrich, the valuer called by the U.S. Debtors, did not value the various assets sold and attempt to allocate them by any particular method. Rather he allocated the entire sale proceeds by taking the revenues of each company whose businesses were sold and allocating to each company (and the group they were in) the percentage of its revenues to the total revenues of all companies whose businesses were sold. His resulting allocation was 11.9% or $340 million to the Canadian Debtors, 18% or $510 million to the EMEA debtors and 70% or $1.99 billion to the U.S. Debtors.

[3] Mr. Malackowski called by the EMEA debtors valued the IP rights sold by using a revenue or license valuation method. His valuation of the IP sold in the business sales was $765.2 million.

[4] Mr. Huffard called by the EMEA debtors then allocated the various kinds of assets sold. He valued the tangible assets that were sold at $118 million and allocated this amount to the companies that sold them. He allocated the IP that was sold and valued by Mr. Malackowski at $765.2 million by a contribution approach which allocated the IP according to the amount of R&D expenditures of each of the RPEs. He attributed the balance of the LOB sale proceeds as "customer related assets and goodwill" and allocated them on the basis of the percentage of revenues generated by each entity in 2008. Mr. Huffard did not give a separate total figure in his report for the allocation of the LOB sale proceeds.

[5] Mr. Green called by the Canadian Debtors dealt with each kind of the various assets sold. He allocated the tangible assets sold by giving to the companies that sold them their book value, which he calculated to be $534.19 million. He valued the workforces sold by their cost that the selling companies would incur to replace them at $255.33 million and allocated those costs to the companies. He allocated the IP and customer relations by valuing what the licensed participants gave up to enable the sales on the basis that their license rights were limited to the "Products" "by or for the Participants" as defined in the MRDA, and allocated the balance of the sale proceeds to NNL as the "owner" of the IP. His resulting allocation was 54.8% or $1.58 billion to the Canadian Debtors, 10.4% or $300.97 million to the EMEA debtors and 34.7% or $1001.5 billion to the U.S. Debtors.

(i) Mr. Kinrich

[6] Mr. Kinrich's view is that the RPEs that were licensed participants had all license and sublicense rights as owners. Assuming that to be the case for this analysis, I have some concerns with his analysis. Mr. Kinrich allocated all of the assets sold in the business sales on a revenue basis. He stated in his report that the value of the sold assets is reflected in the revenue generated by each entity that sold the assets. That is, value he said was reflected in revenue figures.

[7] Mr. Kinrich himself in his report said that financial economists agree that a discounted cash flow analysis is the preferred technique for asset valuation and that one of the requirements is to have projected future cash flows less costs. In his report he did not say why he had not done such an analysis when dealing with the business sales. At trial he relied on texts to support his use of a revenue approach in firms with losses, one of which is *Valuing Small Businesses and Professional Practices*, which suggests gross revenue multiples may be used in restricted situations, being to approximate a range of possible values with a minimum effort, conclude an estimate of value when other data are unavailable or inadequate or as one indicator of value used in conjunction with more rigorous valuation methods. The text also said that for companies with losses or erratic earnings, multiples of price to revenue for other comparative companies may give some indication of how others asses the future of the industry or profession. But that is not what Mr. Kinrich did. He did not look at revenue multiples from the sale of any comparable companies. I viewed his attempt to bolster his revenue approach by resort at trial to texts to be an attempt at *ex post facto* rationalization. It would have been a little more persuasive if these rationales has been provided in his report, particularly as in his report he did a sensitivity check based on gross margin (revenue less cost of goods sold) and contribution margin (revenue less selling, general and administrative expenses).

[8] Mr. Kinrich said at trial that he did not have available forecasts that would divide income streams by territory but that is beside the point so far as a gross revenue valuation is concerned. The issue is whether it would have been preferable to take costs into account in his revenue approach to allocation.

[9] Because the U.S. market had the highest revenues, it follows that using a revenue approach as Mr. Kinrich did will result in the high allocation of the business sale proceeds to the U.S. (70%) and a low allocation to Canada (11.9%). However, because revenue does not consider costs, this result ignores the way in which Nortel operated as a matrix structure and the reliance by all operating areas, including the U.S., on IP generated by R&D elsewhere. The 2009 revenue that Mr. Kinrich used in his analysis to compare revenues, the basis of which was assumed license rights under the MRDA, was subject to the obligation in the MRDA to make payments pursuant to the RPSM measured by R&D expenditures of each RPE. Mr. Kinrich did not take into account.

[10] Mr. Kinrich acknowledged on his cross-examination that while he assumed that the set of license rights as he saw them would continue in the future to exist, he gave no effect to sharing obligations that might arise under the MRDA, his reason being that he understood that the sharing provisions did not apply to sales proceeds. That in my view was no answer. What he undertook was to determine the relative value surrendered by each of the selling entities, including the RPEs. To determine the value of rights of each of the RPEs without taking into account the RPSM sharing obligations failed to properly determine relative values among the RPEs. I accept the opinion of others, including Dr. Bazclon and Mr. Green, on the point. The various businesses in Nortel historically operated on varied operating margins.

[11] Mr. Green pointed out, with reference to texts including those that Mr. Kinrich referred to at trial, that a disadvantage of focusing on revenues is that it can lull one into assigning high values to firms generating high revenue growth while losing money and that the method assumes that the businesses are equally profitable. His view was that a revenue based allocation was inappropriate in a matrix structure such as Nortel with interrelated operating businesses in which certain entities bore disproportionate shares of expenses like R&D which would be ignored.

[12] EMEA and the UKPC contend that Mr. Kinrich should not have used 2009 revenue figures as 2009 was an anomalous year for Nortel. Nortel filed for insolvency protection in January 2009 and from then on was operating under the supervision of courts in Canada, the US, the UK, and elsewhere. Throughout 2009, Nortel was actively engaged in selling its businesses, signing seven out of eight of its sale agreements in that year. All of this affected its ability to generate revenues. Four of the business sales were concluded before the year's end. Because of these dispositions, complete financials for 2009 were not even available for certain businesses and revenues had to be estimated based upon performance prior to the sale closing date.

[13] Dr. Bazelon's evidence was that NNI's share of global revenue plateaued by 2008 at about 65% but in 2009 it increased by about 4%. In my view, EMEA and the UKPC have a valid point. 2009 was not a typical year for Nortel. While NNI contends that 2009 resembles the weighted average over the years 2001 to 2008, but that ignores the steadily declining trend from NNI having 74% in 2001 to about 65% in 2008. Using 2009 for his revenue analysis was overly aggressive. The effect was to shift about 4%, or $100 million, from EMEA to the U.S. Debtors.

(ii) Mr. Malackowski and Mr. Huffard

[14] The allocation of the proceeds of the LOB sales on behalf of the EMEA Debtors is based on the evidence of Mr. Malackowski who valued the IP sold at $765.2 million and on the evidence of Mr. Huffard who allocated all of the sales proceeds using different methods for each type of asset sold. There are problems with the EMEA allocation.

[15] Mr. Malackowski used a discounted cash flow analysis to value the IP. He said there was a defensive component and a synergistic component to the IP. To measure the defensive component, he took the revenue forecasts of Nortel in the "deal books", market derived growth rates, and royalty rates from an IPCo model. For a discount rate he used an average of weighted average cost of capital rates of the industry in which the Nortel business operated. To measure the synergistic component, he used revenues of a hypothetical market participant for each line of business sold, market derived growth rates, and royalty rates derived from what he said was the implied rate paid by Ericsson as a member of the Rockstar consortium. He added 15% to the discount rate used in his defensive component.

[16] Mr. Malackowski's valuation of the IP sold at $765.2 million, if accepted, means that the IP represented roughly 25 % of the total sales proceeds of $3.1 billion. Yet, the evidence is overwhelming that IP created by Nortel's R&D was the driver of the profitability of the business. Even Mr. Huffard view was that within Nortel, IP was considered the driver of revenue in each of the businesses and purchasers of the businesses would have considered the acquisition of IP as a critical aspect. Mr. Britven, an expert called by the CCC, arrived at figures based on the purchase price allocations made by the purchasers that stated what the purchasers considered the fair value of the various acquired assets to be. Those figures put the percentage of the IP of the total business sale proceeds at 40%.

[17] In his rebuttal report, Mr. Malackowski in an attempt to show the size of what he considered to be a windfall if the position of Mr. Green were accepted, said that all of the Nortel the IP in total in the hands of Nortel could be worth $10.4 billion, of which he allocated $3.761 to the business sales and $6.6 billion to the residual sale to Rockstar. His reason for this extra value in his report was that some of the residual IP sold to Rockstar was encumbered by the non-exclusive licenses given to the purchasers of the lines of business. Rockstar paid $4.5 billion. If Mr. Malackowski's figures are

right, it means that the non-exclusive licenses given to the purchasers of the lines of business reduced the value of the residual IP sold to Rockstar from $6.6 billion to $4.5 billion, or by $2.1 billion. That reduction in value to Rockstar attributed to the non-exclusive licenses granted in the business sales means that those non-exclusive licenses were worth $2.1 billion, and it does not make sense that Mr. Malackowski valued both the outright licenses and the non-exclusive licenses given to the purchasers of the lines of business at only $765.2 billion.

[18] The Monitor points out that the royalty rates used by Mr. Malackowski in establishing revenues to be valued were taken from the IPCo litigation light model and that within that litigation light model he chose the lowest of three rates. He did not use any Nortel intercompany-stated royalty rates. The Monitor suggests that is an explanation why the IP valuation of Mr. Malackowski is too low. For certain the royalty rates charged directly affect the revenues and thus the value obtained by a DCF method of valuation. Whether it is the only reason for the low valuation is another matter. There are many inputs in a valuation.

[19] Mr. Huffard was the expert called by EMEA to opine on the allocation to be made of each component of the business sales. The Monitor is critical of his qualifications. Mr. Huffard is an investment banker with considerable experience advising distressed companies who has "led valuation analyses" for companies and their assets. He holds a Master of Management degree from Kellogg Graduate School of Management at Northwestern University. Mr. Huffard is not accredited as a valuator and said that in the field of investment banking that is typical.

[20] I must say that Mr. Huffard was not forthcoming in his evidence about his experience. When asked if he had done any valuations or the allocating of assets in connection with intellectual property companies, he said several times that he had trouble understanding what an intellectual property company was and asked if Nortel was an intellectual property company. Yet when asked on his deposition whether he had done any valuations or the allocating of assets in connection with intellectual property companies, he answered "Not in connection with intellectual property companies." I think it fair to consider this answer in dealing with his evidence.

[21] Mr. Huffard believed that there were three classes of assets to be valued and examined in the business sales. The first is net tangible assets. The second is the IP. The third is customer-related assets and goodwill not otherwise encompassed in goodwill. Mr. Huffard did not do any valuation exercise for his third class. Rather he just took the balance of the purchase price and allocated it. The values attributed to the first two classes therefore directly affected the value of his third class.

[21] For the tangible assets, Mr. Huffard took the book values of the assets, which consisted of accounts receivable and prepaid expenses, inventory and fixed assets. This book value in his report totalled $403 million. At trial, in his demonstrative exhibit, his total was $361 million. Why the difference was not explained. From the book values, Mr. Huffard deducted liabilities assumed by the purchasers of the lines of business, the largest of which was deferred revenue. He viewed the assumed liabilities as a fourth asset class that resulted in an increase in the purchase price from the buyer's perspective and a reduction from the seller's perspective. They had to be deducted from the assets and he did this the tangible asset class. This resulted in net tangible assets in his report of $124 million, being $39 million for Canada, a negative $27 million for EMEA, $106 million for the U.S. and $6 million for Asia and the Caribbean. At trial, his demonstrative showed the net tangible assets at $118 million with the same net figures for Canada, EMEA and the U.S. as in his report. How this occurred on the different book values in his report and in his demonstrative was not explained.

[22] For the allocation of the IP, Mr. Huffard took Mr. Malackowski's figure of $765.2 billion. He allocated them amongst the RPEs using Mr. Malackowski's contribution approach using historical R&D spending from 1992 to 2008. His view was that the portions of the sale proceeds attributable to IP were, in effect, a capitalization of future revenues that would otherwise have been shared among the RPEs in accordance with the RPS methodology. This resulted in 40.8% or $312.2 million being allocated to Canada, 42.6% or $326 million being allocated to the U.S. and 16.5% or $126.2 million being allocated to EMEA. In his demonstrative at trial, these percentages were rounded, with 41% to Canada, 43% to the U.S. and 16% to EMEA.

[23] Mr. Huffard then included the balance of the sale proceeds of $2.198 billion into his third class of customer-related assets and goodwill. He did no analyses of the value of either the customer-related assets or of the goodwill and allocated them based on the revenue generated by each entity in fiscal year 2008. He said he did not use net revenues to allocate among the entities because in his view cash flows are influenced by transfer pricing and inter-company arrangements for tax purposes. Based on the revenues alone, he allocated 9.2% or $202 million to Canada, 62.6% or $1.375 million to the U.S., 18.6% or $155 million to EMEA, 2.6% or $57 million to the Caribbean and 7.1% or $155 million to Asia.

[25] While Mr. Huffard did not provide a total for the business sales allocation, by adding up the different classes, his total allocation to Canada was $553.2 million to Canada, $1.807 billion to the U.S. and $254.2 million to EMEA. This is somewhat less than the $2.85 billion available from the business sales proceeds.

[26] As Mr. Huffard did not undertake any valuation of his third residual category, his conclusion of the amount to be included in it is dependent upon the amount of his tangible asset valuation and Mr. Malackowski's IP valuation. If Mr. Mr. Malackowski's IP valuation is too low, then the amount in this residual class allocated by Mr. Huffard will be too high.

[27] There are problems with allocating this residual class entirely by revenues of each company or groupings of companies. Mr. Huffard described it as the value of customer-related assets and goodwill not otherwise associated with IP. He acknowledged that these assets, like any other assets, have their value fundamentally related to their ability to generate profits, and that while Nortel operated the businesses, it was not revenue that allocated those values but the RPS method of sharing profits after revenues and costs were calculated. This is the same criticism made of Mr. Kinrich in using a revenue tool to allocate the sales proceeds rather than a profitability tool.

[28] Mr. Huffard acknowledged that in circumstance where, because of decisions made and cost-effectiveness and historic reasons, sales and customer support was done in a country which had low domestic revenues, his revenue allocation method for the customer-related assets and goodwill category was not going to compensate that country because it had low revenues. This circumstance was commonplace in Nortel with its matrix structure, with customer support carried out in one country for sales in another. He acknowledged if a large percentage of the workforce is in a place like Canada, which does R&D and which does sales support and supports the global organization but doesn't have a large native revenue stream, he was allocating the value of that workforce to the other entities where there is a revenue stream and not to Canada.

(iii) Mr. Green

[29] Mr. Green valued different asset classes differently. He first valued tangible assets by taking their book value and allocating them to the companies which owned them. This was the same method used by Mr. Huffard. However, different from Mr. Huffard, he did not deduct any deferred liabilities from the tangible asset amount. His evidence was that deferred liabilities are essentially amounts that would be due that are related to projects that have already been billed and perhaps paid for and so they didn't offset the physical assets, the tangible assets such as the accounts receivable, the other things that were sold. He pointed out that by his not deducting deferred liabilities, it was to the relative benefit to the U.S. Debtors because they had the highest deferred revenues and, accordingly, deducting the liabilities would most significantly decrease the U.S. Debtors' share of the value of net tangible assets. He also pointed out in his rebuttal report that not all liabilities recorded on the books of Nortel were assumed by the purchasers and for those that were it was not possible to determine on which entity's books those liabilities were recorded. I accept this position of Mr. Green in not deducting assumed liabilities in valuing and allocating the tangible assets on the basis of book values recorded on each entity's books.

[30] Mr. Green's value for the tangible assets was $534.19 million, and he allocated $121.74 million to the Canadian Debtors, $317.59 million to the U.S. Debtors and $94.86 million to the EMEA Debtors.

[31] Mr. Green next valued the workforce in the lines of businesses that were transferred to purchasers. His opinion was that generally speaking, the cost approach is applied to the valuation of an assembled or in-place workforce. He valued the workforce by calculating the cost to replace the work force. He concluded that the total value of the work force was $255.33 million and he allocated $78.68 million to the Canadian Debtors, $134.74 million to the U.S. Debtors and $41.91 million to the EMEA Debtors.

[32] In the sale of the Enterprise business, several corporate entities owned by NNI were sold. Mr. Green valued these assets based on contemporaneous fair market valuations done at the time these businesses were sold. There is no evidence that these assets had a value other than as set out by Mr. Green. Mr. Green made an allocation to NNI of proceeds attributable to the sale of its subsidiaries in the amount of $110,970,000. No other valuer dealt with this asset.

[33] Mr. Green was of the view that once the tangible assets and the workforce were valued, the balance of the business sale proceeds was attributable to IP, the primary driver of Nortel's value, and customer relationships. He valued and allocated the IP and customer relationships sold in the business sales by valuing the license rights of NNI and the EMEA RPEs surrendered by them to permit the sales to take place on the basis that their licenses were restricted to Products by or for the Participants as defined in the MRDA and as contended by the Monitor. The balance he attributed to NNL as the owner of the IP.

[34] Mr. Green performed a DCF valuation. He projected revenues and expenses for each business sold and for this to project the future revenues of the Nortel businesses he used forecasts prepared by Nortel that were referred to as "Retained by Nortel" forecasts. They projected the revenues that would have been earned and the expenses that would have been incurred, if the operating businesses had been retained by Nortel. After calculating the operating profits of each business sold, Mr. Green aggregated those profits and applied the RPSM on the assumption that the MRDA would have remained in place, using the capital stock percentage for the first quarter of 2010, which covered a rolling average from 2005 to 2009. He applied a discount rate of 12% for the operating profits derived from existing technology and 30% for operating profits to be derived from yet to be invented

technology and thus more risky. He concluded that the value of the license rights surrendered by NNI was $438.2 million and by the EMEA RPEs was $164.2 million. The balance of his residual amount, being $1.379 billion was allocated to NNL.

[35] Mr. Green's resulting allocation was 54.8% or $1.58 billion to the Canadian Debtors, 10.4% or $300.97 million to the EMEA debtors and 34.7% or $1001.5 billion to the U.S. Debtors.

[36] EMEA and the U.S. Debtors contend that a basic problem with Mr. Green's analysis is his conclusion or assumption that NNL was the owner of the IP and entitled to its residual value after deducting the license rights of EMEA and NNI which he limited to Nortel Products by or for the Participants. This is a basic legal issue.

[37] EMEA argues that customer relationships were very important to Nortel and that they should have been valued and allocated separately from IP and not included in Mr. Green's residual category. Mr. Green's explanation for not doing so was that customer intangibles represented historical relationships in which customer files and ongoing agreements exist, the value of which was represented in his revenue figures that he used and were thus subsumed in the IP license rights which he valued. He said that a separate valuation of customer relationships would be duplicative of the values of the license rights surrendered because it would be based on the same revenues and profits as used in the license rights valuation.

[38] Mr. Malackowski argued that the MRDA did not transfer customer relationships to NNL. This does not strike me as a valuation concept and one can argue, as the Monitor does, that NN Technology was owned by NNL and it included all intangibles.

[39] This is a valuation issue. There is no question that customer relationships were important to Nortel. However that is not the issue. The issue is how to value them. Mr. Berenblut was of the opinion that customer relations were co-mingled with IP rights because the value to use them depended on the ability to sell Nortel products and that their value would be included in the value of rights to sell Nortel products. Dr. Bazelon, an EMEA expert, agreed on cross-examination that goodwill and customer relationships are entangled with the IP and take their value from the IP, at least in part. Brian McFadden, the Chief Technology Officer at Nortel for some time, said that R&D was crucial in initiating relationships with and developing sales from customers for Nortel products. I accept Mr. Green's opinion that no separate valuation needed to be made for customer relationships.

[40] It is also argued that Mr. Green should have separately valued and allocated goodwill. Mr. Huffard included goodwill in his residual class, although he did not attempt to value it. Mr. Britven, called by the CCC, included a value for goodwill in his business sales analysis. He took what the purchasers had allocated in their PPAs as goodwill, and referred to it as Purchaser Goodwill.

[41] Mr. Green's response to this is that Nortel wrote off all of its acquired goodwill at the end of 2008. This indicated that, at the time, Nortel management did not believe it would be able to realize the value of the goodwill from these acquisitions in the future. As for its own "internal goodwill," Nortel was suffering losses from its operations and was not generating positive cash flows. Thus, from an accounting and finance perspective, Nortel had no goodwill from its own operations. By classifying the residual value as goodwill, Mr. Huffard accounted for an asset that did not exist within Nortel and was not transferred to the buyers. By applying the buyer's perspective, Mr. Huffard failed to answer the question of how to allocate the sales proceeds according to the value of the interests each of the Debtors transferred and rights each of them relinquished.

[42] There is actually support for Mr. Green's position in Mr. Britven's report in which he included a value for goodwill taken from the purchasers' PPAs. These purchaser allocations are done by purchasers for accounting purposes and usually are driven in part at least by tax considerations. Mr. Britven said that Nortel wrote off the value of substantially all of the goodwill that it had on its balance sheet. He said that Nortel did not have sufficient value to support any significant goodwill value and that the goodwill in the business sales related to the attributes of the buyer, not the attributes of Nortel. He said that any goodwill recognized by purchasers in their PPAs did not reflect amounts that could have been realized by the licensed participants through the continued operations of their lines of business.

[43] I agree with Mr. Green's approach to goodwill and accept his opinion that there was no goodwill value in the Nortel businesses that were sold.

[44] Regarding the DCF method used by Mr. Green to value the U.S. and EMEA license rights, Mr. Kinrich was critical of the revenue forecasts used by Mr. Green and stated that he had not followed the International Financial Reporting Standards which state that in measuring value in use, an entity shall base cash flow projections on reasonable and supportable assumptions that represent management's best estimate of the range of economic conditions that will exist over the useful life of the asset.

[45] This IFRS material was not put to Mr. Green on his cross-examination, which it should have been for this argument to be made. However, I do not think the criticism is justified. Mr. Green used projections made by Nortel. He used projections referred to as a "Retained by Nortel" scenario which projected what revenues and expenses would be either retained by Nortel or spun-out on its own as a stand-alone company. He declined to use Nortel's "Safe Hands" projections for several reasons that he explained, including the fact that they forecasted the businesses in the hands of a well-capitalized third party who could invest adequate capital in the business and who could earn greater profits than if they remained in Nortel's hands. Mr. Green did no DCF analysis as he allocated the business sales solely on revenues.

[46] Mr. Kinrich was also critical of Mr. Green for not including a terminal value in his DCF valuation. Mr. Green's explanation for this on his deposition was that in his present value analysis, at year nine the present value factors were close to zero. So even if there were a terminal value, it would be virtually of no value in a present value computation. In his report, he said he thought that to include potential profits after nine years was too speculative. There is no competing DCF valuation to indicate what Mr. Green did was wrong.

[47] Mr. Green's analysis in part is dependent on the interpretation of the MRDA advanced by the Monitor on behalf of the Canadian Debtors. One cannot quarrel with thc logic of it if that interpretation were to govern the allocation.

* * * * *

APPENDIX B

Residual IP proceeds allocation

[1] The residual IP was sold to Rockstar for $4.5 billion. After payment of a break fee and expense reimbursement to Google, the remaining net proceeds held for allocation amount to $4.45 billion.

[2] There is differing expert opinion as to how to allocate the proceeds of the Rockstar sale amongst the Canadian debtors, the U.S. debtors and the EMEA debtors.

[3] Mr. Green allocated the proceeds on the basis of his interpretation of the MRDA under which it was NNL that owned all of the patent rights that were sold to Rockstar.

[4] Mr. Kinrich for the U.S. debtors allocated the proceeds on a revenue approach on the basis that each Participant owned all of the economic rights to the patent rights sold to Rockstar in their exclusive jurisdictions and that their revenue streams that they gave up should be valued. Mr. Green as an alternative analysis for the Canadian debtors and Mr. Malackowsi as an alternative analysis for the EMEA debtors prepared valuations correcting what they saw as errors by Mr. Kinrich.

[5] Mr. Malackowski allocated the proceeds on a contribution basis by calculating what he saw as the contributions by each of the Participants to R&D over the life of the patents that were sold to Rockstar.

(i) Mr. Kinrich's license approach to value

[6] Mr. Kinrich assumed that each of NNL, NNI and the EMEA debtors owned all of the economic benefits of the residual IP. He allocated all of the Rockstar proceeds to NNL, NNI and EMEA by taking what he said would be the revenue earned in each of those three geographical areas and then doing what he said was a discounted cash flow analysis ("DCF") on those revenue streams. I have held that the Licensed Participants did not own all of the economic benefits of the residual IP. However, on the assumption that they did, I will consider Mr. Kinrich's analysis.

[7] Mr. Kinrich obtained his revenue streams by taking one of the IPCo revenue model assumptions. He then apportioned the net revenues after costs and taxes to each of the three geographical areas by using those countries' relative telecom infrastructure expenditures for six of the eight IPCo franchises that Nortel had and apportioning all of the net revenues after costs and taxes for two of the franchises (PC and Internet advertising) to the U.S. He then applied a discount rate to those net cash flows allocated to each country.

[8] I have considerable difficulty with a number of aspects of Mr. Kinrich's analysis. If the value of the net cash flows as stated by Mr. Kinrich is overstated, the overstated amount would belong to NNL, as the amount of the sales proceeds from the Rockstar transaction would represent more than the value of the net cash flows, which on Mr. Kinrich's assumption is what the Licensed Participants gave up in the Rockstar sale. The expert evidence called by the Monitor is exactly to that effect, contending that Rockstar paid more than the value of the cash flow projections from the IPCo model for other motives.

[9] Nortel had no material business licensing its IP or monetizing its technology by suing others, either before or after filing for protection from creditors in early 2009. Mr. John Veschi had been hired in July 2008 to take responsibility for Nortel's IP group and to look at options for licensing its IP.

[10] Development of the IPCo option was led by Mr. Veschi after the insolvency filings. The premise of IPCo was that the residual patents would be monetized by the threat of patent infringement litigation and, if necessary, actual infringement proceedings against various technology companies in an attempt to force such companies to pay royalties to IPCo. It was considered important that IPCo not carry on any telecommunications or other technology business, because, if it did, it would

be vulnerable to counterclaims for alleged infringement being brought by the targets of its infringement litigation, which would undercut its revenue generating ability.

[11] Over the course of 2009 and 2010, Mr. Veschi and his team, assisted by Lazard Frères & Co, Nortel's financial advisor, and Global IPCo, a law firm specializing in patent sales, prepared several versions of a preliminary financial model, in an attempt to forecast the operating profit that could be earned by IPCo so that the potential economic benefits could be weighed against value expected to be received on a sale of the portfolio.

[12] The various versions of the preliminary financial model had three sub-models, with differing assumptions relating to how much litigation IPCo would pursue. The scenarios were dubbed "Harvest" (assuming very little litigation), "Litigation Light" and "Litigation Heavy". More litigation resulted in greater forecast revenues, at greater forecast cost. Assumptions regarding litigation success of 60 percent, 70 percent and 100 percent were used. A wide variety of assumed net cash flows were used and a variety of discount rates to value the cash flows were used.

[13] There is a difference in the evidence of Sharon Hamilton, a partner of Ernst & Young, the Monitor, and Mr. John Ray, the principal officer of NNI, as to how reliable the IPCo forecasts were. Ms. Hamilton was of the view that the projected cash flows were largely guesswork, given that Nortel had little experience in licensing and there were no good precedents about the estimated cash flow. Mr. Ray was more confident of the forecasts taken the work that went into them.

[14] What is clear is that there were a number of different models. Version 1 was presented on March 10 2010, version 2 on April 27, 2010, version 2.2 on May 6, 2010, version 3 undated, version 3.1 on October 25, 2010 and version 4 on November 18, 2010. Each version had different cash flow forecasts.

[15] I think it fair to conclude that the forecasts were not considered to be in any way certain. There were many permutations and combinations, and at no time did Nortel agree that any one forecast was the appropriate one. The process never got that far before the decision was made not to operate IPCo but rather to sell the residual IP.

[16] Mr. Kinrich chose to use version 3.1, although he did not explain why. Version 3.1 had the highest cash flows of all versions. It is noteworthy that the latest version 4 had projected cash flow forecasts of approximately half of what was projected in the earlier version 3.1 used by Mr. Kinrich.

[17] Mr. Green, an expert valuer called by the Monitor, points out that version 3.1 itself was not a finalized document or accepted by Nortel or its advisors. Within it there were a number of scenarios and options still being explored. The unreliability of the forecasts in the various models can be seen by the wide disparity in discount rates used. Lazard used discounts of 25, 35 and 45% to value the various projected cash flows. These are very high discounts, as more than one expert testified, and indicated a high risk to the cash flows being achieved. Mr. Kinrich used much lower discount rates of 12% and 15%, which I will come back to, which did not reflect the risks in the IPCo forecasts and which caused a higher valuation of the cash flows than would be the case if the discounts used by Lazard in the IPCo models were used.

[18] While there were multiple scenarios in the version 3.1 model, Mr. Kinrich used only the most aggressive case that maximized revenue. Mr. Green's view is that there is inadequate explanation by Mr. Kinrich why the specific scenarios of Version 3.1 were selected for the analysis as opposed to other lower cash flow scenarios or the later Version 4 model with lower cash flows and as the anal-

ysis is unsupported, it makes the valuation unreliable. I must say that in reviewing the details of Mr. Kinrich's report it is not at all apparent what his justification was for using the cash flows that he did. It leaves an open question as to the reliability of what Mr. Kinrich was doing.

[19] The value allocated to each of the debtors by Mr. Kinrich is based on the attribution to the geographic regions of the debtors of the projected operating cash flows in the IPCo model chosen by Mr. Kinrich. Those cash flows projected royalty payments on a regional level, namely North America, EMEA and China.

[20] The IPCo model estimated North American licensing revenue based on sales in Canada and the U.S. Mr. Kinrich apportioned the revenue to Canada and the U.S. using those countries' relative telecom infrastructure expenditures, saying that relative telecom expenditures were a reasonable basis on which to estimate relative market size and were consistent with the structure of the IPCo model that used market size as the driver of royalty revenues. He did the same thing for EMEA as the IPCo model estimated EMEA revenue based on sales in France, Germany and the U.K.

[21] Global IPCo, the IPCo law firm retained to assist in preparing the models, stated early on in their work that they had no opinion regarding the territorial split of patents or patent-related revenue. There was certainly no agreement by any of the Nortel entities as to how the projected IPCo cash flows would be split territorially.

[22] Mr. Kinrich then deducted costs from the revenue streams including a number of litigation costs. It is not possible from looking at his report to know exactly what level of litigation costs was assumed by him.

[23] After calculating the net cash flows for each country, Mr. Kinrich then said he did a discounted cash flow calculation to arrive at a valuation for each country. In my view, Mr. Kinrich did not carry out a valid DCF valuation. The discount rate he used was not appropriate and was not derived by any conventional valuation approach.

[24] Mr. Kinrich acknowledged in his evidence that a DCF analysis requires knowledge about the cash flows over time and requires a discount rate to take those cash flows over time and convert them to present value. He acknowledged in his report that typically a discount rate is derived from the cost of capital (the cost of debt and equity split on some basis), referred to by valuators as the weighted average cost of capital. However, he did not do this. Instead he said that the value of the residual IP was known from the $4.5 billion paid for it by Rockstar and by taking his projected cash flows that he used from the IPCo model, he could back into (or reverse-engineer) a discount rate, being 12.2% when China is not included and 15% when China is included.

[25] This analysis proceeds on the assumption that the amount paid by Rockstar was based on the revenues taken by Mr. Kinrich from the particular IPCo model that he used. However, neither Mr. Kinrich nor anyone else knew what revenue streams were used by Rockstar to base their purchase price on or indeed, if Rockstar based their purchase price solely on anticipated revenues they could earn from the patent portfolio they acquired. Without knowing that, it is not possible to say that the Rockstar purchase was based on a discount rate of 12.2% or 15%. A discount rate, as Mr. Kinrich conceded, should reflect the risk of the cash flows being achieved, but without knowing what cash flows Rockstar based its purchase price on, saying the Rockstar purchase reflected a certain discount rate is artificial. Rockstar did not even know what the various IPCo cash flow models were.

[26] Mr. Green, Mr. Berenblut and Dr. Cox and Mr. Malackowski, all expert valuers, were critical of the method used by Mr. Kinrich to arrive at his discount rates of 12.2% and 15%. I accept their criticism. These discount rates were much lower than the rates used by Lazard in the IPCo models, including the very net cash flow model used by Mr. Kinrich, of 25% to 45%. Mr. Berenblut testified that he would expect the range of discount rates to be between 30% and 70%, recognizing the fact that this was a contemplated rather than an established business and recognizing the risks associated with it.

[27] Mr. Malackowski used a discount rate of 30% in his analysis of the potential revenue from the residual IP portfolio. He derived that rate by examining risk-adjusted hurdle rates associated with implementation of technology-based IP. These rates account for a buyer's required rate of return or the associated risk of commercializing a technology.

[28] Mr. Kinrich in his report stated that the inferred rates of 12.2% and 15% that he obtained were consistent with discount rates observed in the market place at the time, being the median weighted average cost of capital for communication equipment companies. However, even Mr. Kinrich noted in his report that IPCo would not have been a communications equipment manufacturer. There was no analysis by Mr. Kinrich to lead to a conclusion that the cost of capital for a start-up litigation and licensing business would be comparable to an established communications equipment manufacturer. Messrs. Berenblut and Cox in their reply report stated:

> The Kinrich Report's use of discount rates for established publicly traded companies in the communications industry as benchmarks for its selection of discount rates for its valuation of a yet-to-be established business to exploit the Residual IP is not supportable. A discount rate of 30 percent or more for this type of business is consistent with our understanding and experience and is also consistent with the discount rates used in the IP Co Model. The academic literature reports venture capital discount rates in the range of 30 to 70 percent.

[29] I accept the criticism of Messrs. Green, Berenblut and Malackowski that the discount rates obtained by Mr. Kinrich were too low. Had Mr. Kinrich used higher rates such as those used by Lazard in the IPCo models, or the rate used by Mr. Malackowski, the value of the revenues given up by the Licensed Participants, assuming they belonged to the Licensed Participants, would have been far less than opined by Mr. Kinrich.

[30] Mr. Green calculated the values from the IPCo models using the discount rates used by Lazard in the models. Taking the most optimistic cash flows from the IP Co. model, the lowest discount rate used by Nortel and its advisors, and a litigation success rate of 100%, the maximum DCF value of IP Co. is only $2.7 billion, compared to the $4.5 billion paid by Rockstar. Messrs. Berenblut and Cox calculated that if a 30 percent discount rate is used to discount the cash flows used by Mr. Kinrich, the resulting net present value of the expected cash flows from the IP Co Model is $1.8 billion. They think this figure is overstated because of the range of values for all of the various scenarios in the IPCo models with various discounts of 25 to 45% and litigation strategies and assumed success rates of the litigation strategies from 60 to 75 to 100%. That range went from $424 million to $2.7 billion. Mr. Green put the range of values in the IPCo models from $400 million to $2.7 billion.

[31] The report of Messrs. Berenblut and Cox explains why Rockstar would be likely to have paid more for the residual IP than Nortel could have made from it, that is, on the theory that the Licensed Participants owned all of the benefits sold to Rockstar, more than what the Licensed Participants

gave up in the Rockstar transaction. The defensive value of the residual IP to the members of the Rockstar consortium made the residual IP far more valuable to Rockstar than it was in the hands of Nortel.

[32] As explained by them, Rockstar obtained ownership of the residual IP and each of the members of the consortium (including Apple, Microsoft, Ericsson and Blackberry) received a license to the residual IP. The structure enabled Rockstar to exercise all rights of ownership of the residual IP against third parties, while providing the individual consortium members with the defensive benefits to prevent others from suing them for patent infringement. As a single company, Nortel was less likely to be able to derive defensive benefits equal to the combined and cumulative defensive benefits that could be gained by several large companies with extensive product and service lines that ranged well beyond what Nortel offered. Several members participating in the Rockstar portfolio are more likely to find patents contained in the Residual IP that will be useful to responses to litigation. Furthermore, as a company in financial difficulty, Nortel was less likely to be an attractive target for patent litigation and therefore less in need of patents to assert in response.

[33] Mr. Green also made the same this point. He stated that the members of the Rockstar consortium purchased the residual IP portfolio, at least in part, as a defensive measure. It was his experience that having access to a large patent portfolio can help protect a large technology firm from lawsuits from other large companies. Access to a large patent portfolio, like the residual IPCo portfolio, can act as a deterrent because potential opposing parties must factor in the probability of a counter-suit. The defensive value of access to a significant patent portfolio is valuable to purchasers like the Rockstar consortium members, but would not be relevant to an entity like IPCo which intended to pursue an offensive licensing and litigation strategy, but had no operating business in the technology sector as all such businesses had been sold. The defensive value of such a portfolio to large companies is not measured exclusively by the present value of the cash flows from licensing.

[34] Dr. Catherine Tucker, an economist called by the U.S. Debtors with considerable technology experience, stated the same thing. In her report she said that patents are not just used in litigation to assert rights to a particular technology or domain. There is also the important role of a patent being used in a counter-suit should the company itself be sued for patent infringement. She referred to Kent Walker, Google's General Counsel, who wrote at the time of the Rockstar bid that it was supposed to create a disincentive for others to sue Google. This defensive attribute, of course, would not have been available to IPCo if it decided to operate a patent licensing business as it would not have been in a product producing business that would be vulnerable to patent suits.

[35] Mr. Green also expressed the view that the identity of the bidders themselves in the residual IP auction also illustrates that the basis on which value of the residual IP portfolio was determined is not consistent with that in the Kinrich report. The bidders included Google, Apple, Microsoft, Ericsson and other large technology companies with worldwide operations rather than companies whose primary business model was patent licensing and litigation. If the value of the residual IP sale was closely related to the cash flows from a licensing/litigation strategy, one would expect licensing/litigation businesses to have been bidders in the auction. Instead, the bidders in the auction were operating technology companies, which suggests that the value of the residual IP was determined in the market on some strategic basis in addition to the value of the IP in a licensing/litigation business.

[36] I accept the evidence of Messrs. Berenblut and Cox and Mr. Green that the approach of Mr. Kinrich of allocating proceeds based on cash flows from a licensing /litigation business model such

as the IPCo models is inappropriate and that what Rockstar paid for was more than the value of the potential revenues from the business that was being considered by IPCo. That is, it was more than what the Licensed Participants gave up in the Rockstar sale, assuming it was theirs to give up.

[37] The U.S. Debtors contend that it is wrong to say that Rockstar paid more than the value of what the Licensed Participants gave up when they terminated their licenses in anticipation of the Rockstar sale and to say that the extra value belongs to NNL as the owner of the NN Technology. They say that NNL could not transfer its rights without the consent of NNI and the EMEA Licensed Participants, just as NNI and the EMEA Licensed Participants required the consent of NNL to do so. They say that all parties consented to the transfer of their MRDA interests as part of the Rockstar sale, effectively agreeing to the assignment of their rights under article 14(e) of the MRDA which permitted an assignment of a party's rights under the MRDA only with the consent of all of the other parties.

[38] I do not accept that contention. The MRDA did provide in article 14(a) that the MRDA could not be assigned by any licensed participant without the consent of the other Licensed Participants. But neither the MRDA nor the licenses of the Licensed Participants were assigned to Rockstar. Rockstar would not have taken an assignment of the MRDA with its obligations and duties amongst the participants. I accept the evidence of Mr. Britven, an expert valuer and the national intellectual property consulting practice leader with Duff & Phelps in Houston, that no third party would want to step into the shoes of a Licensed Participant by taking a transfer of the MRDA with its obligations to share profits and transfer ownership of patents to NNL, among other things. Even Mr. Ray eventually admitted that there was no transfer of license rights to Rockstar.

[39] What occurred was a sale of the residual IP to Rockstar with NNI and the EMEA debtors terminating their licenses under the MRDA as a condition precedent to the sale. What is at issue is the value of those licenses that were terminated. If the value of what could be earned from the licenses was less than Rockstar paid for the residual IP, the difference would belong to NNL, the legal owner of that IP.

[40] Mr. Green did an alternative valuation on the assumption, with which he disagreed, that IPCo would have operated on a stand-alone business and that the licenses surrendered by U.S. Debtors and EMEA debtors would have included the rights to the residual IP portfolio. He used version 3.1 of the IPCo model, as Mr. Kinrich had, but made some changes. He used the three discount rates that had been used by Lazard in the various IPCo models and used the three assumptions in the IPCo models as to the anticipated success in litigation against infringing third parties. He also deducted from the revenue streams going out to 2020 the RPS percentages for 2010 under the MRDA on the theory that if the Licensed Participants had rights under their licenses to earn the revenues proposed in the IPCo models, those licenses came with an obligation to make RPS adjustments in favour of the other Licensed Participants. Any gain on the sale above the DCF valuations on the revenue streams was allocated to Canada.

[41] If one assumed the median discount rate (of 35%) and the median litigation success rate (of 70%), and excluding the revenues from China, then Mr. Kinrich's allocation of the Rockstar Sale proceeds, as adjusted by Mr. Green, would be as follows. Also shown is the allocation advocated by Mr. Kinrich.

	Adjusted Kinrich Allocation of Rockstar Sale Proceeds	Kinrich's Actual Proposed Allocation of Rockstar Sale Proceeds
Canada	$4,003.06 million	$430 million
U.S.	$346.12 million	$3,310 million
EMEA	$105.19 million	$710 million
Total	$4,454.37 million	

[42] If revenues from China were included, the results would be an allocation of $3905.44 million to Canada, $420.99 million to the U.S. and $127.94 million to EMEA.

[43] The U.S. Debtors contend that Mr. Green was wrong to apply the RPSM to the value of the cash flows. They say firstly that the MRDA expressly provided in the third addendum signed in December 2008 that it does not apply to the sale of a business. What that amendment provided was that the operating income or loss used to calculate the RPSM was to exclude "gain/loss on the sale of business". That is not a reference to the proceeds of the sale of a business, but rather a reference to the gain or loss, presumably capital gain or loss, recognized on a sale of a business. That makes sense because the RPSM was dealing with the split of profits or losses from operating earnings to be allocated to the participants under the MRDA. Ordinarily the gain or loss on the sale of capital assets would be recognized in an earnings statement but the parties to the MRDA did not want that taken into account in the RPSM.

[44] However, what Mr. Green was valuing in this analysis was the annual profits that would be earned by the Licensed Participants from operating IPCo in the future, assuming the Licensed Participants had the right to do so under their licenses. He was assuming that the profits would be split in accordance with the RPSM in the MRDA. I agree with the theory that if one is to value the benefits that could have been earned by the Licensed Participants if they had operated IPCo, which is what the U.S. Debtors say they would have done but for the Rockstar sale, the Licensed Participants would have been subject to some profit split.

[45] The U.S. debtors point out that what the profit split would be is a matter of conjecture and that it is not possible to assume, as Mr. Green did, that it would be the same in the future. The RPSM under the MRDA was based on the amount of R&D spend each year by Nortel and the Licensed Participants. After Nortel became insolvent, the R&D expenditures essentially stopped after 2009 and there is no evidence of what R&D would have been undertaken if IPCo had been run as a business by Nortel.

[46] Certainly there would have had to be some transfer pricing in place if Nortel had run IPCo as a business. What the parties would have worked out is unknown. The tax authorities would certainly have been interested in the transfer pricing associated with the running of the IPCo had that occurred and it does not mean that the parties would not have had to agree on a profit split of some sort. They would have been required to do so.

[47] It is perhaps fair to be critical of Mr. Green for assuming the transfer pricing would continue to be the same under an IPCo business run by Nortel as it had been before. It is also fair, however, to ask that if the U.S. debtors contend, as they do, that they are entitled to be paid for what they gave up in the Rockstar sale and that the present value of the anticipated net cash flows is what they gave up, one may have expected them to lead some transfer pricing evidence as to what transfer pricing would have been appropriate.

[48] The assumption that the transfer pricing that the parties would have worked out in the event that Nortel operated IPCo would have been the same as provided in the MRDA has some logic to it. The residual IP was created by R&D conducted by the parties, at least in part, during the MRDA that split profits on the basis of the R&D expenditures of NNL and the Licensed Participants. R&D was the driver of the profitability of Nortel and the RPSM was chosen at the request of the tax authorities as the most appropriate method for determining the compensation to each of the participants for the R&D performed by them. The profits to be earned from operating IPCo could perhaps be seen to be an extension of the results of the R&D that had been spent.

[49] The lack of transfer pricing evidence and analysis on the point, however, as to how the profits would be split in an IPCo business casts some doubt on the accuracy of Mr. Green's alternative analysis. It is not a basis, however, to reject it out of hand as contended by the U.S. debtors.

[50] Mr. Malackowski's preferred allocation approach is a contributions approach based on R&D expenditures made by each of the participants to the MRDA. He prepared an alternative revenue or licensed based allocation which contained dramatically different results from his contributions approach. His revenue approach allocated 33.6% of the Rockstar sale proceeds to the EMEA debtors versus 17.6% using his contribution approach. It allocated 11% to the Canadian debtors versus 39.5% using his contribution approach and it allocated 55.4% to the U.S. debtors versus 42.9% using his contribution approach.

[51] For his revenue or license approach, Mr. Malackowski used the data generated as a result of his valuation methodology to allocate the proceeds of the Residual IP Sale. He valued the Residual IP Portfolio by determining what revenues were expected to be generated by a worldwide licensing strategy in specific geographic territories and allocating the values to those territories. He estimated global revenues for the business areas in which the technology was used, royalty rates, licensing expenses, tax and discount rates. Mr. Malackowski concluded that the value of the residual IP was $3.570 billion, approximately one billion less than actually paid by Rockstar. He then "reconciled" this value with the actual purchase price of $4.5 billion by increasing pro rata the values he had calculated for each business franchise.

[52] For the exclusive territories of Canada, United States, Britain, Ireland and France, he allocated all of the value for those territories to each of the countries. For the rest of the world ("ROW") he allocated 20% to each of the countries. It was this latter allocation of ROW that was the main cause of the increase in the allocation to EMEA as it had what he called "three seats at the table of five".

[53] I have difficulty with Mr. Malackowski's revenue or license model of allocating the Rockstar sale proceeds. The first is that there is no explanation by Mr. Malackowski why his market based valuation was $1 billion less than the actual sale proceeds. Rather than simply grossing his value up to "reconcile" it with the actual proceeds, it seems to me that his valuation was an indication that Rockstar paid for more than what could be achieved in revenues from the acquired IP portfolio. Mr. Green expressed the opinion that the adjustment was inappropriate and unsupported by valuation principles, and assumed that Rockstar just used different royalty or revenue assumptions. I accept that criticism.

[54] Mr. Green also expressed other criticisms of Mr. Malackowski's calculations, all of which appear logical and which I accept. For example:

(i) Mr. Malackowski assumed all revenues for a country should be included in the royalty base, whereas he should have considered that only revenues from products and not services on which no patent royalty would likely be available.

(ii) Mr. Malackowski assumed that revenues from all licensees will begin to be earned in 2011 i.e. he assumed that all licensing efforts against dozens of targets across multiple jurisdictions would be 100% successful within a few months of the portfolio being sold. Mr. Green's view is that his assumption is hard to credit and is inconsistent with the fact that the royalty rates selected by Mr. Malackowski are the IPCo "litigation light" rates, which would, by definition, require at least some form of enforcement action, which would necessarily delay the receipt of royalty payments.

(iii) Mr. Malackowski assumed increasing royalties through 2022 without considering that the patents and technologies are wasting assets and many are likely to expire before the end of the period used by Mr. Malackowski.

(iv) Mr. Malackowski deducted costs of 20% of royalty revenues, stating that he based the rate on the observed financial performance of sophisticated non-practicing entities such as Acacia Research Group. Mr. Green reviewed Acacia's public filings and those of other licensing entities and have found a significant discrepancy between their reported costs and those that the Malackowski Report asserts are representative. The Acacia public filings disclosed that the company's costs of operation from 2005 through 2012 have ranged from 112% of revenue in 2005 to a low of 52% of revenue in 2012. Other licensing entities, such as Interdigital and Rambus, report operating costs from 2005 to 2012 ranging from a low of 28% of revenues to as much as 164% of revenues.

[55] These errors lead to the conclusion that Mr. Malackowski's valuation of $3.570 billion of the residual IP sold to Rockstar was likely overstated, indicating an even greater discrepancy between his value and the actual sale price. It also indicates issues with the territorial split of the revenues. The assumption of Mr. Malackowski that the entire sale proceeds were based on revenue forecasts by Rockstar, permitting him to simply increase his $3.570 billion value by another $1 billion without analyses ignores the likelihood that Rockstar paid what it did in part as a defensive move for its participants to protect their operating businesses, which Nortel no longer had. I do not have confi-

dence in using Mr. Malackowski's analysis to allocate the proceeds of the Rockstar sale on a license or revenue basis.

[56] In the end, I also cannot accept Mr. Kinrich's calculation of the amounts from the Rockstar sale to be allocated to NNL, NNI and EMEA. Assuming the Licensed Participants had a right to the value of the residual IP that Nortel could have achieved, and looking at the various scenarios in the IPCo models, I would recalculate those values and allocate the proceeds by adjusting the calculations of Mr. Kinrich and averaging them with the calculations of Mr. Green in his alternative approach.

[57] I would take the mid-point between the low value of $400 million to $2.7 billion, or $1.5 billion using the discount rates of Mr. Green and Messrs. Berenblut and Cox. Using the same split as Mr. Kinrich, on the assumption that value would not be realized in China, would result in an allocation of 9.3% or $139.5 million to the Canadian debtors, 14% or $210 million to EMEA and 76.7% or $1.15 billion to the U.S. debtors. The balance of the $4.45 billion, or $2.9 billion, would be allocated to Canada. On the assumption that value could be realized in China, the resulting allocation would be 11.1% or $166.5 million to the Canadian debtors, 22% or $330 million to EMEA and 66.9% or $1.0 billion to the U.S. debtors. The balance of the $4.45 billion, or $2.9 billion, would be allocated to the Canadian debtors.

[58] I would then average these allocations with the allocations arrived at by Mr. Green in his alternative analysis, set out in paragraphs 358 and 359 above, which were based on the median discount rates and litigation success rates used in the IPCo models.

[59] The results of that allocation, assuming the revenues from China are included, would be an allocation to Canada of $3,485.97 million, to EMEA of $228.97 million and to the U.S. of $710.5 million, or a total of $4,425.44 million. I would round these figures up on a pro rate basis to arrive at the proceeds available of $4,454.37.

[60] The results of that allocation, assuming the revenues from China are not included, would be an allocation to Canada of $3,521.28 million, to EMEA of $157.6 million and to the U.S. of $748.06, or a total of $4,426.94 million. I would round these figures up on a pro rate basis to arrive at the proceeds available of $4,454.37.

[61] The U.S interests assert that on a license or revenue analysis, very little revenue should be attributed to China. They assert that the IPCo models included both a "China in" and "China out" option. I must say I have carefully looked at the IPCo model 3.1 used by Mr. Kinrich and I cannot find a China out option. On cross-examination of Mr. Malackowski, who thinks China revenues should be included, it was put to him that the IPCo model had a "toggle" for China, which I take to be a sheet with revenues for China.

[62] In any event, Mr. Kinrich testified that he at first took the mid-point of the particular China forecasts he used after doing an economic literature search on patent value and speaking with Mr. Zenkich, who told him that the market would pay little to nothing for a China patent, he reduced his revenues for China downward more towards the US in some qualitative fashion. He reduced then by 75%. Mr. Zenkich, an expert in valuing patents, testified that in 2009-2010 participants in the market for patent portfolios assigned little to no value to Chinese patents.

[63] The thinking of Nortel's patent people changed over time. In December 2000, Angela Anderson, Director, Intellectual Property Law in the U.K stated that China was a sizeable and growing

market accessible at moderate cost. She said that the target filing % (3% of cases) would be higher but for enforcement issues. "Show the flag, but don't over-invest." She testified that at that time, it was clear that China was going to become more of a potential marketplace for Nortel products. In addition, the patent system was starting to look like a real patent system, so it made sense to start using the patent system in China at that time.

[64] By 2006, Nortel intended to file far more patents in China. The plan was to file up to 30% of the top patents in China and in 18 months' time raise this to up to 50%, selecting those having the highest commercial potential. In the IPCo model of May, 2010 that included revenues from China, it stated that early 2010 modelling did not include China in its royalty base but the new plan included China but only in the years 2015 to 2020. It stated that 80% of its patents and 70 % of the applications in China were for wireless 4G technology. The logic of waiting until 2015 was the time for 4G market maturity. EMEA contends, and I have no reason to question it, that the assumptions in the IPCo model regarding China were conservative.

[65] Mr. Malackowski's view was that in doing a revenue or license approach, it would be wrong to exclude China revenues. His reasoning was that Nortel had decided to file high interest patents in China, that patent protection was improving in China and had improved over the past five to ten years and that China was a very important and large market. He has had experience in China. His firm has a partner in Shenzhen for addressing the work they do in China.

[66] Mr. Zenkich testified that the basis for his conclusion that no one would pay anything for a Chinese patent was based on his business of being a patent broker. He testified that when his clients had large patent portfolios, there was no interest expressed in the Chinese patents that were part of those portfolios. Similarly, they were never asked by clients who looked to purchase patents to identify Chinese assets for purchase. I take this to be no evidence of knowledge of values that could be achieved for a Chinese patent, but only that Mr. Zenkich had no knowledge of a client being interested in in a Chinese patent. Included in material referred to in his report was a 2011 report entitled "China's Emerging Patent Trading Market" that referred to a patent auction in China in 2010 which sold 38 lots and the intention of the seller to hold another auction in 2011. The article also referred to efforts being made to set up an exchange in China with the support of governments that would facilitate transactions. That article was contradictory of the view expressed by Mr. Zenkich.

[67] Mr. Zenkich referred to a 2012 publication by the U.S. Patent Office that referred to comments it had received to the effect that there were difficulties with enforcing Chinese patents. That is certainly anecdotal evidence of statements made by others, and it cannot be belittled. How accurate are all of the statements is perhaps a matter of some debate. For example, a comment by one person as to the cap on damages in China was shown during the evidence to be incorrect. While Mr. Zenkich had stated in his report his belief that that significant interest in patent granting activity in China over the last ten years has increased the risk that patents may be challenged as invalid, even if granted, he acknowledged on cross-examination that he had no experience in trying to enforce patents in China and that his company had no experience in trying to enforce a patent anywhere in the world. He also acknowledged that he did not independently conduct surveys or seek out patent data of this kind of activity and that he was unable to identify a single instance where a Chinese patent was found invalid and its US or European counterpart was not. One of the documents cited by Mr. Zenkich in his report was a publication by a Beijing law firm of October 2009 that stated that the major cities, in particular Beijing, Shanghai and Guangzhou, can be considered as a reliable forum

for patent infringement actions. Mr. Zenkich chose instead to rely on the U.S. Patent Office document that contained comments regarding the difficulty of enforcing patents in China.

[68] I am afraid that I cannot put a great deal of reliance on Mr. Zenkich's evidence of the unreliability of the Chinese patent system. I accept he may be of the view that it is unreliable, but his view was not supported by any cogent, reliable and admissible evidence. The views of Mr. Kinrich are also not supported by any cogent evidence. He appears to have largely relied on Mr. Zenkich.

[69] In my view, if a license or revenue approach to value is to be used to value the residual IP, it should include revenues from China that were used in the IPCo model, mainly for the reasons expressed by Mr. Malackowski and the fact that the projections were somewhat conservative.

[70] The conclusion I come to, if an allocation of the proceeds of the Rockstar sale were to be based on a license or revenue approach, would be an allocation to Canada of $3,485.97 million, to EMEA of $228.97 million and to the U.S. of $710.495 million, or a total of $4,425.435 million. I would round these figures up slightly on a pro rate basis to equate to the proceeds available of $4,454.37.

(ii) Mr. Malackowski's contribution approach to value

[71] The EMEA debtors contend that the allocation of the proceeds of the Rockstar sale should be made on the basis of the contribution to R&D made by each of the RPE entities that created the residual IP sold to Rockstar. They contend that the contributions by each RPE to measure this should not be the contributions made during the five year look-back period used to allocate the residual profits under the MRDA but rather the contributions made during the period of time that the residual IP that was sold to Rockstar was invented. Based on the evidence of Mr. Malackowski, they say the look-back period should be from 1991 to 2006[26].

[72] There are two fundamental issues that have been raised to the calculations if the contribution approach to allocation is to be used. The Canadian Debtors contend that there is no basis to use a contribution approach to allocate the proceeds of the Rockstar sale or the business line sales. They say that if a contribution approach is nevertheless used, the look-back period for looking at R&D contributions should be the five year look-back period under the MRDA from 2005 to 2009. The U.S. Debtors also disagree that a contribution approach should be used to allocate the Rockstar and business line sale, but contend that if a contribution approach is used, they agree with the EMEA debtors as to the length of look-back period but contend that all R&D spending must be taken into account. They contend that what must be taken into account is not only the R&D costs incurred by each RPE in their own exclusive territory, but also all transfer pricing adjustments made by an RPE, particularly the adjustments made under the CSA agreements prior to the MRDA coming into force.

[73] Mr. Malackowski said in his report that to measure contribution, ideally, the contributions of the RPE's labs to the development of the patented technologies could be fully and accurately determined by interviewing all of the firm's R&D staff, and by reviewing all the documentation related to the firm's research (e.g. lab notebooks, invention disclosures, meeting minutes, research presentations etc.). This approach was not possible for Nortel's IP due to the size of the portfolio, the limitations on time and the availability of information. Mr. Malackowski did not have access to lab notebooks and R&D staff. Moreover, as R&D was organized across the Nortel Group and carried out in a highly coordinated and integrated manner across the various RPEs, it was even more difficult to separate out the distinct contributions of the various RPEs. In these circumstances he said he had to select a proxy data that reasonably reflected the research efforts of the various RPE's labs.

[74] Mr. Malackowski chose to measure contributions to the development of the IP by measuring each RPE's spending on R&D. He stated that in a large organization, where R&D funding supports a large number of R&D personnel and results in a large number of patents over time, this funding can be valid and indeed the most accurate proxy measurement for determining the contribution of each research group to the development of IP. He stated that it is common practice to regard each dollar spent on R&D as fungible for the purposes of measuring relative contribution to R&D in a group, as Nortel did under the RPSM.

[75] Mr. Malackowski stated that in his experience, in large IP portfolios the vast majority of the value of the portfolio is usually derived from a minority of the patents. This is due in part to the fact that technology IP can be overlapping and duplicative. Value is often derived from a relatively small number of patents that are essential to industry standard technology or that cover an essential process or solution to a common problem. Mr. Malackowski expressed the view that the patents that were categorized as high interest by Global IP likely represented the vast majority of the value of the residual patent portfolio. Approximately 37% of the total residual patent portfolio was identified as high interest.

[76] The evidence was that it generally took one year for Nortel R&D spending to result in a patent application for an invention. He therefore thought it appropriate to determine contribution to the creation of Nortel's IP by measuring R&D spending starting the year before the filing of the earliest unexpired patent categorized by Global IP as high interest, i.e. in 1991. He stated that the most logical end point was in 2006, the year before the last high interest patent was filed. He provided calculations for four look back periods produced by two different start points and end points. His two start points were 1991, reflecting the year before the earliest unexpired high interest patent in the residual patent portfolio, and 2001. His two end points were 2006, representing the year before the last high interest patent in the residual patent portfolio, and 2008, representing the last year of ordinary course operations[27]. 2001 was the start of the MRDA.

[77] By looking at the expenditures on R&D for this period from 1991 to 2006, Mr. Malackowski allocated 39.5% or $1.777 billion to Canada, 42.9% or $1.930 billion to U.S. and 17.6% or $793 million to EMEA. For the period 1991 to 2008, he allocated 40.6% or $1.827 billion to Canada, 43% or $1.935 billion to U.S. and 16.4% or $738 million to EMEA.

[78] The effect of using the longer look-back period substantially reduces the amount allocated to Canada, the reason being that the R&D expenditures from 2005 to 2009 during the five year RPSM were proportionally done more by Canada than EMEA and the U.S. The percentages from 2005 to 2009 were 49.5 for Canada, 38.8 for the U.S. and 11.7 for EMEA.

[79] Mr. Malackowski's report contains discussion why he looked at a long period back to 1991 to measure R&D spending. He said that old patents maybe more valuable than recently filed ones. He said that technologies are adopted by the market slowly over time and do not realize their full value until later in the life of the patent. He did recognize that newer patents will have longer life before they expire and they may have favour due to technological obsolescence, but pointed out that there is risk in newer technologies that they may not be accepted by the market. Based on these considerations he concluded that he should take into account R&D spending from the year before the first high interest patent.

[80] Mr. Malackowski did not consider what Nortel's thinking was about the life to its technology. In the first version of the MRDA the R&D spending used to split residual profits was calculated us-

ing an amortized 30% rate, with expenditures from any one year declining by 30% in the following years. In Nortel's response to questions from the tax authorities in 2003 in connection with its request for an APA for that MRDA, Nortel stated:

> It is difficult to ascertain the exact useful life of R&D developed at Nortel; however, Nortel's analyses indicated that a 30% amortization was conservative yet reasonable. Numerous sources suggest that the useful life of telecommunications R&D is short; however, there is no one definitive external source that explicitly determines that a 30% amortization rate is correct.

[81] The tax authorities did query this response in a question that referred to information from Nortel that it said seemed to suggest that the useful life of R&D is equivalent to product useful life. "However, isn't it the case that benefits from R&D may persist beyond product useful life? For instance, value may result from further developing the intangible."

[82] In preparation for APA negotiations with the tax authorities, Gilles Fortier, NNL's taxation manager for transfer pricing, circulated a document among Nortel tax executives dated May 10, 2002 summarizing the "key drivers" for Nortel, on the one hand, and the tax authorities, on the other, with regard to the APA. The position of the tax authorities was stated to be that the life of Nortel's intellectual property was 7-10 years or more whereas Nortel was suggesting 4-7 years. This position of Nortel was consistent with using a 30% amortization rate for R&D spending in allocating profits under the CSA. Nortel wanted a shorter period because using a longer period would increase the profits in NNI for tax purposes that Nortel did not want. Canada had a lower tax rate due to its generous research and development policies.

[83] A later application by NNL and NNI for an APA with the tax authorities for the years 2007 to 2011, in which a straight five year R&D expenditure would be used to allocate profits, indicated that NNL and NNI thought that the useful life of the Nortel intangibles was estimated to be approximately five years with a gestation lag of one year. Included in the APA request was the following:

> The economic life of technology is difficult to measure because as long as the technology is being sold, it is also being continuously updated and enhanced. Indeed, software and hardware development in the telecommunications industry is widely understood to be an iterative process, because of the tendency to superimpose improvements upon older versions of the technology. Therefore, any discussion of product useful life must consider when an individual product was originated, how to apportion the impact of successive improvements, and when the product was completely superseded.
>
> Nortel's telecommunications technology consists of hardware and software, and it continues to grow and change as demand for bandwidth and functionality grows. As a result, there has been an evolution in the commercial and economic life span of technologies from longer to shorter cycles.
>
> Nortel's Chief Technology Office estimated that a dollar spent on R&D typically has a shelf life of about five years, and additionally, the time from when the in-

> vestment in the R&D is made to the time when revenue can be generated from the investment ranges from about 6 to 12 months.
>
> Recognizing the difficulties inherent in estimating the useful life, based on information obtained in our discussion with Nortel management, and our review of the R&D policy documents, the useful life of the Nortel intangibles is estimated to be approximately five years with a gestation lag of one year.

[84] The evidence from Mr. Malackowski's report is that 99% of the high-interest patents sold to Rockstar had an invention date prior to 2006 and the bulk were from 1995 to 2004. This is considerable evidence that what Nortel was telling the tax authorities did not turn out to be the case. This is not to suggest that Nortel did not believe what it was representing to the tax authorities, or perhaps more appropriately put, that Nortel's transfer pricing tax people did not think that a legitimate tax case could be asserted supporting its 30% declining amortization calculation in the first MRDA and then its five year look-back period in the second version of the MRDA. It is clear, however, that Nortel expected negotiations with the tax authorities would take place that could alter the 30% amortization rate and the later five year flat rate, and the MRDA expressly contemplated that in Schedule A. It cannot be said that Nortel as an enterprise conclusively concluded that its profit allocation keys of 30% or five years were necessarily correct. It was a tax position prepared by Nortel and its advisors.

[85] If a contribution theory is to be used to measure the value of what the parties gave up, I think it inevitable that a longer look-back period would be appropriate. The market has indicated that. However, I would lengthen the time to be taken into account. One of the weaknesses of using a contribution approach is that not every dollar spent results in valuable technology. The theory then must be that what one loses in the corners is gained in the straights. That being the case, I see no reason to disregard the R&D expenditures in 2007 to 2009. They were real and cannot be said to have contributed to the residual IP sold to Rockstar[28]. The fact that Rockstar has started out by enforcing earlier patents does not mean that later patents or patent applications will not be of value or that Rockstar did not pay anything for them.

[86] I would take the R&D expenditures from 1991 to 2009. The data is available from exhibit B.1.7.1 of Mr. Malackowski's report. The resulting percentage of expenditures is 40.93% for Canada, 42.87% for the U.S. and 16.2% for EMEA.

[87] The U.S. Debtors contend that because under the CSA agreement NNI was required to allocate transfer payments to other RPEs, those payments should be included in what is considered to have been contributed to R&D. They rely on upon the opinion of Laureen Ryan, a forensic accountant who went through the transfer pricing worksheets and calculated $4.4 billion allocated to other RPEs under the CSA agreement. On her figures, the percentages for R&D expenditures for 1989 to 2000 would be 21% for Canada, 6% for EMEA and 73% for the U.S.

[88] There is a problem with Ms. Ryan's evidence. The first is that she did no cash analysis to determine if NNI actually paid out any cash to any other RPE as part of its transfer pricing requirements under the CSA and later MRDA. There is no evidence in the record that anything allocated to any party was actually transferred by way of cash and Ms. Ryan conceded that she could not say if anything was actually paid. She did speak to her general understanding that money was transferred by NNI to NNL but I take that to be hearsay evidence and not any cogent evidence that any funds were transferred in fact. Just as important, there was no evidence as to how cash transferred from

NNI or any other RPE was actually used. Cash was moved throughout the Nortel Group as required, but what those requirements were at any time is not a matter of record or available evidence. Ms. Ryan also conceded that she was not able to say where any of the money came from to actually do the R&D spending, whether from customers, governments, shareholders or other Nortel entities.

[89] While Ms. Ryan in her report and evidence calculated what she said were allocations for R&D made by NNI to the other RPEs under the MRDA, the U.S. Debtors made no argument in their closing briefs that these payments should be attributed to NNI. One problem with the evidence on this point is that Ms. Ryan assumed that the RPEs used transfer pricing adjustments for only for only two types of expenses: direct R&D spending figures, and sales, general, and administrative costs. Ms. Ryan pro-rated the intercompany funding between those two expenses. That assumption was obviously incorrect because, as Ms. Ryan conceded, it ignores very significant additional costs incurred by the RPEs, including restructuring costs, costs of revenues, manufacturing, and distribution. The very need for an assumption to be made was because Nortel never kept records of what transferred cash from one Nortel company to another was used for. Ms. Ryan also erred in failing to deduct the $2 billion settlement with the IRS and CRA regarding the $2 billion that was deemed to be a dividend paid by NNI to NNL. She also failed to take into account the sale of Nortel's UMTS business to Alcatel.

[90] As stated above, Mr. Malackowski thought that ideally to determine contribution to R&D by any particular RPE, he would need to have access to lab notebooks and other records and to Nortel R&D personnel. As he did not have that he had to select a proxy data that reasonably reflected the research efforts of the various RPE's labs. He chose to measure contributions to the development of the IP by measuring each RPE's spending on R&D. He testified that this would be reflective of the types of activities that we know lead directly to the inventive process. It is the engineering time and the related expenses that result in the innovation. He testified that a transfer pricing adjustment is an allocation that is done for other purposes, specifically tax efficiency, not for recording the matching between the inventive nature of contribution and results, and he viewed it as inappropriate.

[91] Ms. Ryan is a specialist in accounting and forensic investigations. I prefer the evidence of Mr. Malackowski on this point that for his contribution analysis, it is not appropriate to add to any RPE's contribution amounts that were allocated from that RPE under the transfer pricing regimes in the CSA or MRDA.

[92] Mr. Malackowski did an "inventorship" analysis in his reply report of the countries in which the inventors of the residual patent portfolio resided. He stated that while he did not consider inventorship to be the appropriate basis for allocation, it was a useful metric for testing the allocations of the various parties.

[93] The results of Mr. Malackowski's analysis indicated that for the high interest patents, 46.3% were from Canada, 33% from the U.S., 18.7% from EMEA and 2.6% from ROW. For the entire portfolio, 51.9% were from Canada, 27.4% were from the U.S., 17.7% were from EMEA and 2.9% were from ROW. Using the percentages for the entire residual patent portfolio, which is what was sold, and allocating ROW equally to the others, would give Canada 52.9% of $4.45 billion or $2.35 billion, U.S. 28.4% or $1.26 billion and EMEA 18.7% or $832 million.

[94] Mr. Britven, an expert called by the Monitor, while of the opinion that a contribution allocation theory was not correct, also did an inventor based analysis. That analysis allocated 51.3% to Cana-

da, 28.9% to the U.S., 18.2% to EMEA and 1.6% to others. That is very close to the figures from Mr. Malackowski's inventorship analysis

[95] I conclude that if the contribution allocation theory asserted by the EMEA debtors is accepted, the percentage allocation of the residual IP sold to Rockstar of $4.45 billion is 40.93% or $1.82 billion for Canada, 42.87% or $1.92 billion for the U.S. and 16.2% or $720 million for EMEA to be rounded down pro rate to get a total of $4.45 billion.

(iii) Mr. Green's approach

[96] Mr. Green allocated virtually all of the proceeds of the Rockstar sale to Canada.[29] There were two categories of patents involved in the sale:

1. patents that had been used in several business lines and in respect of which non-exclusive licenses had been granted to the business line purchasers; and

2. the remaining patents, which had not been used in any Nortel business.

[97] For the group of patents identified in (1) i.e. patents that had been used in several business lines and in respect of which non-exclusive licenses had been granted to the business line purchasers, the value of the U.S. and EMEA Debtors' licenses with respect to those patents (which is the value that they would have earned had they continued to operate the businesses) was determined by Mr. Green and allocated to them as part of his allocation of the business line sale proceeds.

[98] With respect to those patents described in (2) that were not used in any of Nortel's operating businesses, Mr. Green considered whether there was any evidence that the U.S. and EMEA Debtors had any prospect of generating earnings through the exercise of their license rights in connection with those patents. He concluded that they did not because the U.S. and EMEA Debtors' license rights were limited to the right to make Products -- i.e. products made or designed (or proposed to be made or designed) by or for a Participant, embodying or using the Nortel IP. This was consistent with the position taken by the Monitor in this case. Thus he allocated none of the proceeds of the Rockstar sale to the U.S. and EMEA Debtors and all of the proceeds to Canada.

[99] Mr. Green's valuation is a straight result of the interpretation put on the MRDA by the Monitor. One cannot quarrel with the logic of it if that interpretation were to govern the allocation.

1 EMEA is an acronym for 19 Nortel subsidiaries in Europe, the Middle East and Africa.

2 All reference to dollars is to U.S. currency.[3] Judge Kevin Gross is the U.S. bankruptcy judge.

3 Judge Kevin Gross is the U.S. bankruptcy judge.

4 See *Nortel Networks Corp. (Re),* (2013), 2 C.B.R. (6th) 1;aff'd (2013), 5 C.B.R. (6th) 254 (Ont. C.A.); 2013 WL 1385271; aff'd 737 F.3d 265.

5 A later Allocation Protocol which set out procedural matters to govern the allocation hearing was made and approved by orders of both Courts in May, 2013.

6 Unless otherwise indicated, statements of fact in these reasons are findings of fact.

7 Nortel Networks Australia was also a RPE until December 31, 2007.

8 This was an alternative argument for the CCC to its first argument that the MRDA should govern the allocation.

9 There were different CSAs for different types of costs. The relevant CSAs were the R&D CSAs that provided for the sharing of costs of the R&D carried out by the Nortel entities doing R&D. NNL made a separate CSA with each of those entities.

10 I prefer this test to that articulated in *Ventas, Inc. v. Sunrise Senior Living Real Estate Investment Trust* (2007), 85 O.R. (3d) 254 (C.A.), in which it was said that interpreting a contract that accords with sound commercial principles is limited to situations in which there is some ambiguity. I do not think that is correct and it is not what other cases of appellate authority have stated. See my comments in *Thomas Cook Canada Inc. v. Skyservice Airlines Inc.* (2011), 83 C.B.R. (5th) 106 at para. 13 and *Oncap L.P. v. Computershare Trust Co. of Canada* (2011), 94 B.L.R. (4th) 314 at paras. 21 to 24. See also Geoff R. Hall, *Canadian Contractual Interpretation Law*, 2nd ed. (Markham Ont.:LexisNexis 2012 at p. 46 fn. 191.

11 There was a separate R&D CSA made with each participant. They were the same. Reference during argument was to the CSA made between Northern Telecom Limited [now NNL] and Northern Telecom Inc. [now NNI], and I refer to it in these reasons.

12 The amended Schedule A was effective January 1, 2006 and reflected a change in the calculation of the amount spent on R&D by each participant.

13 The NN Technology in the MRDA was called the NT Technology in the CSA as the parties at the time of the CSA in 1992 were Northern Telecom, later changed to Nortel Networks.

14 Rulings on admissibility of evidence were left for decision to be made after argument at the conclusion of the trial.

15 At page 30 of the report, Horst Frisch, in referring to intercompany transactions between participants under a RPSM allocation, state-"The old CSPs possess and will continue to possess valuable intangible property." What property is being referred to is not stated. It could be a reference to license rights.

16 *C.I. Covington Fund Inc. v. White*, [2000] O.J. No. 4589 paras. 38-39 (S.C.J. (Commercial List)), *aff'd* [2001] O.J. No. 3918 (Div. Ct.). *G.D. Searle & Co. v. Novopharm Ltd.*, [2007] F.C.J. No. 625 (C.A.), *leave to appeal to SCC refused* [2007] S.C.C.A. No. 340 . *Patchett v.*

Sterling Engineering Coy. Ltd. (1955), 72 R.P.C. 50 (H.L.). This has now been codified in section 39 of the *Patents Act 1977* (U.K.), c. 37.

17 *Board of Trustees of Leland Stanford Junior Univ. v. Roche Molecular Sys., Inc.*, 131 S. Ct. 2188, 98 USPQ (2d) 1761 (2011) at p. 2195-2196, quoting *United States v. Dubilier Condenser Corp.*, 289 U.S. 178 (1933) at p. 189.

18 See the affidavit of Peter Currie sworn April 11, 2014 for a full description of Nortel's matrix structure and operations.

19 Early in these proceedings, on the motion in 2009 to approve the IFSA, counsel to the U.S. Debtors stated in its written brief that NNL owned the IP. The report of the administrators for the EMEA Debtors of June 14, 2009 stated that all IP rights belonged to NNL. Once the size of the sale proceeds became known, these positions of the U.S. Debtors and EMEA Debtors changed.

20 In *In re Owens Corning*, 419 F. 3d 196 at 205 (3rd Cir. 2005) the U.S. Court of Appeals observed that substantive consolidation "treats separate legal entities as if they were merged into a single survivor left with all the cumulative assets and liabilities, (save for inter-entity liabilities which are erased). The result is that claims of creditors against separate debtors morph to claims against the consolidated survivor."

21 The projected cash on hand in all of the Nortel entities as of June 30, 2014 after payment of secured creditors was $1.525 billion, being $343 million in the Canadian Debtors, $744 million in the U.S. Debtors and $438 million in the EMEA Debtors. See schedule 5 of the Britven report, ex. 45.

22 Mr. Kilimnik prepared an expert report on which he was deposed prior to the trial. At the opening of the trial, counsel for the ad hoc group of bondholders said that Mr. Kilimnik would be called as a witness. However, on the day before he was scheduled to testify, his report was withdrawn by the bondholders and he was not called as a witness at the trial.

23 I also prefer the evidence of Mr. Kilimnik and Mr. Binning as to the data in exhibit 58 that compared Nortel bond spreads to government yields and what could be drawn from it. Professor McConnell said he could not draw an inference from the data but also said that he was not contradicting Mr. Binning.

24 There was one series of bonds for $200 million issued by NNL with a NNC guarantee but no guarantee by NNI.

25 The CCC contended for an "ownership" allocation very similar to the Monitor, being $5.805 billion to the Canadian Debtors, $1.009 billion to the U.S. Debtors and $488 million to the EMEA Debtors.

26 For the IP sold in the business line sales, EMEA says that the look-back period should be from 1991 to 2008, two years longer than for the Rockstar sale.

27 Mr. Malackowski said he did not think it appropriate to look at 2009 R&D expenditures post-filing as he understood that little basic research was being performed during this time given that R&D spending was cut dramatically and none of the patents designated as high interest by Global IP were filed during this time period. The R&D expenditures in 2008 were $1.458 billion and in 2009 were $1.076 billion. Mr. Malackowski also said an appropriate look-back period for the business sales would be 2001 to 2008.

28 The Canadian expenditure in 2009 was not just to preserve the business lines as asserted by EMEA. Canada spent $564 million in 2009 on R&D, far more than the $180 million spent on the CDMA and LTE businesses.

29 He allocated $426,097 to the U.S. representing the value of the workforce transferred to Rockstar, being very few people.

TAB 8

Para 4

Indexed as:

Royal Oak Mines Inc. (Re)

IN THE MATTER OF the Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36., as amended
AND IN THE MATTER OF the Courts of Justice Act, R.S.O. 1990, c. C-43, as amended
AND IN THE MATTER OF a plan of compromise or arrangement of Royal Oak Mines Inc., and the applicants listed on Schedule "A"
APPLICATION UNDER the Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36, as amended and the Business Corporations Act, R.S.O. 1990, c. B.16, as amended

[1999] O.J. No. 864

96 O.T.C. 279

7 C.B.R. (4th) 293

86 A.C.W.S. (3d) 1016

1999 CanLII 14843

Court File No. 99-CL-3278

Ontario Court of Justice (General Division)
Commercial List

Farley J.

March 14, 1999.

(15 pp.)

Mechanics' liens -- Priorities -- Preferences, what constitute -- Between lienholders and general creditors of insolvent contractor.

Application by creditors of Royal Oak Mines to remove the grant of superpriority given to DIP financing. Royal Oak brought an application under the Companies' Creditors Arrangement Act, and

the creditors sought to protect their investment. Some of the creditors were not provided with timely notice of Royal Oak's application. The matter of superpriority had previously been dealt with, but because of the lack of notice, some creditors now sought to have their liens declared to be of superpriority. The lien claimants challenged the superpriority granted to DIP financing. The lien claimants argued that the court had no jurisdiction in CCAA proceedings to grant superpriority to DIP. Secondly, the lien claimants argued that even if the court had such jurisdiction, the court's discretion should not have been exercised in the circumstances to grant superpriority.

HELD: Application allowed. The CCAA court did not have jurisdiction to grant superpriority over the subject liens. The liens were a relatively small charge upon the property in relation to other security granted, and it was inappropriate to have taken the radical step of granting superpriority. The lien claimants were parties who had not voluntarily offered credit to Royal Oak on an extended time basis, as opposed to other creditors who did offer credit to Royal Oak on an extended time basis, with their security terms being negotiated between the parties. Even if the court did have jurisdiction, it would have been inappropriate to exercise its discretion to grant a superpriority over the liens.

Statutes, Regulations and Rules Cited:

Builder's Lien Act, R.S.B.C. 1996, c. 41, s. 11.

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

Counsel:

David E. Baird, Patricia D. Jackson and Mario J. Forte, for Royal Oak Mines. K. McElcheran, for the Monitor. P. Griffin and L. Thacker, for Trilon/Northgate. M. MacNaughton, for the Unoffficial Committee of Senior Secured Subordinated Noteholders. Sarah E. Pepall, for the Bank of Nova Scotia. David R. Byers, for Bankers Trust and Macquarrie. J.H. Grout, for Tercon and Kiewit. Benjamin Zarnett, for Export Development Corporation. Stephen I. Graff, for Associates Leasing. Lyndon Barnes, for Glencorp. D.V. MacDonald, for Golden Hill. Michael Weinczok, for Wajax Industries. C. Hill and R. Brent, for Kilborn. P. Shea, for Regata.

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1 **FARLEY J.**:-- CCAA matter was heard on Friday and I was faced with a functional deadline of Monday, March 15, 1999 at 9:30 a.m. in this real time litigation. I am in complete accord with the views of Blair J. as expressed in his expanded reasons released March 10, 1999. I think it worthwhile to repeat for emphasis paras. 20, 24 and 28.

> 20. CCAA orders will of necessity involve a certain complexity. Nevertheless, at least a nod in the direction of plainer language would be helpful to those having to review the draft on short notice, or to react to the order in quick fashion after it has been made on no notice. It would also be helpful to the Court, which - as I have noted - is not infrequently asked to give its approval and grant the order with very little advance opportunity for review or consideration. The language of orders should be clear and as simple and

readily understandable to creditors and others affected by them as possible in the circumstances. They should not read like trust indentures. These comments are relevant to all orders, but to Initial CCAA Orders in particular.

24. It follows from what I have said that, in my opinion, extraordinary relief such as DIP financing with superpriority status should be kept, in Initial Orders, to what is reasonably necessary to meet the debtor company's urgent needs over the sorting-out period. Such measures involve what may be a significant re-ordering of priorities from those in place before the application is made, not in the sense of altering the existing priorities as between the various secured creditors but in the sense of placing encumbrances ahead of those presently in existence. Such changes should not be imported lightly, if at all, into the creditors mix; and affected parties are entitled to a reasonable opportunity to think about their potential impact, and to consider such things as whether or not the CCAA approach to the insolvency is the appropriate one in the circumstances - as opposed, for instance, to a receivership or bankruptcy - and whether or not, or to what extent, they are prepared to have their positions affected by the DIP or superpriority financing. As Mr. Dunphy noted, in the context of this case, the object should be to "keep the lights [of the company] on" and enable it to keep up with appropriate preventative maintenance measures, but the Initial Order itself should approach the objective in a judicious and cautious matter.

28. The comeback provisions are available to sort out issues as they arise during the course of the restructuring. However, they do not provide an answer to overreaching Initial Orders in my view. There is an inherent disadvantage to a person having to rely on those provisions. By the time such a motion is brought the CCAA process has often taken on a momentum of its own, and even if no formal "onus" is placed on the affected person in such a position, there may well be a practical one if the relief sought goes against the established momentum. On major security issues, in particular, which arise at the Initial Order stage, the occasions where a creditor is required to rely upon the comeback should be minimized.

2 I would think it helpful also to have interested parties in a CCAA proceeding to review my observations in Re Inducon Development Corp. (1991), 8 C.B.R. (3d) 306 (Ont. Gen. Div.), Additional Dimensions To Consider In Reviewing The Barrack Paper at p. 501 (Corporate Restructuring and Insolvencies - Issues and Perspectives, the Queen's Annual Business Law Symposium 1995 (Carswell, Toronto)) and Canada (Minister of Indian Affairs and Northern Developments) v. Curragh Inc. (1994), 27 C.B.R. (3d) 148 (Ont. Gen. Div.), especially at pp 157-9.

3 What have we got in the current situation as we approach (or may be approaching) what in bull fighting is called the moment of truth. Of course it should be remembered that bull fighting is a dangerous activity not only for the bull but also for the bull fighter. Then again the interested spectators all wish to have a seat under protective coverage as opposed to being exposed to the relentless sun. The preferred seating is Sombra - not Sol. However some here submit that they have the preferable seating but that others are trying to force them out into the exposed area.

4 A difficulty mentioned by Blair J. is that CCAA litigation (being real time) is subject to the participants being caught up in the momentum of events. A further difficulty in sorting matters out in real time litigation is when one is faced with dealing with the elements of stare decisis while recognizing that there is no functional opportunity to have the higher level of court consider the issue as that would take months (or more) as opposed to days (or immediately). In light of the very general framework of the CCAA, judges must rely upon inherent jurisdiction to deal with CCAA proceedings. However, inherent jurisdiction is not limitless; if the legislative body has not left a functional gap or vacuum, then inherent jurisdiction should be brought into play. I appreciate that there may have been some blurring of distinction among discretion, inherent jurisdiction and general jurisdiction (including the common law facility). This combination is implicitly recognized in Baxter Student Housing Ltd. et al v. College Housing Co-operative Ltd. et al. (1975), 57 D.C.R. (3d) 1 (S.C.C.) in Dickson J.'s analysis of inherent jurisdiction at pp 4-5. See also Galligan J.A. at p. 19 of Ontario (Securities Commission) v. Consortium Construction Inc. (1992), 14 C.B.R. (3d) 6 (Ont. C.A.). It must also be observed that Halsbury's (4th ed, vol. 37, para 14) and Jacob, H. The Inherent Jurisdiction of the Court, (1970) 23 Current Legal Problems were dealing with litigation matters generally - and not with the particulars of insolvency and reorganization litigation. However, the reference in Halsbury's at para 14 to:

> In sum, it may be said that the inherent jurisdiction of the court is a virile and viable doctrine, and has been defined as being the reserve or fund of powers, a residual source of powers, which the court may draw upon as necessary whenever it is just or equitable to do so, in particular to ensure the observation of the due process of law, to prevent improper vexation or oppression, to do justice between the parties and to secure a fair trial between them. (emphasis added)

5 Should be viewed in context. See in particular Montreal Trust Co. v. Churchill Forest Industries (Manitoba) Ltd., [1971] 4 W.W.R. 542 at p. 548, 21 D.L.R. (3d) 75 at p. 81 (Man. C.A.) per Freedman C.J.M. See also in Curragh, supra, my quotations of Macdonald J. in Re Westar Mining Ltd., [1992] 6 W.W.R. 331 (B.C.S.C.) and Tysoe J. in Re Woodwards Ltd. (1993), 17 C.B.R. (3d) 236, (B.C.S.C.). In Curragh I went on to observe at page 159 in a somewhat analogous situation:

> It would appear to me that Parliament did not take away any inherent jurisdiction from the Court but in fact provided, with these general words, that the Court could enlist the services of an interim receiver to do not only what "justice dictates" but also what "practicality demands." It should be recognized that where one is dealing with an insolvency situation one is not dealing with matters which are neatly organized and operating under predictable discipline. Rather, the condition of insolvency usually carries its own internal seeds of chaos, unpredictability and instability. (emphasis added)

6 With that said, I do not wish to be interpreted as being unduly critical of any party in these proceedings but these observations are made with a view toward being helpful and assisting with focus. It must be recognized that these observations are made after the benefit of hindsight and without the benefit of any previous oral submissions before Blair J. The observations and determinations are in no particular order.

1. It is interesting what the interested parties have said; it is perhaps even more interesting what they have not said. No doubt more will be said and more will be revealed as the moment of truth draws closer and to a close.
2. Royal Oak, Trilon and other major participants should likely have a fairly good idea of value at the present time (i.e. value of the assets as well as value of the corporation including tax loss carry forwards, all as affected by environmental concerns) which would be based upon the reasonably foreseeable future. Royal Oak has had the benefit of Nesbitt Burns working with it since last October. Trilon invested $120 million U.S. last July and the Hedge Lenders and Subordinated Notes postponed to the Trilon debt; would all this have been done without the benefit of due diligence (including ranges of values based upon metals markets which were then declining)?
3. It was indicated that the urgency of the application did not make it possible to provide all interested parties with notice of the relief being requested on Monday, February 15, 1999. The application was dated that day; however the essence and significant bulk of the application was a 100 paragraph Witte affidavit with exhibits sworn Friday February 12th with a minor 6 paragraph Witte affidavit sworn Sunday February 14th. See my views about notice of ex-parte permitted CCAA application in Inducon, supra. As well since a CAA application can be made ex-parte, it is quite permissible to notify all interested parties of the application by telephone: Re Cadillac Fairview Inc. (1995), 30 C.B.R. (3d) 29 (Ont. Gen. Div.).
4. CCAA applications should be brought in a timely basis. This timing is a delicate matter since an applicant has to gauge the perceptions and reactions of those with which it is dealing. I appreciate that Royal Oak was said to have been working on prepackaging a proposal. However, given what appears to have been adverse conditions of such long standing, it is unclear what truly precipitated the February 15th application. Applicants should not rely on indulgence being "automatically" given when the applicant has in effect placed a gun to its own head and threatened to pull the trigger.
5. It is puzzling and troublesome why Royal Oak made the three improper payments referred to in paras. 36-39 of the Monitor Third Report (March 10, 1999). At para. 40, the Monitor advised that these payments (including one to Trilon itself for certain machine equipment lease payments) were the basis for Trilon not continuing to fund under the approved limit set by Blair J. In response to any enquiry as to why these payments were in fact made, I was only advised that Royal Oak had made a very serious mistake. I trust Royal Oak will reflect upon that very carefully as this (and anything similar) impacts upon its future as a corporation and could have extremely serious negative consequences, among others, to its employees, their communities, creditors and governments.
6. Notwithstanding the obvious talents of Mr. Dennis Belcher and Prof. Kenneth Klee, it would be inappropriate to admit their affidavits as expert opinion. Prof. Klee is dealing with the U.S. Bankruptcy Code; we are not dealing with U.S. law. It is inappropriate to import concepts and tests from

other jurisdictions; Canadian problems are to be resolved by Canadian concepts and tests. At the most one may very carefully examine general analytical approaches while being fully cognizant of the foreign jurisdictions' different problems and different legislative and judicial solutions to those different problems. Mr. Belcher has set forth in essence his view of the CCAA situation; he should be regarded as a powerful advocate for the interests of his employer The Bank of Nova Scotia. See my views as to expert opinion admissibility in general in my endorsement of April 21, 1998 (Royal Mutual Funds Inc. et al v. Schneider Corporation et al) given during the trial of that matter; these views were affirmed by the Court of Appeal in Pente Investment Management Ltd. v. Schneider Corp. released October 20, 1998.

7. I appreciate that everyone is under immense pressure and have concerns in a CCAA application. However, as much advance notice as possible should be given to all interested parties. It may be helpful to provide the service list with an initial letter or draft notice of motion which would clearly set out the nature of the relief sought and the general grounds (with reasonable elaboration) with the formal material following in due course. At a minimum, absent an emergency, there should be enough time to digest the material, consult with one's client and discuss the matter with those allied in interest - and also helpfully with those opposed in interest so as to see if a compromise can be negotiated. Responding material may require further time before the hearing actually takes place. I am not talking of a leisurely process over weeks here; but I am talking of the necessary few days in which the dedicated practitioners in this field have traditionally responded. Frequently those who do not have familiarity with real time litigation have difficulty appreciating that, in order to preserve value for everyone involved, Herculean tasks have to be successfully completed in head spinning short times. All the same everyone is entitled the opportunity to advance their interests. This too is a balancing question.
8. It is understood that the Monitor must have increased powers and authority to ensure that Royal Oak does not get off the tracks as it did concerning the three unauthorized payments.
9. The Monitor has not had sufficient time to analyse and comment upon the proposed expenditures over the next month. It proposes to do that by Tuesday, March 16, 1999.
10. It would be inappropriate to authorize DIP financing with or without any superpriority for the next month before having the benefit of the Monitor's review. Such authorizations are based upon the particular fact situations then prevailing. Blair J. gave certain authorizations in his earlier orders in the CCAA application. The question of whether they should have superpriority over the security of others is a live question before me in this hearing.
11. I will deal with future authorizations and superpriorities, if any, for the next month on Thursday, March 18, 1999 and if necessary this may go over to Friday March 19th. I note that there are other matters scheduled for

those two days which I have to deal with along with the Associates Leasing conversion claim in this matter. The stay arrangements and other provisions of Blair J.'s initial order are extended then until Friday March 19, 1999 (subject to possibly a further extension at that time or if I do not give a decision that day).

12. I am given to understand that Trilon and the Export Development Corporation (EDC) have worked out an understanding which in its essence is that Trilon claims no priority over the vehicles which EDC has valid PPSA security pursuant to registrations under the Ontario and British Columbia legislation with the proviso that any accretions financed by Trilon and properly registered as to ensuring valid security would not be affected by the EDC registrations. It was proposed that in the event that the vehicle (with accretions) were sold, then Trilon and the EDC should share the proceeds pro rata according to their respective dollar interests secured. I would expect that this is a more practical solution than to require that the vehicles and the accretions be sold and dealt with separately. It would likely be helpful to have confirmation of that negotiation by the end of this coming week.
13. Trilon is not claiming priority over the lien claimants as to facility 3 (Trilon interest and principal repayment).
14. I would assume that Trilon would consider its position forthwith and, if so advised, proceed immediately to fund Royal Oak up to the limit previously authorized by Blair J. I understand that a half a million dollars more has already been spent than authorized and that there is therefore no unspent cushion.
15. I would remind everyone that timely negotiation of disputes in real time litigation is generally more helpful to the overall insolvency/reorganization regime than proceeding in court. However the court must be available in real, timely and substantive way not only if required ultimately but also to ensure that negotiations can take place on a principled basis.
16. The Monitor is envisaged as having a broader role by everyone - namely that within a maximum of 4 weeks from now, it will report on alternative methods of dealing with the Royal Oak situation (i.e. give various options and comments thereon).
17. Absent (unadvanced) reasons, it would appear that liens which have not been registered before any authorized superpriority DIP financing which has been advanced would be subject to and subsequent in priority to that authorized superpriority DIP financing.
18. Funding of DIP financing necessary for a CCAA applicant to carry on operations should not be restricted to any one source. It may be in certain situations that some or all of the existing creditor body would find it attractive and in their best interest to be a source of such funding - on a pro rata basis or on what one might refer to as a pro rata cash call and fill-up deficit with or without some inducement. For example one inducement may be that for every $10 of new DIP financing, $1 of existing financing would be given the same priority (or at least some enhanced priority).

19. Any one who is dissatisfied with the present CCAA proceedings or their progress (or lack thereof) may, with the approval of the Court, institute a creditor CCAA proposal or take other legal steps. Parties should very carefully consider the situation and the circumstances generally before taking such a step.
20. The Bank of Nova Scotia did not appeal Blair J. granting superpriority to the first $8.4 million of DIP financing to be advanced by Trilon. However, BNS asserted that no further DIP financing should be granted superpriority.
21. BNS is concerned that Royal Oak has not specifically elaborated upon its good faith and due diligence effort as envisaged by s. 11(4) CCAA. While we may read between the lines and also extrapolate in real time litigation, it is better form to cover off the bases specifically.
22. Aside from the question of the lienholders who have registered liens which but for the Initial Order granted by Blair J. (but subject to the comeback clause) would have priority over the DIP financing, I see no reason to interfere with this superpriority granted. It would seem to me that Blair J. engaged properly in a balancing act as to the $8.4 million of superpriority DIP financing as authorized. I am in accord with his views as expressed in Re Skydome Corporation released Nov. 27, 1998, where Blair J. stated at p. 7

> This is not a situation where someone is being compelled to advance further credit. What is happening is that the creditor's security is being weakened to the extent of its reduction in value. It is not the first time in restructuring proceedings where secured creditors - in the exercise of balancing the prejudices between the parties which is inherent in these situations - have been asked to make such a sacrifice. Cases such as Re Westar Mining Ltd. (1992), 14 C.B.R. 88 (B.C.S.C.) are examples of the flexibility which courts bring to situations such as this. See also Re Lehndorff Gen Partner (1992), 17 C.B.R. (3d) 24 (Ont. Gen. Div.); Olympia & York Developments Limited v. Royal Trustco (1993), 17 C.B.R. (3d) 1 (Ont. Gen. Div.).

Implicit in his analysis and part of the equation is the reasonably anticipated benefits for all concerned which derive from these sacrifices. It would seem to me that Holden J.A. in his endorsement in Re Dylex Limited released January 23, 1995 implicitly engaged in this balancing of prejudices act where he observed:

> I do not believe that the Bank of Montreal will be adversely affected by the making of this order. As a result of the bridge financing, new receivables will be generated which will assist in re-paying or securing the bridge financing.

Better and more timely information will be of assistance in minimizing the momentum effect in the future. My conclusion as to the appropriateness of the superpriority granted the DIP financing is of course limited to the Initial Order $8.4 million amount and is based upon the conditions now determined to be prevailing as of the authorization date. Each subsequent DIP financing authorization and the priority to be attributed to it will have to be determined on the merits and circumstances then existing.

23. The lienholders here assert that there should be no superpriority granted the DIP financing as to any of their previously registered liens. Their claim is based upon two elements: firstly, they state that the CCAA proceedings court has no jurisdiction in law to grant such superpriority and secondly, they state that even if there were jurisdiction, the Court's discretion should not be exercised in the circumstances so as to grant such superpriority. As to the lack of jurisdiction, they point to Baxter, supra being binding upon the point. When this Manitoba case went to the Supreme Court of Canada, Dickson, J. for the court determined that the motions court judge had exceeded his jurisdiction when he appointed a receiver of the balance of the proceeds of the CMHC mortgage and purported to grant subsequent CMHC advances as having a priority as to security over and above prior liens registered against the property. He stated at pp 3-4:

> Did the learned Chambers Judge exceed his jurisdiction in making the order? However politic and expedient the appointment of a receiver may have appeared as a means of tapping the only available source of funds and preventing a stalemate, I am of the opinion that the Judge had no proper ground in law for making the appointment. The appointment was wrong in law because provision 2 above quoted runs contrary to s. 11 (1) of the Mechanics' Liens Act of Manitoba R.S.M. 1970, c. M.80, reading:
>
> > 11(1) The lien created by this Act has priority over all judgments, executions, assignments, attachments, garnishments, and receiving orders, recovered, issued or made after the lien arises, and over all payments or advances made on account of any conveyance or mortgage after notice in writing of the lien to the person making these payments or after registration of the lien as hereinafter provided.
>
> Section 11(1) goes a long way in ensuring that once a lien claimant has protected his rights by filing a lien in accordance with the provisions of the Act, the lien is a paramount legal charge not subject to being defeated or eroded in any manner: see Boake v. Guild, [1932] 4 D.L.R. 217, [1932] O.R. 617; affirmed [1933] 4 D.L.R. 401, [1934] S.C.R. 10, sub nom. Carrel v. Hart; and Rand J., in Earl F. Wakefield Co. v. Oil City Petroleums (Leduc) Ltd. et al. (1958), 14

> D.L.R. (2d) 609 at p. 612, [1958] S.C.R. 361 at p. 364. Section 59(1) [am. 1970, c. 79, s. 1] of the Queen's Bench Act R.S.M. 1970, c. C.280, it is to be observed, empowers the Court to appoint a receiver "in all cases in which it appears to the Court to be just and convenient so to do" and further provides that "any such order may be made either unconditionally or upon such terms and conditions as the Court thinks fit" [s-s. (2)]; but this cannot afford comfort to the owner because s. 11 of the Mechanics' Liens Act, in terms, gives a lien created by the Act priority over all receiving orders made after the lien arises. The question whether the receiving order here in question is a receiving order of the kind contemplated in s. 11(1) need not detain us because even if this question be resolved in favour of the validity of the appointment, the closing words of the subsection, in clearest language, give a mechanics' lien priority over all payments or advances made on account of any mortgage. One may escape the first part of the subsection only to be impaled on the second part of the subsection and Mr. Houston, counsel for the owner, concedes as much.
>
> In my opinion the inherent jurisdiction of the Court of Queen's Bench is not such as to empower a Judge of that Court to make an order negating the unambiguous expression of the legislative will. The effect of the order made in this case was to alter the statutory priorities which a Court simply cannot do.

This position would appear to be supported by the views of Macdonald J. in Westar, supra at pp. 91-2:

> I accept the argument of the provincial crown that property taxes under the Municipal Act [R.S.B.C. 1979, c. 290] and the Taxation (Rural Area) Act, [R.S.B.C. 1979, c. 400] have "priority over any claim ... or encumbrances of any person except the Crown," and that it is not open to this court to grant its own charge priority over property taxes, at least in the context of CCAA proceedings.

and by the views of Glube C.J. in Mutual Life Assurance Co. of Canada v. Polsky Energy Corp. of Brooklyn Inc. (1998), 2 C.B.R. (4th) 213 (N.S.S.C.) at p. 218.

> It can be argued that although s. 15(1) lists a number of specifics such as judgments, executions and so on, the list does not include every type of order intended to be covered. The Mechanic' Lien Act was first passed in 1879; s. 15(1) dates back to 1899 when it was s. 11(1). There have been many social changes since those dates, as well as legislation such as the Companies' Creditors Arrangement

> Act, R.S.C. 1985, c. C-36, which may be included in the listing in s. 15(1) without being actually added to the list. (emphasis added)

However it is unclear whether Macdonald J. was influenced by the question of the Crown not being bound by the CCAA there and whether Glube C.J. felt compelled by the analogy. However, it is fair to say that the SCC in Baxter, when faced with the choice between an unpractical but "legal" solution and a practical one, opted for the unpractical one. Thus, one is constrained from distinguishing on the basis of the recognition of the CCAA over the past 15 years having a familial relationship with Necessity. On this - of necessity hurried - analysis, it would appear that s. 11 of the Builders Lien Act, R.S.B.C. 1996, c. 41, which provides:

> 11. Subject to this Act, a claim of lien that has been filed in the land title office or gold commissioner's office, if applicable,
>
> (a) takes effect from the date of commencement of the work or when the first materials are furnished or placed for which the lien is claimed, and
>
> (b) takes priority over all judgments, executions, attachments and receiving orders recovered, issued or made after the lien takes effect.

would operate in such a way as to eliminate the inherent jurisdiction which could otherwise be used to grant a superpriority of the DIP financing over other security. That does not of course affect the situation where other security does not have the statutory "protection" or "supremacy" of which this type of legislation affords liens. It may be that if this is demonstrated to be a significant problem that a statutory amendment should be considered.

7 However, even if I were to have concluded that the CCAA court did have jurisdiction to grant a superpriority over the subject liens, I would decline to exercise my discretion to do so under the circumstances. This is a fact driven and practicality driven exercise. The following are my reasons. Firstly, the liens are otherwise a relatively small charge in dollar amount upon the Kemess property in relation to other security granted and it seems to me inappropriate to take such a radical first step which is tantamount to executing a mini-plan of arrangement affecting only the liens at this stage. Secondly, the lien claimants are parties who (to the extent of their valid lien claims) have not voluntarily offered credit to Royal Oak on any extended time basis as opposed to other secured creditors who may be viewed as having offered credit to Royal Oak on an extended time basis with their security terms being negotiated between the parties. Thirdly, I would specifically note in the case of Tercon that the lien was specifically the subject of an order of Brenner J. of the B.C.S.C. dated Sept. 22, 1998 wherein it was ordered that such $2.9 million lien was:

> a charge, lien or encumbrance in preference and priority to all rights and interests of the Defendant in the Lands, in preference and priority to all charges and encumbrances granted by the Defendant in respect of the Lands after February 26, 1998.

8 Then there is the aspect of why should the lienholders be treated any differently than the EDC which would appear to be in a less statutorily protected position than the lienholders.

9 I would wish to note that any of my observations here are not to be taken as having any bearing upon the question of classification of claims. That is for another day and subject to different considerations. However it may be well for Royal Oak and its supporter Trilon to look a few steps ahead to see what the ramifications could be.

10 Order reflecting above to issue accordingly.

IN THE MATTER OF THE *COMPANIES' CREDITORS ARRANGEMENT ACT*, R.S.C. 1985. c. C-36. AS AMENDED **Court File No.: CV-17-11846-00CL**

AND IN THE MATTER OF A PLAN OF COMPROMISE OR ARRANGEMENT OF SEARS CANADA INC., CORBEIL ÉLECTRIQUE INC., S.L.H. TRANSPORT INC., THE CUT INC., SEARS CONTACT SERVICERS INC., INITIUM LOGISTICS SERVICE INC., INITIUM COMMERCE LABS INC., INITIUM TRADING AND SOURCING CORP., SEARS FLOOR COVERING CENTRES INC., 173470 CANADA INC., 2497089 ONTARIO INC., 6988741 CANADA INC., 10011711 CANADA INC., 1592580 ONTARIO LIMITED, 955041 ALBERTA LTD., 4201531 CANADA INC., 168886 CANADA INC., AND 3339611 CANADA INC.

ONTARIO
SUPERIOR COURT OF JUSTICE - COMMERCIAL LIST

Proceeding commenced at TORONTO

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