2025 01G
IN THE SUPREME COURT OF NEWFOUNDLAND AND LABRADOR
IN BANKRUPTCY AND INSOLVENCY

IN THE MATTER OF the *Companies Creditors Arrangement Act* R.S.C., 1985 c. C- 36 as Amended (the "**CCAA**")

AND IN THE MATTER OF an application by Ocean View Farms Ltd. for relief under s. 11 of the CCAA

MEMORANDUM OF FACT AND LAW OF THE APPLICANTS

O'KEEFE & SULLIVAN
Suite 202, 80 Elizbeth Ave.
St. John's, NL A1A 1W7
Telephone: 709.800.6536
Attn: Darren D. O'Keefe
Email: dokeefe@okeefesullivan.com
Solicitor for the Applicants

TO:

The Supreme Court of Newfoundland and Labrador
233 Duckworth Street, St. John's, NL

AND TO:

Counsel and others listed in the "Service List" at **Schedule A** to the Originating Application.

2025 01G
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APPLICANT'S MEMORANDUM OF FACT AND LAW

SUMMARY OF CURRENT DOCUMENT	
Court File Number:	2025 01G
Date of Filing of Document:	04 September 2025
Name of Filing Party or Person:	Applicants, Ocean View Farms Ltd.
Application to which Documents Being Filed Relates:	Notice of Motion filed by the Applicants
Statement of Purpose of Filing:	In support of the Notice of Motion seeking a 10-day Initial Order pursuant to section 11 of the CCAA, appointing Grant Thornton as CCAA Monitor, granting an interim Administration Charge and an interim DIP Lender's Charge, and imposing a stay of proceeding;
Court Sub-File Number, if any:	N/A

TO:

The Supreme Court of Newfoundland and Labrador
233 Duckworth Street, St. John's, NL

AND TO:

Counsel and parties listed in the Service List attached as Schedule "A".

2025 01G
IN THE SUPREME COURT OF NEWFOUNDLAND AND LABRADOR
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IN THE MATTER OF the *Companies Creditors Arrangement Act* R.S.C., 1985 c. C- 36 as Amended (the "**CCAA**")

AND IN THE MATTER OF an application by Ocean View Farms Ltd. for relief under s. 11 of the CCAA

APPLICANT'S MEMORANDUM OF FACT AND LAW

OVERVIEW:

1. The Applicant has filed an Application seeking an initial order ("**Initial Order**") pursuant to s. 11 of the CCAA. The Applicant submits this Memorandum in support of its Application.

2. Unless otherwise defined, all capitalized terms herein have the meanings ascribed to them in the Application and affidavit of Richard Walsh dated 03 September 2025 (the "**Initial Affidavit**").

FACTS:

3. Ocean View Farms Ltd. (the "**Applicant**") is a Newfoundland and Labrador dairy farm (the "**Farm**") encompassing 660 acres of land in Bay Bulls which is split between 58 acres owned by the Applicant fee simple and the remaining 602 held pursuant to 50-year Crown leases.

4. The Applicant possesses 4,303L of fluid milk quota which is filled by its herd of 170 dairy cows. This represents at least 15% of the Province's on-island dairy production, making the Applicant a critical supplier of provincial food security. Without immediate protection and financing, herd welfare will be compromised and significant economic harm will result.

5. The Applicant's current financial distress has been caused by multiple drivers: (a) sharp post-Covid increases in input costs, particularly animal feed and diesel; (b) regulated milk pricing that has not kept pace with inflation; and (c) unilateral interest rate increases of over 5% imposed by its main secured lender, the Bank of Nova Scotia ("**BNS**").

6. The above noted challenges ultimately caused the Applicant to default on its financial commitments to BNS. As a result, BNS placed the Applicant into special loans and hired a third party (MNP) to oversee its account. The related professional fees worsened the Applicant's situation. In September 2024, BNS advised the Applicant to seek another lender.

7. BNS issued its s. 244(1) Notice of Intention to Enforce under the *Bankruptcy and Insolvency Act* ("**BIA**") in November 2024. After an unsuccessful attempt at the Farm Debt Mediation process in early 2025, the Applicant has faced continued and escalating pressure from BNS. The Applicant lacks access to additional credit under its current financing arrangement and has been unable to secure a new lender or to otherwise informally restructure.

8. The Applicant no longer has enough cash to meet its immediate operational demands and urgently needs capital to maintain operations, ensure herd safety, and prevent a loss of herd productivity. In consultation with professional advisors, the Applicant has determined that immediate CCAA protection is necessary to preserve and maximize its value for the benefit of all stakeholders, including creditors, employees, suppliers, and customers.

9. The Applicant has entered a Term Sheet with Libra Finance Company Inc. (the "**DIP Lender**") to provide interim debtor-in-possession financing (the "**DIP Loan**") and is seeking Court approval of the DIP Loan up to an initial maximum amount of $150,000.00 and a Charging Order to secure the same maximum amount.

10. With the benefit of the DIP Loan, the Applicant intends to continue operating as a going concern after either restructuring/refinancing or a sales and investment solicitation process ("**SISP**"), with the SISP Order and related procedures to be presented for Court approval at a future hearing.

11. If granted, the CCAA protection sought will provide the Applicant with the necessary time to maintain the status quo and restructure its operations, aiming to remain a valuable contributor to Newfoundland and Labrador's agriculture industry and provincial economy.

12. Without immediate CCAA protection and interim financing, the Applicant's operations

cannot continue, herd welfare will be compromised, and significant economic harm will result.

13. Further details regarding the Applicant's structure, stakeholders, economic contributions, and the circumstances leading up to this CCAA filing are outlined in the Initial Affidavit.

ISSUES FOR CONSIDERATION:

14. The Court must determine whether the Applicant has met the burden imposed on those seeking an Initial Order under s. 11 of the CCAA, and that their requested relief is necessary and appropriate in the circumstances.

LAW AND ARGUMENT:

CCAA Applies and an Initial Order is Appropriate

15. The Applicant is currently insolvent, i.e. has been unable to meet its obligations as they generally become due. The Applicant qualifies for relief under s. 3(1) of the CCAA, which applies where an insolvent debtor company has claims exceeding $5,000,000.00.

16. Under the CCAA s. 11.02(1), a Court may grant an order staying all proceedings in respect of a debtor company for a period of not more than 10 days if the Court is satisfied that circumstances exist to make the order appropriate. Appropriateness is assessed by inquiring whether staying proceedings advances the policy objectives underlying the CCAA.

17. The CCAA prioritizes avoiding the social and economic losses resulting from liquidating an insolvent company. The CCAA's core policy objectives were summarized in ***Edward Collins Contracting Limited (Re)***[1] as follows:

    (a) providing for timely, efficient and impartial resolution of a debtor's insolvency;
    (b) preserving and maximizing the value of a debtor's assets;
    (c) ensuring fair and equitable treatment of the claims against a debtor;
    (d) protecting the public interest; and
    (e) balancing the costs and benefits of restructuring or liquidating the company.

18. The threshold for an initial order under s. 11.02(1) is low. The Applicant must satisfy the

[1] ***Edward Collins Contracting Limited (Re)***, 2022 NLSC 149, para 20 **[TAB 1]**

Court that the policy considerations noted above are generally met. An applicant is not required to have a fully developed plan, nor are they required to have the support of all creditors.[2]

19. The Applicant submits that the evidence establishes appropriate circumstances to grant the Initial Order and that this relief will satisfy the policy considerations underlying the CCAA as articulated by this Court in *Edward Collins Contracting Limited (Re)*.

20. A stay of proceedings will allow the Applicant to maintain its status quo operations and preserve herd health with the benefit of DIP financing while gaining the breathing room necessary to devise an organized go-forward approach with the Proposed Monitor.

21. The Applicant's current longer-term goal is to refinance or complete a going-concern sale within a SISP. Either case will satisfy the remedial policy aspirations underlying the federal insolvency statutes. Even if unsuccessful, an orderly debtor-led liquidation is far preferable to a creditor-driven process to ensure that the value of the Applicant's assets is maximized, and its livestock is kept productive and properly cared for during the interim period.

Relief Sought is Necessary

22. Pursuant to s. 11.001 of the CCAA, the relief sought on an initial application is limited to what is reasonably necessary to continue ordinary operations during the initial stay period.

23. The Applicant has ensured that the relief requested in the Initial Order is limited to what is strictly necessary to protect assets and maintain regular business operations pending the Comeback Hearing. As set out below, this includes approval of the initial 10-day stay of proceedings, the DIP Loan up to a maximum initial amount of $150,000.00, an Administration Charge of $250,000.00, and approval of the Proposed Monitor.

DIP Financing

24. As confirmed by the Cash Flow Statement and the Proposed Monitor's Pre-Filing Report, DIP financing is immediately required to fund operations, preserve herd health and productivity, and avoid irreversible damage to one of the Province's largest milk suppliers. Courts have repeatedly recognized that preservation of livestock and other perishable

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[2] ***Edward Collins Contracting Limited (Re)***, 2022 NLSC 149, paras 37-39 **[TAB 1]**

assets is a compelling justification for interim financing.

25. In consultation with the Proposed Monitor and the Proposed Chief Restructuring Officer, the Applicant has determined that they require $150,000.00 in the first 10 days of the CCAA proceedings following the Initial Order.

26. Interim financing is permitted by s. 11.2 of the CCAA on notice to affected secured creditors. Section 11.2(4) of the CCAA sets out the factors to be considered in assessing a request for interim financing:

> (a) the period during which the company is expected to be subject to proceedings under this Act;
>
> (b) how the company's business and financial affairs are to be managed during the proceedings;
>
> (c) whether the company's management has the confidence of its major creditors;
>
> (d) whether the loan would enhance the prospects of a viable compromise or arrangement being made in respect of the company;
>
> (e) the nature and value of the company's property;
>
> (f) whether any creditor would be materially prejudiced as a result of the security or charge; and
>
> (g) the monitor's report referred to in paragraph 23(1)(b).

27. This list is not exhaustive. No one factor set out in s.11.2(4) governs or limits the CCAA court's ability consider this relief. The exercise involves balancing the interests of the debtors and their stakeholders towards insuring, if appropriate, that the financing will assist the debtor company to obtain the breathing room needed to hopefully achieve a restructuring acceptable to the creditors and the court.[3]

28. Pursuant to s. 11.2(5) of the CCAA, where an application for interim financing is made at the same time as the initial application, a court must also be satisfied that the "terms of the loan are limited to what is reasonably necessary for the continued operations of the debtor company in the ordinary course of business during that period". Courts have consistently approved interim financing upon an initial application where appropriate.[4]

29. The materials submitted demonstrate that DIP financing at this stage is required for the Applicant to maintain its ordinary course operations while proceeding with its efforts to

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[3] ***1057863 BC Ltd. (Re)***, 2020 BCSC 1359, para 35 **[TAB 2]**
[4] ***Mountain Equipment Co-Operative (Re),*** 2020 BCSC 1586, para 2 **[TAB 3]**

prepare a viable restructuring plan. The proposed initial DIP Loan up to a maximum of $150,000.00 is supported by the Proposed Monitor. The Applicant's cashflow forecast demonstrating the necessity of this is credible and has been independently reviewed.

30. As is standard, the DIP Loan is conditional upon, among other things, the issuance of the proposed Initial Order approving the DIP Term Sheet and granting the DIP Lender a Court-ordered priority charge over the assets and property of the Applicant to secure all amounts advanced (the **"DIP Lender's Charge"),** subject only to the Administration Charge discussed below. The DIP Lender's Charge is both necessary and appropriate.

31. At the Comeback Hearing, the Applicant will seek authority to borrow up to the maximum amount of $500,000.00 permitted by the DIP Term Sheet and will seek a corresponding increase to the DIP Lender's charge in the ARIO.

Appointment of Proposed Monitor

32. Subsection 11.7(1) of the CCAA requires a court, when granting an initial order, to appoint a person to monitor the business and financial affairs of the applicant company.

33. S.R. Stack & Company (2023) Ltd. (the "**Proposed Monitor**") is a "trustee" within the meaning of s. 2 of the BIA and is not subject to any of the restrictions on who may be appointed as Monitor set out in s. 11.7(2) of the CCAA.

34. The Proposed Monitor has consented to act as Monitor for the Applicant, subject to this Court's approval. The Proposed Monitor is experienced in the Newfoundland and Labrador business community and can perform monitoring functions without delay and is well-suited to this mandate. To ensure a thorough approach, the Proposed Monitor will collaborate with the Proposed Chief Restructuring Officer to develop a viable restructuring plan. The Chief Restructuring Officer will offer essential support and expertise, providing insights into financial analysis, strategic planning, and risk management.

35. The Applicant believes that it is in its best interests that the Proposed Monitor be appointed as Monitor.

Administration Charge

36. The Court may grant an administration charge pursuant to s. 11.52 of the CCAA. In deciding whether to grant an administration charge, courts may consider a number of

factors, including: (a) the size and complexity of the businesses being restructured; (b) the proposed role of the beneficiaries of the charge; (c) whether there is an unwarranted duplication of roles; (d) whether the quantum of the proposed charge appears to be fair and reasonable; (e) the position of the secured creditors likely to be affected by the charge; and (f) the position of the Monitor.[5]

37. The Professionals whose fees will be secured by the Administration Charge are: (i) the Proposed Monitor and its counsel; (ii) the Applicant's counsel; and (iii) the Proposed Chief Restructuring Officer. Their support is indispensable to the restructuring.

38. An initial aggregate Administration Charge of $250,000.00 is fair, reasonable, and proportionate. This amount is consistent with charges granted in similar Atlantic Canada proceedings of comparable size. It is required upfront based on livestock urgency and the immediate restructuring efforts required. There is no unnecessary duplication among the proposed team of Professionals. The CRO's role is intended to compliment the Monitor's role and reduce overall Monitor costs.

39. As is typical and contemplated in all CCAA model orders, the Administration Charge will be secured by a charge on all the Applicant's present and future assets, property, and undertakings, ranking ahead of all Applicant's other secured and unsecured creditors. This Administrative Charge does not unduly prejudice the Applicant's creditors when considered against the benefit that the Professionals will bring to the CCAA proceeding.

40. The Proposed Monitor is supportive of the Administration Charge and believes it to be to the benefit of all stakeholders.

Ability to Pay Various Key Expenses with Approval of the Monitor

41. During these CCAA proceedings, the Applicant proposes to pay amounts owing for essential goods or services supplied to the Applicant prior to the Initial Order, if, in the opinion of the Monitor, the payment is necessary and appropriate.

42. Courts can authorize an applicant to pay certain amounts, including pre-filing amounts, to suppliers where the applicant is not seeking a charge in respect of critical suppliers.[6] Factors to consider are the following:

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[5] ***Walter Energy Canada Holdings, Inc (Re)***, 2016 BCSC 107 at para 42 **[TAB 4]**
[6] ***Cinram International Inc. (Re)***, 2012 ONSC 3767, para 68 **[TAB 5]**

a) whether the goods and services were integral to the business of the applicants;

b) the applicants' dependency on the uninterrupted supply of the goods or services;

c) the fact that no payments would be made without the consent of the Monitor;

d) the Monitor's support and willingness to work with the applicants to ensure that payments to suppliers in respect of pre-filing liabilities are minimized;

e) whether the applicants had sufficient inventory of the goods on hand to meet their needs; and

f) the effect on the debtors' ongoing operations and ability to restructure if they were unable to make pre-filing payments to their critical suppliers.

43. The Applicant relies on the efficient and sometimes expedited supply of products and services from critical suppliers (ex. feed, diesel, veterinary services) to ensure that its operations operate efficiently to meet its quota. Major operational disruptions would impair herd productivity/health and impede the Applicant's cash flow and restructuring efforts.

A Partial Sealing Order is Required

44. One exhibit to the Initial Affidavit, relating to the Farm Mediation Process, contains commercially sensitive information. The Applicant seeks a narrowly tailored sealing order limited solely to this exhibit.

45. The requested sealing order is limited in scope and balances the "open court" principle with the legitimate commercial requirements for confidentiality in the circumstances. The benefits of the requested sealing order outweigh the negative impact on the "open court" principle. This satisfies the ***Sierra Club of Canada v. Canada (Minister of Finance)*** requirements, as modified in ***Sherman Estate v. Donovan***.[7]

CONCLUSION:

46. The Applicant requires immediate CCAA protection. As stated in the Initial Affidavit, the Applicant supplies over 15% of the on-island dairy. It is vital from a food security perspective that operations at the Farm continue while the Applicant restructures.

47. The proposed Initial Order will provide the Applicant with the necessary breathing room to stabilize and remain in control of its business while reviewing operational and financial

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[7] ***Sierra Club of Canada v. Canada (Minister of Finance)***, 2002 SCC 41; ***Sherman Estate v. Donovan***, 2021 SCC 25, para. 38 [copies available upon request]

restructuring options with the Proposed Monitor. The Applicant is seeking only what is reasonable and necessary in the circumstances. The relief sought is strictly interim and limited to what is required to stabilize operations pending the Comeback Hearing.

48. At the s. 11.02 Comeback Hearing, the Applicant will update the Court on the status and timing of its proposed plan, will establish that they have been acting in good faith and with due diligence, as required by s. 11.02(3), will seek an extension of the stay, and will seek an increase in the DIP loan, along with such other reasonable and necessary relief as determined in consultation with the Proposed Monitor.

RELIEF SOUGHT:

49. The Applicant seeks (a) a "first-day" Initial Order pursuant to the CCAA substantially in the form attached as **Schedule "B"** to this Notice of Application, including the relief summarized in paragraph 1 of this Application, and (b) a "sealing order" as set out in paragraph 1 above. The proposed Initial Order is substantially in the form of the Model Order.

DATED at St. John's, Newfoundland and Labrador, this 4th day of September 2025.

O'KEEFE & SULLIVAN

Megan Taylor

DARREN D. O'KEEFE
MEGAN TAYLOR
Counsel for the Applicant
80 Elizabeth Avenue, Suite 202
St. John's, NL, A1A 1W7
dokeefe@okeefesullivan.com
mtaylor@okeefesullivan.com

TO: Counsel and parties listed in the Service List attached as **Schedule "A"**.

SCHEDULE "A"

SERVICE LIST

Ocean View Farms Limited (the "**Applicant**" or "**OVFL**")

PARTY	CONTACT
Ocean View Farms Limited Farm Road P.O. Box 108 Bay Bulls NL, A0A 1C0 **Applicant**	**O'Keefe & Sullivan** 80 Elizabeth Ave., Suite 202 St. John's, NL, A1A 1W7 **Counsel for the Applicant** **Darren D. O'Keefe** Email: dokeefe@okeefesullivan.com **Megan Taylor** Email: mtaylor@okeefesullivan.com
S.R. Stack & Company (2023) Ltd. Suite 101, Regatta Plaza II 84-86 Elizabeth Ave., St. John's, NL, A1A 1W7 **Proposed Monitor**	**Sean R. Stack** Email: sean@srstack.ca
Resolve Advisory Services Ltd. **Proposed Chief Restructuring Officer for the Applicants**	**David Boyd** Email: davidboyd@resolveadvisory.ca **Chris Brown** Email: chrisbrown@resolveadvisory.ca
Boyne Clarke Lawyers 99 Wyse Road, Suite 600 P.O. Box 876, Dartmouth Main Dartmouth, NS, B2Y 3Z5 **Counsel for the Proposed Monitor**	**Joshua Santimaw** Email: JSantimaw@boyenclarke.ca
The Bank of Nova Scotia 10 Wright Boulevard Stratford, ON, N5A 7X9 **The Bank of Nova Scotia** Pejavar, Anuradha Lending Services Commercial Banking	**Cox & Palmer** 235 Water Street, Suite 1100 St. John's, NL, A1C 1BC **Counsel for Bank of Nova Scotia**

4715 Tahoe Boulevard Mississauga, ON, L4W 0B4	**Mark Russell** Email: MRussell@coxandpalmer.com
Canada Revenue Agency Insolvency Intake Centre Shawinigan – Sud National Verification and Collections Centre 4695 Shawinigan-Sud Boulevard Shawinigan, QC G9P 5H9	**Maeve Baird** Email: Maeve.Baird@justice.gc.ca **Caitlin Ward** Email: caitlin.ward@justice.gc.ca
Town of Bay Bulls 2 Southside Road P.O. Box 70 Bay Bulls, NL A0A 1C0	Email: info@townofbaybulls.com
Workplace NL P.O Box 9000 St. John's, NL A1A 3B8	**Jennifer Langdon** Email: jennifer.langdon@workplacenl.ca
Office of the Superintendent of Bankruptcy Canada Maritime Centre 1505 Barrington Street, 16th Floor Halifax, NS B3J 3K5	Email: osbccaa-laccbsf@ised-isde.gc.ca
Truro Agromart Limited 547 Onslow Road Upper Onslow, NS, B6L 5L3	Email: office@truroagromart.ca
Atlantic Provinces Department of Justice Legal Services Division Atlantic Regional Office Suite 1400, Duke Tower 5251 Duke Street Halifax, Nova Scotia B3J 1P3	**Atlantic Canada** Email: AGC_PGC_ARO-BRA@JUSTICE.GC.CA

Email List

dokeefe@okeefesullivan.com; mtaylor@okeefesullivan.com; mdecaria@okeefesullivan.com; smudekwe@okeefesullivan.com; sean@srstack.ca; davidboyd@resolveadvisory.ca; JSantimaw@boyenclarke.ca; MRussell@coxandpalmer.com; deanna.frappier@justice.gc.ca; caitlin.ward@justice.gc.ca; osbccaa-laccbsf@ised-isde.gc.ca; Maeve.Baird@justice.gc.ca; osbccaa-laccbsf@ised-isde.gc.ca; office@truroagromart.ca; AGC_PGC_ARO-BRA@JUSTICE.GC.CA; info@townofbaybulls.com;

APPLICANT'S MEMORANDUM OF FACT AND LAW

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TAB NUMBER	CASE NAME
1	***Edward Collins Contracting Limited (Re),*** 2022 NLSC
2	***1057863 BC Ltd. (Re)****,* 2020 BCSC 1359
3	***Mountain Equipment Co-Operative (Re),*** 2020 BCSC 1586
4	***Walter Energy Canada Holdings, Inc (Re)***, 2016 BCSC
5	***Cinram International Inc. (Re)***, 2012 ONSC 3767

IN THE SUPREME COURT OF NEWFOUNDLAND AND LABRADOR
GENERAL DIVISION
In Bankruptcy and Insolvency

2022 NLSC 149 (CanLII)

Citation: *Edward Collins Contracting Limited (Re)*, 2022 NLSC 149
Date: October 14, 2022
Docket: 202201G1964

IN THE MATTER OF the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36, as amended (the "*CCAA*")

AND IN THE MATTER OF an application of Edward Collins Contracting Limited, Classic Security Ltd., FGC Holdings Ltd., 51037 Newfoundland and Labrador Inc. and H & E Designs Ltd. (collectively, the "Companies ")

- AND -

Docket: 202201G1853

IN THE MATTER OF the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3, as amended (the "*BIA*");

AND IN THE MATTER OF the Receivership of Edward Collins Contracting Limited, H & E Designs Ltd., Classic Security Ltd., FGC Holdings Ltd. and 51037 Newfoundland and Labrador Inc.

BETWEEN:

ROYAL BANK OF CANADA

APPLICANT

AND:

EDWARD COLLINS CONTRACTING LIMITED, H & E DESIGNS LTD., CLASSIC SECURITY LTD., FGC HOLDINGS LTD. and 51037 NEWFOUNDLAND AND LABRADOR INC.

RESPONDENTS

2022 NLSC 149 (CanLII)

Before: Justice Alexander MacDonald
Edited Transcript of Oral Reasons for Judgment

Place of Hearing:	St. John's, Newfoundland and Labrador
Dates of Hearing:	September 16, 2022 and September 28-29, 2022
Date of Oral Judgment:	October 5, 2022

Appearances:

Darren D. O'Keefe	Appearing on behalf of the Companies
Neil L. Jacobs, K.C. and Joseph J. Thorne	Appearing on behalf of Royal Bank of Canada
Maeve A. Baird	Appearing on behalf of the Minister of National Revenue

David L. Hearn	Appearing on behalf of the Government of Newfoundland and Labrador
Andrew Punzo and Mark A. Borgo	Appearing on behalf of Western Surety Company
Tim Hill, K.C. and Joshua J. Santimaw	Appearing on behalf of Daimler Truck Financial Services Canada Corporation
Andrew A. Fitzgerald, K.C.	Appearing on behalf of S.R. Stack & Company Ltd.
Phil Clarke	Appearing on behalf of Grant Thornton Limited, the Proposed Monitor
Steven McLaughlin	Appearing on behalf of Ernst & Young Inc.

Authorities Cited:

CASES CONSIDERED: *9354-9186 Québec Inc. v. Callidus Capital Corp.*, 2020 SCC 10; *Ted Leroy Trucking [Century Services] Ltd., Re*, 2010 SCC 60; *Norcon Marine Services Ltd., (Re)*, 2019 NLSC 238; *Hester Creek Estate Winery Ltd., Re*, 2004 BCSC 345; *United Used Auto & Truck Parts Ltd., Re*, (1999), 12 C.B.R. (4th) 144, 93 A.C.W.S. (3d) 411 (B.C.S.C.); *Montréal (Ville) c. Restructuration Deloitte Inc.*, 2021 SCC 53; *Industrial Properties Regina Limited v. Copper Sands Land Corp.*, 2018 SKCA 36

STATUTES CONSIDERED: *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36; *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3

REASONS FOR JUDGMENT

MACDONALD J.:

INTRODUCTION

[1] On July 8, 2022, the Royal Bank of Canada ("RBC") applied to appoint Ernst and Young Inc. as a court-appointed receiver over all or substantially all of the assets

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of Edward Collins Contracting Limited, Classic Security Ltd., FGC Holdings Ltd., 51037 Newfoundland and Labrador Inc. and H & E Designs Ltd ("Companies"). The Companies oppose the application.

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[2] On July 18, 2022, the Companies applied for creditor protection and other relief under the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36, as amended ("*CCAA*"). They asked me to grant an initial order called for under section 11.02(1)(a) of the *CCAA* ("Initial Order"). If I deny the Initial Order, they ask that I dismiss the receivership application.

[3] On July 19 and 20, 2022, the Court heard the parties on both applications. The Court informed the parties that it could not hear these matters until September 16, 2022.

[4] On July 20, 2022, the Court granted a consent order ("Consent Order"). The Court ordered that any person having a contractual arrangement or a statutory mandate for the supply of goods or services, were restrained until further order from the Court from discontinuing, altering or terminating the supply of such goods or services ("Consent Stay") until September 16, 2022 ("Consent Stay Period").

[5] I heard both applications on September 16, 28 and 29, 2022. On September 16, 2022, I continued the Consent Order until now.

[6] The parties agree that I will deal with the *CCAA* application first. If I dismiss the *CCAA* application, I will then deal with the receivership application. I now turn to the *CCAA* application.

CCAA APPLICATION

[7] RBC, the principal secured creditor of the Companies, and Daimler Truck Financial Services Canada Corporation, a secured lender of certain equipment, oppose the *CCAA* application.

[8] The Western Surety Company ("Surety"), Edward Collins Contracting Limited's ("Collins Contracting") construction surety provider, the Canada Revenue Agency ("CRA"), and the other parties at the hearing neither supported nor opposed the *CCAA* application.

[9] I hereby grant the Companies the Initial Order which I attach as Schedule A. I will now explain why I made this decision.

[10] I have considered:

(a) Do the Companies have standing under the *CCAA*?

(b) Have the Companies satisfied the test to allow me to grant an Initial Order?

(c) If so, should the Companies' conduct during the Consent Stay cause me to refuse the Initial Order? and

(d) Did the Companies act in bad faith?

[11] I will then deal with:

(a) Should the Court exercise its discretion to grant the administration charge? and

(b) What conditions should I impose in the Initial Order?

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[12] I will first deal with whether the Companies have standing under the *CCAA*.

Do the Companies have standing under the *CCAA*?

[13] I find the Companies have standing under the *CCAA*. The *CCAA* applies to a debtor company or affiliated debtor Companies, if they are insolvent or have committed an act of bankruptcy and owe more than $5 million.

[14] The Companies owe RBC in excess of $5 million and CRA about $4.9 million. I am satisfied that the Companies are insolvent.

[15] Thus, I find that the Companies qualify as debtor companies under the *CCAA*. I now turn to whether the Companies met the test to allow me to issue an Initial Order.

Have the Companies satisfied the test to allow me to issue an Initial Order

[16] I find that the Companies have satisfied the test. I will now explain why I made that decision.

[17] Under section 11.02(1)(a) of the *CCAA*, I may pursuant to an initial order stay all proceedings against the Companies for not more than 10 days.

[18] The Supreme Court of Canada in *9354-9186 Québec Inc. v. Callidus Capital Corp.*, 2020 SCC 10 ("*Callidus*"), gives me guidance on the purpose and objectives of the *CCAA* in paragraphs 39 to 42. I will now summarize that guidance.

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[19] The *CCAA* is one of three principal insolvency statutes in Canada. Canada's insolvency statutes pursue an array of overarching remedial objectives that reflect the wide ranging and potentially "catastrophic" impacts insolvency can have.

[20] These objectives include:

(a) providing for timely, efficient and impartial resolution of a debtor's insolvency;

(b) preserving and maximizing the value of a debtor's assets;

(c) ensuring fair and equitable treatment of the claims against a debtor;

(d) protecting the public interest; and

(e) balancing the costs and benefits of restructuring or liquidating the company.

[21] Among these objectives, the *CCAA* generally prioritizes avoiding the social and economic losses resulting from liquidation of an insolvent company.

[22] The typical *CCAA* case has historically involved an attempt to facilitate the reorganization and survival of the pre-filing debtor company in an operational state – that is, as a going concern.

[23] However, the *CCAA* is fundamentally insolvency legislation, and thus it also "has the simultaneous objectives of maximizing creditor recovery, preservation of going-concern value where possible, preservation of jobs and communities affected by the firm's financial distress ... and enhancement of the credit system generally". (*Callidus* at para. 42).

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[24] *CCAA* proceedings have evolved to permit outcomes that do not result in the emergence of the pre-filing debtor company in a restructured state, but rather involve some form of liquidation of the debtor's assets under the auspices of the *CCAA* itself. Such scenarios are referred to as "liquidating *CCAA*s", and they are now commonplace in *CCAA* applications.

[25] Liquidating *CCAA*s take diverse forms and may involve:

(a) the sale of the debtor company as a going concern;

(b) an "en bloc" sale of assets that are capable of being operationalized by a buyer;

(c) a partial liquidation or downsizing of business operations; or

(d) a piecemeal sale of assets (*Callidus* at para. 43).

[26] In this case, the Companies seek the reorganization and survival of the Companies as a going concern. That is not to say the Companies' plans may change when it formulates its final restructuring plan.

[27] Under Section 11.02(1) of the *CCAA*, I may, in an initial order, make any orders I see fit. I may:

(a) Stay proceedings under the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3 ("*BIA"*); and

(b) restrain proceedings in any existing action against the Companies and prohibit any new action against them.

[28] I cannot make the Initial Order effective for more than 10 days.

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[29] Under subsection 11.02(2) of the *CCAA*, I can amend the Initial Order and extend the stay at a so-called comeback hearing. I must hold the hearing before the expiry of the stay in the Initial Order. I may amend these Orders. I will call these amendments the Amended Orders.

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[30] Under section 11.02(3) of the *CCAA*, I cannot grant an Amended Order unless the Companies satisfy me that:

(a) circumstances exist that make the extension appropriate; and

(b) they are acting in good faith and with due diligence.

[31] Section 11.02(3)(b) of the *CCAA* says, "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". Subsection 2 deals with orders after the initial order.

[32] Despite the wording of section 11.02(3)(b) indicating "good faith and due diligence" applies only to orders under subsection (2), that being orders "other than initial applications", the Supreme Court of Canada in *Ted Leroy Trucking [Century Services] Ltd., Re*, 2010 SCC 60 at para. 69, determined good faith and due diligence applies to initial orders as well.

[33] It said at paragraph 70 that "the requirements of appropriateness, good faith, and due diligence are baseline considerations that a court should always bear in mind when exercising *CCAA* authority".

[34] Under section 11.7(1) of the *CCAA*, when I make an Initial Order, I must appoint a person to monitor the business and financial affairs of the Companies. The monitor must be a trustee, defined in section 2 of the *BIA*. The Companies ask that I appoint Grant Thornton Limited, represented by Phil Clarke, Senior Vice-President and Bankruptcy Trustee ("Proposed Monitor").

[35] During the currency of the Initial Order and comeback Amended Orders, the Companies attempt to complete a plan of compromise and arrangement with its creditors. The Proposed Monitor assists them. The Proposed Monitor, as an officer of the Court, periodically reports to the Court on the progress of the plan.

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[36] I will now turn to the circumstances the Companies must show me to allow me to grant the Initial Order.

Legal Test – Contents of Plan

[37] Justice Orsborn in *Norcon Marine Services Ltd., (Re)*, 2019 NLSC 238, said at paragraph 15, that I should consider whether the Companies have some chance, by engaging the *CCAA* process, of furthering the purposes of the legislation.

[38] Justice Orsborn observed the Companies must overcome a low bar to trigger the *CCAA* process. However, the Companies must do more than simply ask for time.

[39] The Companies must put forth "a germ of a plan" that suggests "a reasonable possibility of restructuring" (*Norcon* at para. 16). However, they need not present a fully developed plan at the initial hearing, nor are they required to have the support of all of their creditors.

[40] To put this test in context, I will now describe the financial difficulties the Companies find themselves in and how these difficulties arose.

Companies' Financial Woes

[41] Collins Contracting is a general contractor specializing in roadworks. As described in the affidavit of David Savoie, Business Specialist with RBC, in the 2019

fiscal year, its revenue was $12.1 million and its net income was $393,000. In the 2020 FY, its revenue was $11.4 million and its profit was $310,000.[1] Significantly, Collins Contracting's obligation to CRA increased from about $60,000 to about $451,000.[2]

[42] He says that in the 2021 FY, the Companies' revenue decreased to $8.5 million. Its 2020 FY profit became a $3.4 million loss in 2021. This loss was incurred despite Collins Contracting's $1.2 million emergency wage subsidy from Canada.[3]

[43] He further says the information in the 2021 financial statements caused Collins Contracting to be in default of the RBC loan facility because it no longer had minimum debt service coverage ratio of 1.25X called for in the loan facility.[4]

[44] Because of the Companies' financial difficulties and default, on December 31, 2021, RBC, Collins Contracting, H & E Designs Ltd., Frank Collins and Josh Collins executed the forbearance agreement.

[45] In the agreement, Collins Contracting acknowledges it is in default of its obligations to RBC. It agreed to provide interim financial statements and CRA balance reporting.

[46] It also agreed, at paragraph 1(e), to "confirm the rights and remedies available to the Bank under the Security are fully and immediately enforceable by [RBC] and hereby waive all notice periods of application thereto, including notice period of application under Section 244 of the [*BIA*]".

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[1] Affidavit of David Savoie, filed August 5, 2022, [Savoie Affidavit], at para. 15.
[2] *Ibid.* at para. 16.
[3] *Ibid.* at para. 34.
[4] *Ibid.*

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[47] In the second recital of the agreement, RBC agreed not to call it loans until February 28, 2022.

[48] Collins Contracting provided RBC monthly interim year-to-date financial statements from October, 2021 to March, 2022. All showed a continued deterioration of Collins Contracting's financial position.[5]

[49] The March 2022 interim statement, provided to RBC on June 9, 2022, shows revenue of $5.3 million, compared to forecasted revenue of $15.2 million, and a net loss of $2.1 million compared to forecasted net income of $3 million. The amount owing to CRA was then about $3.2 million.[6]

[50] Thus, over the 2021 FY and up to March 2022 FY, the Companies incurred a cumulative loss of about $5.5 million. Its CRA obligation increased from $451,000 in 2020 to $3.2 million.

[51] RBC demanded its loans on July 17, 2022. RBC was owed, as of June 15, 2022, more than $5 million, together with interest, expenses and fees.[7]

[52] CRA filed an affidavit on September 12, 2022, of Mark Lohnes, Resource Officer/Complex Case Officer with CRA. He said that the Companies owe CRA about $4.9 million. He said that over $3.3 million is for deemed trust unremitted employee payroll source deductions and HST.[8] This, excluding interest and penalties, is the so-called deemed trust debt.

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[5] *Ibid.* at paras. 39-51.
[6] *Ibid.* at para. 51.
[7] Receivership Originating Application, filed July 8, 2022 at para 11.
[8] Affidavit of Mark Lohnes, filed September 12, 2022, [Lohnes Affidavit] at para. 38.

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[53] CRA says Collins Contracting owes almost $4 million of this amount. It says about $2 million (excluding penalties and interest) is for deemed trust for unremitted employee payroll source deductions ("Payroll deemed trust debt") and about $756,000 for HST deemed trust debt.[9]

[54] In paragraph 38, CRA says the remainder of the Companies owe CRA about $939,000. About $348,000 (excluding penalties and interest) is for Payroll deemed trust debt and about $205,500 is for HST deemed trust debt.[10]

[55] CRA says that Collins Contracting last remitted amounts in March 2022, and it was the last of the Companies to do so. The Proposed Monitor said, and I accept, that he made remittances over the summer of Collins Contracting's monies owed to CRA for that period, but he did not remit any of the arrears.

[56] CRA is in the process of reviewing the Companies' accounts, and it will determine the final arrears after that review. The timing of this review is currently within the control of CRA, and its counsel could not provide me any guidance on when this review might begin or end.

[57] The Companies provided little explanation for their financial difficulties in its application or in Francis Collins' July 18, 2022 affidavit. They did not explain how it incurred the CRA debt.

[58] On July 18, 2022, Francis Collins, director of the Companies, filed an affidavit supporting the initial application. He provided me with the Companies' 2021 FY financial statements, but provided no cash flow statements or any other historical financial data.

[9] *Ibid.* at para. 19.
[10] *Ibid.* at para. 38.

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[59] Francis Collins, addressed the CRA balances by saying, "As appears from the Company's books and records, there is currently a significant amount outstanding to the Canada Revenue Agency ("CRA"). The Company is actively working with CRA to determine the full outstanding balances and to work on a payment plan to relieve this liability. The Company is hopeful that the CCAA proceedings will bring CRA to the table to discuss options, as to date CRA has not been forthcoming with information or responsive to requests from the Company to discuss the Company's CRA's position of potential discrepancies in CRA's accounting."[11]

[60] This statement shows, at best, a disturbing lack of awareness of how the Companies incurred almost $5 million in CRA obligations, including almost $3.3 million in deemed trust amounts for both income tax and HST.

[61] On September 23, 2022, Josh Collins filed an affidavit to provide me with further information. He answers the question, "How did [Edward Collins Contracting Limited] get itself into financial trouble and accumulate such a high amount of CRA Debt?"[12] He says two primary events caused both.

[62] The first event is the purchase of a defective asphalt plant. Collins Contracting underestimated the risk of purchasing a defective plant and the cost and time necessary to rectify the plant deficiencies and to bring its software up-to-date.[13]

[63] The second event is the collapse of Collins Contracting's revenue during COVID-19.[14]

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[11] Affidavit of Francis Collins, filed July 18, 2022 at para. 12.
[12] Affidavit of Josh Collins, filed September 23, 2022 [Collins' Second Affidavit], at heading A.
[13] *Ibid.* at paras. 3-12.
[14] *Ibid.* at paras. 14-25.

[64] He says that both events contributed to a loss of almost $3 million in 2021.[15] RBC said the loss was $3.4 million and I can only assume this was because Mr. Savoie relied on interim rather than final statements.

[65] Josh Collins admits that Collins Contracting maintained its liquidity despite these losses by not paying their CRA obligations,[16] and in May 2020 by borrowing $1 million from RBC by way of a $1 million loan under the so-called "Highly Affected Sectors Credit Availability Program" ("HASCAP"). The Government of Canada guaranteed this HASCAP loan. This program is designed to support companies that suffered financially during the COVID-19 epidemic.

[66] The Proposed Monitor confirms in his first pre-filing report that the unpaid CRA funds "were used to offset the acquisition and operating losses incurred" for capital acquisitions, losses for underutilized equipment and other operational losses.[17] In paragraph 21(b), the Proposed Monitor also identifies that Collins contracting lost more than $1 million dollars on an unfavourable bridge construction contract.

[67] Thus, I find the triggering causes of the Companies' financial crisis are an improvident capital purchase, an unfavourable construction contract, and the general collapse of the Companies' revenue and its resulting operating losses. This in turn caused the Companies not to pay the deemed trust debt to CRA to fund these losses.

[68] This, together with the collapse in the Companies' retained earnings[18] and profits and the increase in CRA's deemed trust debt, caused RBC to take action to protect its security from further erosion.

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[15] *Ibid.* at para. 17.
[16] *Ibid.* at para. 18.
[17] Pre-filing Report of Grant Thornton Limited, September 15, 2022 [Proposed Monitor's First Pre-filing Report], at para. 21(c).
[18] *Supra* note 12 at para. 20 (from about $2.9 million to almost nothing in 2021).

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[69] Having discussed the cause of the Companies' financial problems, I now turn to whether the Companies put forth "a germ of a plan" that suggests "a reasonable possibility of restructuring". (*Norcon* at para. 16)

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Companies' "Germ of a Plan"

[70] I find that they have. I now will explain why I made that decision.

[71] The Companies' plan is contained in the Proposed Monitor's first and second pre-filing reports and in affidavits from Josh Collins.

[72] The plan is based on two pillars. The first pillar is the prospect of Travelers Capital refinancing the Companies' debt obligations. The Companies provided me with an executed "summary of terms and conditions" dated September 22, 2022. Joshua Collins is named as a guarantor. I will call this the Term Sheet.

[73] The Term Sheet indicates that Travelers will lend the Companies 90% of the appraised forced liquidation value of the Companies' equipment value and 50% of the appraised value of certain real property. Travelers estimates this value is $6,796,490.

[74] The Companies provided me with the forced liquidation value appraisal on September 23, 2022. The Proposed Monitor tells me the valuation supports the valuation of the equipment in the Term Sheet.

[75] Travelers also requires that the Companies provide it with:

(a) completed environmental reports on specified property;

(b) real estate appraisals;

(c) forward-looking income and cash flow statements; and

(d) Year-to-date statements and historical three-year prior financial statements.

[76] On September 22, 2022, the Companies filed copies of:

(a) an appraisal of a residence on Lakeview Dr. in Deer Lake;

(b) A real estate agent's assessment of a property at 30 Reid's Lane in Deer Lake;

(c) an appraisal of Collins Contracting's office building in Placentia;

(d) an appraisal of a real estate development;

(e) a purchase and sale agreement for property on Charter Avenue in Placentia; and

(f) an offer to purchase property at 28-30 Reid's Lane in Deer Lake.

[77] The total value of real estate described in these filings is about $2.75 million.

[78] The Term Sheet also provides that Travelers must be satisfied that the Companies have paid all CRA priority payments. As the CRA priority payments are not current, I presume they mean that the CRA priority debt must be retired from the proceeds of the loan.

[79] The Term Sheet lists all the Companies as borrowers. Thus, this condition would include deemed trust amounts due to CRA, or at least that portion that could rank ahead of Travelers' security if they remain unpaid on closing.

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[80] However, the Proposed Monitor testified at the hearing that Travelers has agreed that the HST deemed trust debt need not be paid on closing. He also said he "understands" that CRA is open to compromising the HST deemed trust debt.

[81] Thus, it seems that Travelers will expect that the HST liability will be resolved by agreement with CRA or pursuant to a *CCAA* order before it advances funds under the Term Sheet.

[82] Travelers says in the Term Sheet that the total outstanding amounts to secured creditors and the CRA total is $7,058,337. It says this must be paid on closing.

[83] Josh Collins in his affidavit filed September 13, 2022, said there is a shortfall of about $250,000 between the amount of the Travelers' loan and the debt the Companies must repay on closing. I will call this the Loan Gap. He said the Companies can finance the Loan Gap through a variety of sources being from:

(a) $253,000 owed to the Companies by Olympic Construction Ltd. He did not provide me with any evidence of this amount or an acknowledgement from Olympic that this amount is due;

(b) a potential sale of real property in Deer Lake based on an expression of interest with an asking price of $500,000. He said, "If this offer materializes, we will net approximately $250,000".[19] On September 22, 2022, he provided me with an offer of purchase and sale for a piece of property in Deer Lake for less than that amount; and

(c) sale of equipment by the Companies for about $250,000 once they "further review our operational needs".[20] This is highly contingent. It is subject to a review of operational needs. I have no evidence of the value of this equipment. I do not know if Travelers intends to take security over this equipment.

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[19] Affidavit of Josh Collins, filed September 13, 2022 [Collins' First Affidavit], at para. 67(b).
[20] *Ibid.* at para. 67(c).

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[84] Even if the Companies can access this money, I do not accept that the Loan Gap is only $250,000.

[85] The Proposed Monitor provided an analysis of the amount Collins Contracting owes to CRA. He largely agrees with CRA's position but states that interest and penalties are not deemed trust amounts.

[86] He concludes that Collins Contracting and 51037 Newfoundland and Labrador Inc., after excluding interest and penalties, owes about $2.2 million in Payroll deemed trust debt. He acknowledges that CRA claims Collins Contracting owes it about $756,000 in HST deemed trust debt. However, he did not do an analysis in which he breaks out interest and penalties.

[87] He did not do a similar analysis for the remaining Companies. I only have CRA's evidence. It said that Classic Security Ltd. owes about $348,000 in payroll deemed trust amounts and about $151,000 in HST deemed trust debt, while H & E Designs Ltd. and FGC Holdings Ltd. owe about $28,000.[21] I do not know what portion of these is interest and penalties.

[88] In his second report filed on September 26, 2022, the Proposed Monitor disagrees with Josh Collins' Loan Gap. He said it is $473,362.[22]

[89] He said that the Companies now intend to close the Loan Gap by selling instead of financing one of the Reid Lane properties, thereby achieving a contribution of 100% of the sale price rather than 50% of its appraised value. This would net $199,000.[23]

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[21] Affidavit of Mark Lohnes, filed September 12, 2022 at paras. 27, 34 and 37.
[22] Pre-filing Report of Grant Thornton Limited, filed September 26, 2022 [Proposed Monitor's Second Pre-Filing Report] at 5.
[23] *Ibid.* at para. 17(a).

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[90] Both he and Josh Collins say Collins Contracting is a beneficiary under a $500,000 insurance policy now, as the insureds died.[24] The Collinses say they discovered the existence of this policy at the end of August 2022.

[91] The Proposed Monitor said that only half of this amount, or $250,000, is available to offset the Loan Gap. The other half will be used to bolster Collins Contracting's cash flow.[25] I will discuss Collins Contracting's cash flow statements later in this decision.

[92] The Proposed Monitor described how Collins Contracting intends to sell equipment to realize more cash than Travelers 90% forced liquidation financing would generate.[26]

[93] However, the Loan Gap is likely larger unless RBC continues to hold some of its debts, notably the HASCAP.

[94] Furthermore, the Proposed Monitor says the Companies' estimated value of real estate is about $3.3 million.[27]

[95] However, the Companies' submitted appraisals, drive-by estimates and agreements of purchase and sale totaling about $2.7 million. Furthermore, the Proposed Monitor says the real estate value is $65,000 less than Travelers' estimate.[28] Although the difference is not material to my decision, I ask the Proposed Monitor to explain the discrepancy at or before the comeback hearing.

[24] *Ibid.* at para. 17(b).
[25] *Ibid.* at paras. 17(c) and 17(d).
[26] *Ibid.* at para. 18.
[27] *Ibid.* at para. 14(a).
[28] *Ibid.* at para.16(a).

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[96] Travelers provides in the Term Sheet that the Companies are to repay the loan principal in 24 monthly blended installments of principal and interest, with interest at the rate of 12.75%. The loan amounts are amortized up to 120 months for real estate, and 60 for equipment. The loan balance is payable at the end of the 24 months.[29]

[97] This would seem to require the Companies to repay large sums of monies over two years. Presumably, the Companies will need to satisfy Travelers that they can meet this obligation when it submits is forward-looking pro-forma income statement.

[98] Finally, the Term Sheet is subject to a condition that said, "Final approval of the subject Loan transaction and the Loan Agreement, in form and in substance, by [Travelers'] credit committee."[30] Thus, Travelers is not yet bound to the Term Sheet.

[99] I will now turn to the second pillar of the Companies' restructuring plan - positive cash flow from existing contracts.

The Cash Flow Statements

[100] The *CCAA* requires the Companies to provide weekly projected cash flow statements. The Companies should make disclosure of all material facts known to them (see *Hester Creek Estate Winery Ltd., Re*, 2004 BCSC 345 at para. 5). The standard of disclosure expected of the Companies in these cash flow statements must be realistic (see *United Used Auto & Truck Parts Ltd., Re*, (1999), 12 C.B.R. (4th) 144, 93 A.C.W.S. (3d) 411 at para. 14 (B.C.S.C.).

[29] *Supra* note 19, Tab L, Travelers Term Sheet [Travelers Term Sheet].
[30] Travelers Loan Sheet, Conditions Precedent to Closing, clause 1.

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[101] I find that these cash flow statements are adequate to support an Initial Order. In the absence of other evidence, the disclosure is realistic and there is no evidence that the Companies have not disclosed all material facts known to them.

[102] If this is not so, the Companies risk an application to set aside the Initial Order. In such an application, the test is whether the undisclosed facts may well have affected the outcome had they been known at the time of the application.

[103] In his first pre-filing report, the Proposed Monitor submitted cash flow statements for a 19-week period from September 17, 2022 to January 27, 2023. He said he prepared cash flow statements for 19 weeks because this gives the Companies time to complete the Travelers refinancing.

[104] In the cash flow statements, found at Tab M of his first pre-filing report, the Proposed Monitor said:

(a) the project cash receipts, mostly from 18 existing construction contracts, is $2.84 million. Its costs associated with this revenue is about $1.19 million;

(b) the Companies' cash flow before operating expenses will be about $1.65 million. Operating expenses will be about $770,000. Thus, the Companies will have a net cumulative cash position of $883,000; and

(c) the cash flow statement includes a speculative "Potential New Projects" column. The Proposed Monitor said these might contribute net cash of $1.2 million. But he does not include this amount as part of his calculated cumulative cash position.

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[105] I have limited information on the status of Collins Contracting's contracts. The Proposed Monitor makes a general statement that the Collins Contracting's trade accounts receivables are about $1.39 million. He said that Collins Contracting' counterparties owe them holdbacks, liquidated damages and force accounts (presumably, he means change orders under existing contracts) of about $1 million.[31]

[106] I do not know if Collins Contracting's counterparties contest these amounts. There is no evidence that the Proposed Monitor did a risk assessment on the potential recovery of these amounts. However, I will not require this information for the purposes of the Initial Order.

[107] The Proposed Monitor said that another counterparty terminated a contract that he did include in his original cash flow. He then submitted revised cash flow statements to address the $225,000 deficiency arising out of the termination. This project is for the Placentia Wellness Centre.[32]

[108] He said Collins Contracting will replace this revenue by allocating $250,000 from the life insurance proceeds.[33]

[109] In his second report, the Proposed Monitor said, "The operational assumptions required to be met to successfully achieve the refinancing include (a) [the Companies] achieve or exceed their cash flow forecast".[34]

[110] Josh Collins responded to my request I made on the first day of the hearing. He said, "Of the four projects where we currently have claims, we are in discussions on two of these projects [the same ones referred to by the Government of Newfoundland and Labrador that I refer to later in this decision] regarding [Collins

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[31] *Supra* note 17 at para. 22(a).
[32] *Supra* note 22 at para. 20(a).
[33] *Ibid.* at para. 20(b).
[34] *Ibid.* at paras. 19 and 19(a).

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Contracting] potentially returning to the projects to complete the work. As of the date of this affidavit we have been asked to present a plan to Western Surety on how we intend to complete the work, for their approval. That work is ongoing."[35]

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[111] I get some comfort from the Proposed Monitor's comments in paragraph 38 of his first pre-filing report. He says that he "has also reviewed the support provided by the Company for the Probable and Hypothetical Assumptions and the preparation and presentation of the Cash Flow Projection".[36]

[112] He goes on and says, "Based on [my] review, nothing has come to [my] attention that causes [me] to believe that, in all material respects:

(a) the Probable and Hypothetical Assumptions are not inconsistent with the purpose of the Cash Flow Projection; and

(b) … the Probable and Hypothetical Assumption, developed by management are not suitably supported and consistent with the Company's plans or do not provide a reasonable basis for the Cash Flow Projection, given the Probable and Hypothetical Assumptions".[37]

[113] However, this comfort goes only so far as he says, "The Cash Flow Forecast has been prepared by management using probable and hypothetical assumptions set out"[38] in the Cash Flow Projections. Thus, Collins Contracting prepared the Cash Flow Projections and the Probable and Hypothetical Assumptions.

[114] The Proposed Monitor did not include two contracts (Numbers 46–21PHP and 12–21PHC) with the Minister of the Department of Transportation and Infrastructure

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[35] *Supra* note 12 at p. 35.
[36] *Supra* note 17 at para. 38.
[37] *Ibid.* at para. 38.
[38] *Ibid.* at para. 37.

("Province") in his cash flow projections. On September 23, 2022, the Province took a motion with respect to these contracts.

[115] It said that on April 8, 2022, the Province declared them in default. The Province called on the Surety's performance bond. The Province has not terminated the two contracts. It said that the Surety accepted responsibility under the bonds.

[116] As the Proposed Monitor did not include these contracts in his cash flow statements, they are not relevant to this application, except to the extent they may give rise to concerns about the other contracts' status.

[117] Under section 21 of the *CCAA*, the owner of the projects can claim set-off. If the Surety responds to these defaults, it may step into the shoes of the owner and then claim set-off.

[118] However, the Supreme Court of Canada in *Montréal (Ville) c. Restructuration Deloitte Inc.*, 2021 SCC 53, at para. 63 said, "Although s. 21 of the *CCAA* indicates that there is a right to effect compensation in proceedings under that statute, we are of the opinion that it applies only to compensation [set-off] between debts that arise *before an initial order is made* (in other words, 'pre-pre compensation')". [Emphasis in original.]

[119] It also said at paragraph 63, "s. 21 of the *CCAA* does not grant creditors a right to pre-post compensation that would be shielded from a supervising judge's power to order a stay under ss. 11 and 11.02 of the *CCAA*."

[120] At paragraph 62 it said "it is our view that in the vast majority of cases an initial order will, and should, stay a creditor's right to set up pre-post compensation against the debtor. Finally, where an initial order has stayed the right of creditors to pre-post compensation, the court retains the discretion to lift the stay having regard to the circumstances."

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[121] It explained the policy reason for this decision by saying at paragraph 75, "allowing pre-post compensation would undermine the effectiveness of the status quo period, would jeopardize the survival of the debtor company or the business it operates and could derail the restructuring process".

[122] If Collins Contracting's counterparts had declared any of the contracts in default, this could undermine the prospect of Collins Contracting's cash flow from these contracts to the extent they seek so-called "pre-pre compensation".

[123] I do not know whether the Surety will continue to provide construction bonding in light of these two defaults. Lack of bonding might compromise Collins Contracting's prospects for new work.

[124] Counsel for the Surety told me that owners have declared other Collins Contracting's contracts in default, but he had no instructions on this point. He said it was unlikely the Surety will continue to offer bonding to Collins Contracting.

[125] Counsel for the Companies advised that I should not accept this evidence as it was hearsay statements from counsel for the Surety. I agree. Surety's counsel said he had no instructions on these points. The Surety did not submit any evidence.

[126] In his September 23, 2022 affidavit, Josh Collins provided me with information about Collins Contracting's bonding facility with Western Surety. Such a bonding facility is essential if Collins Contracting is to bid on any significant provincial contracts. The Surety's counsel told the Court that while a Surety facility is in place, the Surety reserves the right to issue bonds in its sole discretion.

[127] The Surety's support is a critical part of Collins Contracting continuing to work its way out of its financial problems. Josh Collins said in paragraph 26 of his affidavit that in the last 30 days, it has bid $1 million in new construction work. He did not tell me that these contracts required construction bonds.

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[128] Again this is not determinative of whether I will grant the Initial Order, but it represents a significant contingency that Collins Contracting must resolve if it successfully restructures as a going-concern entity.

[129] Thus, the Companies' plan depends on a number of contingencies. The critical ones are:

(a) satisfaction of the Term Sheet conditions precedent, including real estate appraisals supporting Travelers' loan valuation of $6,796,490;

(b) successful efforts to close the Loan Gap;

(c) the consent of RBC to remain as the HASCAP lender subordinate to Travelers and if not, assignment of this debt to another;

(d) resolution of the CRA deemed HST debt and interest and penalties in all of the debt; and

(e) the accuracy of the 17-week cash flow statements provided by the Proposed Monitor.

[130] The Companies' restructuring contingency list is daunting. However, any insolvent debtor who seeks protection under the *CCAA* likely has a similar list.

[131] The Companies seek an Initial Order. That order will expire in 10 days. The Companies have provided more than a "germ of a plan". They presented a plan that, if successful, could present a reasonable possibility of restructuring.

[132] Therefore, the Companies have established that circumstances exist which would allow me to grant the Initial Order. I now turn to whether the Companies' conduct during the Consent Stay cause me to refuse the Initial Order?

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Should the Companies' conduct during the Consent Stay cause me to refuse the Initial Order?

[133] I find that the Companies' conduct during the Consent Stay does not cause me to refuse the Initial Order. I will now explain why I made that decision.

[134] RBC says the Companies' conduct during the Consent Stay is relevant for three reasons:

(a) The first reason is the Companies' late filings show they did not act with due diligence;

(b) The second reason is the Companies' inaction to address its financial problems show they did not act with due diligence; and

(c) The third reason is that the Companies should meet a more onerous standard of whether they have "a germ of a plan" because they had advantage of the Consent Stay Period.

[135] I will first deal with the Companies' late filings.

Did the Companies' late filings show they did not act with due diligence?

[136] I find that the Companies have acted with due diligence to the extent they need to in their application for the Initial Order. I will now explain why I made this decision.

[137] The Saskatchewan Court of Appeal in *Industrial Properties Regina Limited v. Copper Sands Land Corp.*, 2018 SKCA 36 at para. 23 said, "Although it is a consideration for granting an initial order, courts generally defer the in-depth analysis of good faith and due diligence to subsequent applications." It continued

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and said, “If, however, the court determines the debtor corporation is not seeking *CCAA* protection in good faith or there is c*onvincing* evidence of a lack of due diligence, the court may deny an initial order …”. [Emphasis added.]

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[138] Applicants often operate under severe financial pressure when they apply for an Initial Order. They have limited time to prepare their application and information by necessity is usually preliminary. As *CCAA* applications are usually urgent, the court may receive information shortly before the hearing. The timelines are necessarily compressed.

[139] This issue might not have arisen if the Companies had taken its application in September instead of July and made filing shortly before the hearing dates. However, the Court could not schedule the hearing until September 16, 2022, two months after the initial filing.

[140] The parties agreed on the Consent Order. The order included the Consent Stay. Both RBC and the Companies agreed to this in their interest. The Consent Stay likely benefits both the Companies and RBC as it preserves the status quo for both for more than two months. Critically, this is not a stay under the *CCAA*, or under the *BIA*.

[141] In a perfect world, the Companies would have taken advantage of the Consent Stay to improve their plan. However, this likely proved to be impossible because on August 5, 2022, the Companies replaced the Proposed Monitor with Grant Thornton.

[142] This replacement was within their rights. The Proposed Monitor is a critical part of the *CCAA* process. An applicant must have confidence in their monitor. It is not unreasonable for a new monitor to need some time to file a preliminary pre-filing report.

[143] There is no doubt the Companies filed information at the last minute. The Companies did not file their cash flow statements until the Proposed Monitor did so in his first pre-filing report, one day before the hearing. He filed a revision in his second pre-filing report, after the hearing started. Section 10(2) of the *CCAA* requires that these must accompany the application.

[144] The receivership and *CCAA* applications were heard together. RBC's evidence was all filed in the receivership application. A summary of the key filings is set out in this table:

Documents	**Filing Date**
RBC Receivership Application (*BIA*) and supporting Affidavit	July 8, 2022
Companies' initial Application filed and supporting Affidavit	July 18, 2022
Consent Order	July 20, 2022
Companies' termination of S.R. Stack & Company Ltd. as Proposed Monitor	August 5, 2022
Affidavit of David Savoie, RBC (*BIA* proceeding)	August 5, 2022
Companies' Application to replace Proposed Monitor in the Consent Order	August 18, 2022
Affidavit of David Savoie, RBC (*BIA* proceeding)	August 24, 2022
CRA Affidavit	September 12, 2022
Affidavit of Josh Collins	September 13, 2022
Affidavit of Josh Collins	September 15, 2022
Affidavit of David Savoie, RBC (*BIA* proceeding)	September 15, 2022
Proposed Monitor's first pre-filing report	September 15, 2022
Affidavit of Josh Collins	September 23, 2022
Crown's Application	September 23, 2022
Proposed Monitor's second pre-filing report	September 26, 2022

[145] The parties all took advantage of the extra time afforded to them because of the Consent Stay Period, some more than others.

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[146] CRA, a principal creditor of the Companies, filed its documents late in the process. The Province also filed its documents *after* the hearing began.

[147] The Companies filed some information I asked for after the start of the hearing. I asked for further details on the construction contracts and Collins Contracting's construction bonding. Both RBC and I asked for the equipment appraisal. RBC asked for a signed copy of the Term Sheet.

[148] Furthermore, I asked the Proposed Monitor at the end of the first day of the hearing to report to me if he became aware that there was any material change in the circumstances of the Companies' financial situation.

[149] In his second pre-filling report, he altered the cash flow statements because of a termination of a contract. He reported on the proposed use of a newly discovered $500,000 insurance policy payout benefiting Collins Contracting. He was right to do so.

[150] Furthermore, this matter was urgent. No one asked for a postponement. No one said how they might be prejudiced by the delay. Had anyone asked me for one, I would have been reluctant to grant it. Both RBC and the Companies, without a hearing on the merits, obtained the Consent Stay that affected other creditors' rights.

[151] By its nature, *CCAAs* are conducted in, as the Supreme Court of Canada in *Ted Leroy Trucking* at para. 58 states, "the hothouse of real-time litigation". Late filings in these circumstances, although are not condoned, are sometimes inevitable.

[152] The Companies, in particular though, should not assume that I am satisfied with the timing of some of their last-minute filings. The Proposed Monitor and the Companies should not expect similar latitude throughout this process.

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[153] I will now deal whether the Companies' inaction to address their financial problems show they did not act with due diligence.

> *Did the Companies' inaction to address their financial problems show they did not act with due diligence?*

[154] I find it does not. I will now explain why I made this decision.

[155] RBC suggested that I should consider not only the Companies' inaction during the Consent Stay, but before.

[156] This position is inconsistent with the Supreme Court of Canada's guidance in *Callidus*. It suggests at paragraph 51, that the parties must act with due diligence in the *CCAA proceeding*, when it said, "A party's failure to participate in *CCAA* proceedings in a diligent and timely fashion can undermine … the effective functioning of the *CCAA* regime …."

[157] RBC says it asked the Companies to restructure as early as July 2021. RBC says the Companies hired two other consultants to help them with the restructure. They fired them both and hired Grant Thornton about a month and a half ago. RBC says they wasted months before they hired the Proposed Monitor.

[158] The *CCAA* focuses on the go-forward restructuring, not on the past. Someone might speculate that had the Companies taken a series of different actions, they might have avoided their financial difficulty. Perhaps they might have restructured earlier.

[159] I find that speculation about the Companies' actions which led up to its financial difficulties is irrelevant. I will not consider the Companies' failure to take action to restructure before they came to the Court seeking the Initial Order.

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[160] If I were to do so, this would have the effect of denying creditor protection to debtors who are the author of their own misfortune. The *CCAA*, at least for the Initial Order, offers a no-fault remedy, provided that the applicants act in good faith and act with due diligence in the *CCAA* application.

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[161] I will now deal with whether the Companies should meet a more onerous standard of whether they have "a germ of a plan" because they had advantage of the Consent Stay.

> *Should the Companies meet a more onerous standard of whether they have "a germ of a plan" because they had advantage of the Consent Stay?*

[162] I find they should not. I will now explain why I made that decision. However, even if they should have done so, I find that they have.

[163] Justice Orsborn in *Norcon* said at paragraph 17, "The present case is a little different than the usual CCAA initial application. Norcon's Notice of Intention to make a BIA proposal was filed on November 25, 2019, just over two weeks ago."

[164] He continues and said, "In my view, this suggests that restructuring is not a possibility that has just appeared. Although not a lot of time has passed, the fact that the Court is being asked to continue an existing restructuring proceeding suggests that the 'germ' of any plan should exhibit a slightly higher possibility of coming to life than might otherwise be the case."

[165] This may be so, but the Initial Order was not part of any formal restructuring process. There is no court-appointed receiver or monitor to assist the Companies as an intermediary to formulate a restructuring plan.

[166] I find the Consent Stay is not a stay under the *BIA* or the *CCAA*. It is a negotiated order to accommodate the Court schedule. RBC and the Companies negotiated this stay. Presumably, they did so because it was in their mutual advantage to do so.

[167] On the other hand, even if I consider that the *CCAA* application and the request for the Initial Order is a continuation of the restructuring process discussed between RBC and the Companies for over a year, I find it difficult to assess whether the Companies' "plan" exhibits "a slightly higher possibility of coming to life than might otherwise be the case".

[168] I have outlined the challenging contingencies the Companies' face in completing a successful plan. I have no way of knowing if the Companies are more likely to overcome these contingencies than "might otherwise be the case". However, the Companies did more than present "a germ of a plan". I discussed the reason for this earlier in this decision. I now turn to whether the Companies acted in bad faith.

Did the Companies act in bad faith?

[169] Although the Companies referred to RBC's alleged bad faith in their pleadings, affidavits and brief, these allegations relate to RBC's actions leading up to it demanding repayment of the Companies' loans.

[170] While the allegations may be relevant to the receivership application, they have little bearing on the Companies' application for an Initial Order. Furthermore, its counsel said he would not argue that RBC acted in bad faith.

[171] I now turn to RBC's allegation of the Companies' bad faith.

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[172] In argument, RBC's counsel said the Companies acted in bad faith when they failed to report the escalation of the CRA deemed trust debt to RBC and when they failed to comply with the forbearance agreement.

[173] I find that RBC did not properly bring this issue before me. However, even if it had, there is insufficient evidence to establish that the Companies acted in bad faith. I will now explain why I made this decision.

[174] David Savoie says at paragraph 34 of his affidavit, filed August 5, 2022, that RBC did not discover the "substantial" increase in the CRA debt until November 1, 2021. He says that was the first time RBC received any FY 2021 financial statements.

[175] RBC's bad faith allegation perhaps relates to whether the Companies should have told RBC about the increased CRA debt before they revealed it in their financial statements. Perhaps the allegation relates to Collin's Contracting's failure to deliver to RBC the financial statements on time, or perhaps it relates to Collins Contracting's performance of the forbearance agreement.

[176] This imprecision on exactly what good faith obligation the Companies breached is why RBC should have expressly grounded its allegation in its pleadings, affidavits or briefs, and not merely raise the issue in their argument.

[177] The British Columbia Supreme Court dealt with a similar situation in *United Used Auto*. The court said at paragraph 15, "I am also not persuaded by the submissions of the secured lenders that the Petitioners are not acting in good faith. The facts that the Petitioners failed to abide by the terms of the forbearance agreements and that they obtained restructuring advice from Deloitte & Touche Inc. in February 1998 [the court issued its decision in November 1999] does not, in my view, demonstrate a lack of good faith in bringing these proceedings."

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[178] I now turn to whether I should exercise my discretion and grant the administration fee in the Initial Order.

Should the Court exercise its Discretion to grant the administration charge?

[179] I will not grant the administration charge in the Initial Order. I will now explain why I made that decision.

[180] The Companies seek, pursuant to section 11.52(1) of the *CCAA*, a charge on the Companies' property to a maximum amount of $50,000 to secure the Monitor's costs, and his and the Companies' costs for legal, financial and other experts.

[181] I must limit this administration charge to that which is reasonably necessary for the continued operation of the Companies during the initial 10-day stay.

[182] The Companies' cash flow statements show that administration costs and legal fees will be about $45,000 up to the issuance of the Initial Order, and about $20,000 for the two weeks beginning October 15, 2022.

[183] The cash flow statements show a positive cash position without the administration fee for the weeks ending September 30 to October 21, 2022.

[184] In the circumstances, I will not provide for an administration fee in the Initial Order. I will consider this request again at the comeback hearing.

[185] I now turn to what other provisions that were not in the draft order the Companies circulated, I should include in the Initial Order.

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FURTHER ORDERS

[186] Under section 11.02(1) of the *CCAA*, I can make an order on any terms that I may impose.

[187] I first note that the Companies are not asking me to authorize DIP financing in the Initial Order, so I will not do so.

[188] Given some of the information deficiencies I have identified in this decision, on or before the close of business on Thursday, October 13, 2022, the Companies will file:

(a) the FY 2022 financial statements, even if only in interim or draft form; and

(b) a breakdown of the Companies' current contracts, expected revenue, and other information to support the projections in the cash-flow statements provided to the Court in the initial filings. The Companies should disclose if any of the contracts have been declared to be in default.

[189] The Companies and the Monitor shall file an explanation if they cannot provide this information by the deadline. I now turn to the receivership application.

OTHER MATTERS – RECEIVERSHIP APPLICATION

[190] As I have granted the Initial Order, I hereby stay RBC's receivership application.

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OTHER MATTERS - OUTSTANDING MOTION AND APPLICATION

[191] A motion and application remain outstanding.

[192] The first is that the Province asks that I order the Consent Order, or by extension the Initial Order, does not affect the Province's ability to engage the bond, remedy the defaults, and complete the contracts declared in default in the manner directed by the Surety.

[193] Second is that the Companies ask that I hold one of the Companies' contract counterparties in contempt of the Consent Order.

[194] The parties should, at the comeback hearing, be prepared to discuss a process to resolve both matters if I do not set the process before then.

DISPOSITION

[195] I hereby:

(a) grant the Initial Order described in Schedule "A" annexed; and
(b) appoint Grant Thornton Limited to monitor the business and financial affairs of the Companies.

[196] I hereby set the comeback hearing for October 17, 2022, at 10:00 a.m. I make no order as to costs.

ALEXANDER MACDONALD
Justice

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SCHEDULE "A"

2022 01G 1964
IN THE SUPREME COURT OF NEWFOUNDLAND AND LABRADOR
IN BANKRUPTCY AND INSOLVENCY

IN THE MATTER OF the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36, as amended (the "***CCAA***")

AND IN THE MATTER OF an application of Edward Collins Contracting Limited, Classic Security Ltd., FGC Holdings Ltd., 51037 Newfoundland and Labrador Inc. and H & E Designs Ltd. (collectively, "**ECC**" or the "**Company**");

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INITIAL ORDER

Before the Honourable Justice Alexander MacDonald on September 16, 2022, September 28-29, 2022 and October 5, 2022:

THIS APPLICATION made by Edward Collins Contracting Limited, Classic Security Ltd., FGC Holdings Ltd., 51037 Newfoundland and Labrador Inc. and H & E Designs Ltd. (collectively, "**ECC**" or the "**Applicant**") pursuant to the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36, as amended (the "***CCAA***") for an Order substantially in the form filed with the Application was heard on the 16th, 28th and 29th of September, 2022.

ON READING the affidavits of Francis Collins, Josh Collins, David Savoie, Mark Lohnes and the Exhibits attached thereto, the consent of Grant Thornton Limited ("**GTL**") to act as Court-appointed monitor of ECC (in such capacity, the "**Monitor**"), and the Pre-Filing Reports of GTL dated September 13th and September 23rd 2022;

ON HEARING the submissions of counsel for the Company, counsel for the Royal Bank of Canada, and counsel for the Canada Revenue Agency, and such other counsel that were present, no one else appearing for any party although duly served as outlined in the affidavit of service dated the 15th day of July, 2022, and on reading the consent of GTL to act as Monitor:

SERVICE

1. **THIS COURT ORDERS** that the time for service of the Notice of Motion and the Materials filed, as set out in the affidavit of service is hereby deemed adequate notice so that this Application is properly returnable today and hereby dispenses with further service thereof. Further service of Court materials, including the Materials, may be facilitated by the Monitor as prescribed by paragraph 28 below.

APPLICATION

2. **THIS COURT ORDERS AND DECLARES** that Edward Collins Contracting Limited, Classic Security Ltd., FGC Holdings Ltd., 51037 Newfoundland and Labrador Inc. and H & E Designs Ltd. (collectively, "**ECC**" or the "**Company**") is a Company to which the *CCAA* applies.

3. Capital terms not otherwise defined herein shall have the meaning ascribed to them in the within Application.

POSSESSION OF PROPERTY AND OPERATIONS

4. **THIS COURT ORDERS** that the Company shall remain in possession and control of its current and future assets, undertakings and properties of every nature and kind whatsoever, and wherever situate including all proceeds thereof (the **"Property**"). Subject to further Order of this Honourable Court, the Company shall continue to carry on business in a manner consistent with the preservation of its business (the **"Business")** and Property. The Company is authorized and empowered to continue to retain and employ the employees, consultants, independent contractors, agents, experts, accountants, counsel and such other persons (collectively **"Assistants")** currently retained or employed by it, with liberty to retain such further Assistants as it deems reasonably necessary or desirable in the ordinary course of its Business or for the carrying out of the terms of this Order.

5. **THIS COURT ORDERS** that the Company, shall be entitled to continue to utilize its cash management system currently in place, or replace it with another substantially similar cash management system (the **"Cash Management System")** and that any present or future bank providing the Cash Management System shall not be under any obligation whatsoever to inquire into the propriety, validity or legality of any transfer, payment, collection or other action taken under the Cash Management System, or as to the use or application by the Company of funds transferred, paid, collected or otherwise dealt with in the Cash Management System, shall be entitled to provide the Cash Management System without any liability in respect thereof to any Person (as hereinafter defined) other than the Company, pursuant to the terms of the documentation applicable to the Cash Management System, and shall be, in its capacity as provider of the Cash Management System, an unaffected creditor under any plan of compromise or arrangement with regard to any claims or expenses it may suffer or incur in connection with the provision of the Cash Management System.

6. **THIS COURT ORDERS** that the Company shall be entitled but not required to pay the following expenses whether incurred prior to or after this Order:

   (a) all outstanding and future wages, salaries, employee and pension benefits, vacation pay and expenses payable on or after the date of this Order, in each case incurred in the ordinary course of business and consistent with existing compensation policies and arrangements;

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(b) the fees and disbursements of any Assistants retained or employed by the Company in respect of these proceedings, at their standard rates and charges; and

(c) amounts owing for goods and services supplied to the Company, if in the opinion of the Monitor, the supplier or vendor of such goods or services is necessary for the operation and preservation of the Business or Property.

7. **THIS COURT ORDERS** that, except as otherwise provided to the contrary herein the Company shall be entitled but not required to pay all reasonable expenses incurred by the Company in carrying on the Business in the ordinary course after this Order, and in carrying out the provisions of this Order, which expenses shall include, without limitation:

(a) all expenses and capital expenditures reasonably necessary for the preservation of the Property or the Business including, without limitation, payments on account of insurance, maintenance and security services and lease payments for mining equipment used in the operation of the Business; and

(b) payment for goods or services supplied to the Company following the date of this Order.

8. **THIS COURT ORDERS** that the Company shall remit, in accordance with legal requirements, or pay:

(a) any statutory deemed trust amounts in favour of the Crown in right of Canada or of any Province thereof or any other taxation authority which are required to be deducted from employees' wages, including, without limitation, amounts in respect of (i) employment insurance, (ii) Canada Pension Plan, (iii) Quebec Pension Plan, and (iv) income taxes;

(b) all goods and services or other applicable sales taxes (collectively, **"Sales Taxes")** required to be remitted by the Company in connection with the sale of goods and services by the Company, but only where such Sales Taxes are accrued or collected after the date of this Order; and

(c) any amount payable to the Crown in right of Canada or of any Province thereof or any political subdivision thereof or any other taxation authority in respect of municipal realty, municipal business or other taxes, assessments or levies of any nature or kind which are entitled at law to be paid in priority to claims of secured creditors and which are attributable to or in respect of the carrying on of the Business by the Company.

9. **THIS COURT ORDERS** that until a real property lease is disclaimed in accordance with the *CCAA* the Company shall pay all amounts constituting rent or payable as rent under real property leases (including, for greater certainty, common area maintenance charges, utilities and realty taxes and any other amounts payable to the landlord under the lease) or as otherwise may be

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negotiated between the Company and the landlord from time to time (**"Rent"**), for the period commencing from and including the date of this Order. The Monitor, on behalf of the Company, may pay such Rent twice monthly in equal payments on the first and fifteenth day of each month, in advance (but not in arrears). On the date of the first of such payments, any Rent relating to the period commencing from and including the date of this Order shall also be paid.

10. **THIS COURT ORDERS** that, except as specifically permitted herein the Company is hereby directed, until further Order of this Court: (a) to make no payments of principal, interest thereon or otherwise on account of amounts owing by the Company to any of its creditors as of this date; (b) to grant no security interests, trust, liens, charges or encumbrances upon or in respect of any of its Property; and (c) to not grant credit or incur liabilities except in the ordinary course of the Business.

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NO PROCEEDINGS AGAINST THE COMPANY OR THE PROPERTY

11. THIS COURT ORDERS that until and including the 17th day of October, or such later date as this Court may order (the **"Stay Period"**), no proceeding or enforcement process in any court or tribunal (each, a **"Proceeding"**) shall be commenced or continued against or in respect of the Company or the Monitor, or affecting the Business or the Property except with the written consent of the Monitor and the Company, or with leave of this Court, and any and all Proceedings currently under way against or in respect of the Company or affecting the Business or the Property are hereby stayed and suspended pending further Order of this Court.

NO EXERCISE OF RIGHTS OR REMEDIES

12. **THIS COURT ORDERS** that during the Stay Period, all rights and remedies of any individual, firm, corporation, governmental body or agency, or any other entities (all of the foregoing, collectively being **"Persons"** and each being a **"Person"**) against or in respect of the Company or the Monitor, or affecting the Business or the Property are hereby stayed and suspended except with the written consent of the Monitor and the Company, or leave of this Court, provided that nothing in this Order shall (i) empower the Company, to carry on any business which the Company is not lawfully entitled to carry on, (ii) affect such investigations, actions, suits or proceedings by a regulatory body as are permitted by Section 11.1 of the *CCAA*, (iii) prevent the filing of any registration to preserve or perfect a security interest, or (iv) prevent the registration of a claim for lien.

NO INTERFERENCE WITH RIGHTS

13. **THIS COURT ORDERS** that during the Stay Period, no Person shall discontinue, fail to honour, alter, interfere with, repudiate, terminate or cease to perform any right, renewal right, contract, agreement, licence or permit in favour of or held by the Company, except with the written consent of the Monitor and the Company, or leave of this Court.

CONTINUATION OF SERVICES

14. **THIS COURT ORDERS** that during the Stay Period, all Persons having oral or written agreements with the Company or statutory or regulatory mandates for the supply of goods and/or services, including without limitation all computer software, communication and other data services, centralized banking services, payroll services, insurance, transportation services, utility or other services to the Business or the Company, are hereby restrained until further Order of this Court from discontinuing, altering, interfering with or terminating the supply of such goods or services as may be required by the Company, and the Company shall be entitled to the continued use of its current premises, telephone numbers, facsimile numbers, internet addresses and domain names, provided in each case that the normal prices or charges for all such goods or services received after the date of this Order are paid the Company in accordance with normal payment practices of the Company or such other practices as may be agreed upon by the supplier or service provider and the Company or as may be ordered by this Court.

NON-DEROGATION OF RIGHTS

15. **THIS COURT ORDERS** that, notwithstanding anything else in this Order, no Person shall be prohibited from requiring immediate payment for goods, services, use of lease or licensed property or other valuable consideration provided on or after the date of this Order, nor shall any Person be under any obligation on or after the date of this Order to advance or re-advance any monies or otherwise extend any credit to the Company. Nothing in this Order shall derogate from the rights conferred and obligations imposed by the *CCAA*.

APPOINTMENT OF MONITOR

16. **THIS COURT ORDERS** that Grant Thornton Limited is hereby appointed pursuant to the *CCAA* as the Monitor, an officer of this Court, to monitor the business and financial affairs of the Company with the powers and obligations set out in the *CCAA* or set forth herein and that the Company and its shareholders, officers, directors, and Assistants shall advise the Monitor of all material steps taken by the Company pursuant to this Order, and shall co-operate fully with the Monitor in the exercise of its powers and discharge of its obligations and provide the Monitor with the assistance that is necessary to enable the Monitor to adequately carry out the Monitor's functions.

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17. **THIS COURT ORDERS** that the Monitor, in addition to its prescribed rights and obligations under the *CCAA*, is hereby directed and empowered to:

(a) monitor the Company's receipts and disbursements;

(b) report to this Court at such times and intervals as the Monitor may deem appropriate with respect to matters relating to the Property, the Business, and such other matters as may be relevant to the proceedings herein;

(c) assist the Company in its dissemination of reports and other information to the Secured Creditors (as defined herein) and their respective counsel;

(d) advise, in consultation with the Company, the preparation of the Company's cash flow statements and reporting;

(e) have full and complete access to the Property, including the premises, books, records, data, including data in electronic form, and other financial documents of the Company, to the extent that is necessary to adequately assess the Company's business, cashflow, and financial affairs or to perform its duties arising under this Order;

(f) be at liberty to engage with Company legal counsel or retain independent legal counsel or such other persons as the Monitor deems necessary or advisable respecting the exercise of its powers and performance of its obligations under this Order; and

(g) perform such other duties as are required by this Order or by this Court from time to time.

18. **THIS COURT ORDERS** that the Monitor shall not take possession of the Property and shall not, by fulfilling its obligations hereunder, be deemed to have taken or maintained possession or control of the Business or be considered management of the Business, or any part thereof.

19. **THIS COURT ORDERS** that nothing herein contained shall require the Monitor to occupy or to take control, care, charge, possession or management (separately and/or collectively, **"Possession"**) of any of the Property that might be environmentally contaminated, might be a pollutant or a contaminant, or might cause or contribute to a spill, discharge, release or deposit of a substance contrary to any federal, provincial or other law respecting the protection, conservation, enhancement, remediation or rehabilitation of the environment or relating to the disposal of waste or other contamination including, without limitation, the *Canadian Environmental Protection Act* and regulations thereunder (the **"Environmental Legislation"),** provided however that nothing herein shall exempt the Monitor from any duty to report or make disclosure imposed by applicable Environmental Legislation. The Monitor shall not, as a result of this Order or anything done in pursuance of the Monitor's duties and powers under this Order, be deemed to be in Possession of any of the Property within the meaning of any Environmental Legislation, unless it is actually in possession.

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20. **THIS COURT ORDERS** that the Monitor shall provide any creditor of the Company with information provided by the Company in response to reasonable requests for information made in writing by such creditor addressed to the Monitor. The Monitor shall not have any responsibility or liability with respect to the information disseminated by it pursuant to this paragraph. In the case of information that the Monitor has been advised by the Company is confidential, the Monitor shall not provide such information to creditors unless otherwise directed by this Court or on such terms as the Monitor and the Company may agree.

21. **THIS COURT ORDERS** that, in addition to the rights and protections afforded the Monitor under the *CCAA* or as an officer of this Court, the Monitor shall incur no liability or obligation as a result of its appointment or the carrying out of the provisions of this Order, save and except for any gross negligence or willful misconduct on its part. Nothing in this Order shall derogate from the protections afforded the Monitor by the *CCAA* or any applicable legislation.

22. **THIS COURT ORDERS** that the Monitor, counsel to the Monitor, and counsel to the Company shall be paid their reasonable fees and disbursements, in each case at their standard rates and charges, by the Company as part of the costs of these proceedings. The Company is hereby authorized and directed to pay the accounts of the Monitor, counsel for the Monitor, and counsel for the Company on a weekly basis and, in addition, the Company is hereby authorized to pay to the Monitor, counsel to the Monitor, and counsel to the Company reasonable retainers to be held by them as security for payment of their respective fees and disbursements outstanding from time to time.

23. **THIS COURT ORDERS** that the Monitor and its legal counsel shall pass their accounts from time to time, and for this purpose, the accounts of the Monitor and its legal counsel are hereby referred to a judge of the Supreme Court of Newfoundland and Labrador in Bankruptcy and Insolvency.

DUTY TO PROVIDE ACCESS AND CO-OPERATION TO THE MONITOR

24. **THIS COURT ORDERS** that the Company and all its current and former directors, officers, employees, agents, accountants, legal counsel and shareholders, and all other persons acting on their instructions or behalf shall fully co-operate with the Monitor in the exercise its powers under this Order or any other Order of the Court, including by:

    (a) advising the Monitor of the existence of any Property of which such party has knowledge of;

    (b) providing the Monitor with immediate and continued access to any Property in such party's possession or control;

    (c) advising the Monitor of the existence of any books, documents, securities, contracts, orders, corporate and accounting records, and any other papers, records and information of any kind related to the business or affairs of the

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Company, and any computer programs, computer tapes, computer disks, or other data storage media containing any such information **("Records")** of which such party has knowledge of; and

(d) providing access to and use of the Records, including any accounting, computer, software and physical facilities relating thereto, and including providing the Monitor with instructions on the use of any computer or other system as requested by the Monitor and providing the Monitor with any and all access codes, account names and account numbers that may be required to gain access to the Records, provided however that nothing in this Order shall require the delivery of Records, or the granting of access to Records, which may not be disclosed or provided to the Monitor due to the privilege attaching to solicitor-client communication or due to statutory provisions prohibiting such disclosure.

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LIMITATION ON THE MONITOR'S LIABILITY

25. **THIS COURT ORDERS THAT** the Monitor is not and shall not, for any purposes, be deemed to be a director, officer, employee, receiver, receiver-manager, or liquidator of the Company.

26. **THIS COURT ORDERS THAT** the Monitor is not and shall not for the purposes of the *Income Tax Act*, R.S.C., 1985, c. 1 (5th Supp.) be deemed to be a legal representative or person to whom s. 150(3) of that Act applies.

27. **THIS COURT ORDERS THAT** that the rights, protections, indemnities, charges, priorities and other provisions in favour of the Monitor set out in the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36, any other applicable legislation, and any other Order granted in these proceedings, all shall apply and extend to the Monitor in connection with the Monitor carrying out the provisions of this Order, amended as necessary to give effect to the terms of this Order.

SERVICE AND NOTICE

28. **THIS COURT ORDERS** that the Monitor shall (A) make this Order publicly available in the manner prescribed under the *CCAA*, (B) send, in the prescribed manner by electronic means, a notice to every known creditor who has a claim against the Company of more than $1,000, and (C) prepare a list showing the names and addresses of those creditors and the estimated amounts of those claims, and make it publicly available in the prescribed manner, all in accordance with Section 23(1)(a) of the *CCAA* and the regulations made thereunder.

GENERAL

29. **THIS COURT ORDERS** that the Monitor, on behalf of the Company, may from time to time apply to this Court for advice and directions in the discharge of its powers and duties hereunder.

30. **THIS COURT ORDERS** that nothing in this Order shall prevent the Monitor from subsequently acting as an interim receiver, a receiver, a receiver and manager, or a trustee in bankruptcy of the Company, the Business or the Property.

31. **THIS COURT ORDERS** that each of the Company and the Monitor be at liberty and is hereby authorized and empowered to apply to any court, tribunal, regulatory or administrative body, wherever located, for the recognition of this Order and for assistance in carrying out the terms of this Order, and that the Monitor is authorized and empowered to act as a representative in respect of the within proceedings for the purpose of having these proceedings recognized in a jurisdiction outside Canada.

32. **THIS COURT ORDERS** that a hearing for the balance of the relief sought by the Company in the Notice of Motion is hereby scheduled before this Court for the 17th day of October, 2022 at 10:00 a.m. or such other date as determined by this Court (the "**Comeback Hearing**").

33. **THIS COURT ORDERS** that on or before the close of business on Thursday, October 13, 2022, the Company shall provide the Court and each creditor referred to in paragraph 28 above, in the manner of service provided for in paragraph 28 above, with the following information: (the Company and the Monitor shall file an explanation if they cannot provide this information by the deadline):

    (a) a detailed breakdown of the companies' current contracts, expected revenue, and other information to support the projections in the cash-flow statements provided to the Court on the initial filing. The Company should disclose if any of the contracts have been declared to be in default; and

    (b) the FY 2022 financial statements, even if only in draft or interim form and any other information this Honourable Court may request.

ISSUED at St. John's, Newfoundland and Labrador this 5th day of October, 2022.

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IN THE SUPREME COURT OF BRITISH COLUMBIA

Citation: *1057863 B.C. Ltd. (Re),*
2020 BCSC 1359

Date: 20200914
Docket: S206189
Registry: Vancouver

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

and

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

and

In the Matter of a Plan of Compromise or Arrangement of 1057863 B.C. Ltd., Northern Resources Nova Scotia Corporation, Northern Pulp Nova Scotia Corporation, Northern Timber Nova Scotia Corporation, 3253527 Nova Scotia Limited, 3243722 Nova Scotia Limited and Northern Pulp NS GP ULC

Petitioners

Before: The Honourable Madam Justice Fitzpatrick

Reasons for Judgment

Counsel for the Petitioners:	S. Collins W.W. MacLeod J. Roberts
Counsel for Province of Nova Scotia:	R.G. Grant, Q.C. M.P. Chiasson, Q.C.
Counsel for Paper Excellence Canada Holdings Corporation:	P.J. Reardon
Counsel for the Monitor, Ernst & Young Inc.:	E. Pillon L. Nicholson

Counsel for Unifor, Local 440:	R.A. Pink, QC
Counsel Pacific Harbor North American Resources Ltd, as the proposed interim lender:	B. Brammall
Counsel for Atlas Holdings LLC and Blue Wolf Capital Management, LLC:	N. MacParland
Counsel for Envirosystems Inc., dba Terrapure Environmental:	H. P. Whiteley
Counsel for Pictou Landing First Nation:	B. Hebert
Counsel for Nova Scotia Superintendent of Pensions:	S. Choo
Place and Date of Hearing:	Vancouver, B.C. July 31 and August 5, 2020
Place and Date of Ruling with Written Reasons to Follow:	Vancouver, B.C. August 6, 2020
Place and Date of Written Reasons:	Vancouver, B.C. September 14, 2020

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INTRODUCTION

[1] On June 17, 2020, the petitioners filed these proceedings seeking a restructuring solution to their financial problems, pursuant to the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36 (the "*CCAA*").

[2] The petitioner, 1057863 B.C. Ltd., a British Columbia company, is the parent company of the other petitioners. The corporate group also includes various limited partnerships that are not named petitioners. Together, the group operates a pulp mill in Pictou County, Nova Scotia (the "Pulp Mill"). They also conduct related forestry activities in the Province of Nova Scotia to support those operations. I will refer to the group collectively as the "Petitioners".

[3] On January 31, 2020, the Petitioners were required to shut down the Pulp Mill, resulting in a complete cessation of its business activities. At the centre of the reasons for the shut down is an Effluent Treatment Facility ("ETF") that became inoperable after that date. The ETF is source of considerable controversy with certain of the stakeholders.

[4] Without the ability to use the ETF, the Pulp Mill could not operate.

[5] The Petitioners describe that the shut down of the Pulp Mill had a "devastating effect" on them and their partners. Indeed, most employees were laid off after the shut down.

[6] On June 19, 2020, the Petitioners sought and the Court granted an initial order under the *CCAA* (the "Initial Order"). The Petitioners' stated intention at that time was to continue to ensure the orderly hibernation, care and maintenance of the Pulp Mill while they investigated and assessed various restructuring options. The Initial Order granted was what is colloquially termed a "skinny" order, particularly in light of new strictures under s. 11.001 of the *CCAA* that limit the initial relief to what is reasonably necessary during the initial stay period.

[7] In the Initial Order, I appointed Ernst & Young Inc. as Monitor. I granted a Director's Charge limited to $500,000. I extended the stay of proceedings to the limited partnerships, as appropriate in these circumstances: *4519922 Canada Inc. (Re)*, 2015 ONSC 124 at para. 37. Finally, I granted an Administration Charge of $500,000. At the time of the initial hearing, the Petitioners indicated that it was their intention to come back to the Court to seek approval of interim financing and other relief, including approval of a Key Employee Retention Plan ("KERP") and authority to pay certain pre-filing amounts.

[8] Since June 19, 2020, I have extended the stay a number of times to allow further discussions between the Petitioners and their stakeholders toward a possible resolution, including with the Province of Nova Scotia ("Nova Scotia"), their major secured creditor. The Monitor supported those extensions, as set out in its first report to the Court dated July 2, 2020 (the "First Report").

[9] Unfortunately, considerable disagreement remains as to whether this proceeding should continue and if so, on what terms.

[10] This hearing was essentially the comeback hearing. The Petitioners sought an Amended and Restated Initial Order ("ARIO") to incorporate the original relief in the Initial Order, with some amendments; significantly, they sought approval for interim financing that would allow their restructuring activities to continue.

[11] On August 6, 2020, I granted an ARIO that incorporated much of the relief sought. In addition, I granted the order sought by Unifor, Local 440 ("Unifor") for representative status in this proceeding. These reasons follow from my decisions at that time.

BACKGROUND

[12] The Pulp Mill has a considerable history leading to the current and fraught relationship between the owners of the Pulp Mill and other stakeholders, being Nova Scotia in particular. I will only provide a very high-level description of that history as is relevant to this application.

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[13] The Pulp Mill has been in operation since 1967. It is located on Abercrombie Point in Pictou County, NS. The process of producing pulp at the Pulp Mill creates wastewater, and it is necessary to treat that wastewater before discharge. Since 1972, the treatment of the wastewater was done at the ETF, which is located near "Boat Harbour". Nova Scotia owns the ETF and has leased it to the Pulp Mill's owners over the years. As stated, the Pulp Mill cannot operate without treating the wastewater at the ETF.

[14] The Pulp Mill is adjacent to reserve lands of the Pictou Landing First Nation ("PLFN"), a Mi'kmaq First Nation.

[15] In 2011, Paper Excellence Canada Holdings Corporation ("PEC") directly or indirectly acquired ownership of the Petitioners. PEC describes having spent more than $118 million in respect of the operations of the Pulp Mill and related activities.

[16] Events leading to the Petitioners' financial difficulties include:

a) In 2014, there was an effluent leak in the pipeline from the Pulp Mill to the ETF; that event led to PLFN members blockading the area;

b) In 2015, Nova Scotia passed the *Boat Harbour Act*, S.N.S. 2015, c. 4 (the "*BHAct*"). The *BHAct* required the Petitioners cease using the ETF for the reception and treatment of effluent from the Pulp Mill by January 31, 2020. The deadline set in this legislation was contrary to the terms of the lease between Nova Scotia and the Pulp Mill (entered into prior to PEC's involvement) that contemplated use of the ETF until December 31, 2030;

c) The Petitioners set about planning for a replacement ETF ("RETF") that would allow the Pulp Mill's operations to continue past January 2020. The Petitioners have spent considerable monies to advance the project, with financial and other contributions by Nova Scotia;

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d) The Petitioners' efforts to establish the RETF involved, understandably, considerable input and agreement from Nova Scotia under its environmental and regulatory process and requirements;

e) The RETF approval process did not go smoothly, at least from the Petitioners' point of view. In part, the process took place in the face of litigation between Nova Scotia and PLFN relating to Nova Scotia's decisions in relation to the Petitioners and the Pulp Mill;

f) The Petitioners say that they told Nova Scotia that it was not possible to complete the RETF by January 2020. Nova Scotia says that they never gave the Petitioners any inkling that a possible extension would be afforded to them;

g) Matters came to a head somewhat in late December 2019. Nova Scotia's Minister of Environment ("MOE") determined that a further environmental assessment report ("EAR") was required for the RETF. Almost immediately thereafter, Nova Scotia gave formal notice to the Petitioners that no extension under the *BHAct* was forthcoming;

h) In January 2020, the Petitioners filed a judicial review proceeding challenging the MOE's requirement to file a further EAR (the "Judicial Review");

i) The Pulp Mill ceased operations on January 12, 2020;

j) Commencing January 29, 2020, the MOE issued various orders to the Petitioners in respect of the orderly shutdown of the Pulp Mill. The MOE's May 14, 2020 order was appealed to the Supreme Court of Nova Scotia (the "Appeal"); and

k) The Petitioners have clearly signalled to Nova Scotia that they are seeking financial redress from the Province arising from the passage and implementation of the *BHAct* (the "BH Claim"). As matters stand,

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> the Judicial Review and Appeal are in abeyance, along with the Petitioners' consideration of the BH Claim against Nova Scotia.

[17] The primary debt owed by the Petitioners is to PEC and Nova Scotia. The Petitioners owe PEC approximately $213 million; $30 million of that amount is secured against the Petitioners' assets. The Petitioners owe Nova Scotia approximately $85 million, which has a first ranking secured position against the assets. The Petitioners also owe Nova Scotia $1.3 million on an unsecured basis.

[18] In addition to unsecured amounts owed to PEC, Nova Scotia and employees, the Petitioners owe approximately $4.3 million to trade creditors and owners of the timberlands that they harvested.

[19] Before the shutdown of the Pulp Mill, the Petitioners employed approximately 200 unionized persons, represented by Unifor. In addition, there were approximately 135 other full-time employees, including salaried personnel. The Petitioners also retained approximately 600 contractors on a full or part-time basis.

[20] As of June 2020, approximately 32 employees and 18 seasonal part-time employees remained. The rest of the employees were laid off or terminated.

[21] Considered more broadly, the impact of the shutdown of the Pulp Mill has had far-reaching and considerable negative consequences for the stakeholders.

[22] The Monitor confirms in the First Report that the Petitioners contributed more than $279 million annually to the Nova Scotia economy, arising from purchases of goods and services. The Petitioners maintained a supply chain of approximately 1,379 companies who supported the operations of the Pulp Mill. Finally, the Pulp Mill provided employment for an estimated 2,679 full-time equivalent jobs, generating an estimated $38 million annually in provincial and federal taxes.

INTERIM FINANCING

[23] The Petitioners seek court approval of an interim financing term sheet (the "Term Sheet") for a financing facility (the "Interim Lending Facility") between the

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Petitioners, as borrowers, PEC, as arranger and agent, and PEC together with Pacific Harbor North American Resources Ltd., as lenders (collectively, the "Interim Lenders").

[24] The Interim Lending Facility contemplates a maximum principal amount of $50 million. However, the Petitioners presently only seek approval of an initial advance of $15 million and a corresponding charge in favour of the Interim Lenders over the Petitioners' assets in first ranking priority (the "Interim Financing Charge"). The stated purpose for these initial funds is to allow payment of the Petitioners' expenses to December 2020. If the Term Sheet is approved, the Petitioners intend to make later applications for court approval to access further draws.

[25] In support of their request, the Petitioners prepared a budget to detail the uses of the $50 million (the "Financing Budget"). The Financing Budget indicates the projected financing requirements of the Petitioners to June 2022. As stated by Bruce Chapman, the general manager of the Petitioners and PEC, those projections were based on a "successful outcome" of these proceedings, said to include: the successful shutdown of the ETF; hibernation of the Pulp Mill; identifying, designing, and obtaining approvals for the RETF; and, negotiating contributions and financing associated with those activities.

[26] After the Petitioners' introduced the Financing Budget as part of this application, Nova Scotia raised a variety of objections. Nova Scotia's response at para. 2, filed in opposition to the application, sets out those objections:

> (a) there is no restructuring plan being pursued by the Applicants;
>
> (b) the DIP financing will be used to fund the Applicants' pre-filing obligations;
>
> (c) the DIP financing will be an inappropriate re-prioritization of security;
>
> (d) the cash flow statements are not supported by appropriate documentation; and
>
> (e) the Applicants have not engaged the Province in any meaningful way, other than to continue to pursue their agenda for obtaining the DIP financing to fund existing obligations.

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[27] The Monitor has brought considerable balance and objectivity forward in terms of assisting the stakeholders in understanding the Financing Budget. In particular, the Monitor has sought to address Nova Scotia's concerns in the face of significant disputes between the Petitioners and Nova Scotia.

[28] In the Monitor's second report dated July 23, 2020 (the "Second Report"), the Monitor introduced the concept of milestones. The milestones set out categories of work or activities required to move the overall restructuring toward the anticipated "success" date of June 2022. Target Completion Dates are identified in the "Milestones Schedule" at Appendix C to the Second Report, along with Evaluation Dates and the Cumulative DIP Draw required by the respective dates. This "Milestones Schedule" provides, in my view, considerable structure to the approval process and it will allow, in the future, the Court, the Monitor and the stakeholders (particularly Nova Scotia) to gauge the ongoing progress of the Petitioners' efforts.

[29] In addition, the Monitor assisted in the development of an interim budget to December 2020 (the "Interim Budget"). That document, discussed in the Monitor's Second Report and its Supplemental Report dated July 30, 2020, provides a detailed breakdown of the activities and the estimated cost of those activities under the initial draw of $15 million. Those activities and costs are:

Activity	**Activity Costs**
Boat Harbour operations and de-commissioning costs and environmental costs	$6,846,698
Mill operating costs	$1,231,650
Financing and administration costs	$407,734
Employee costs	$1,161,104
Severance and salary continuations	$2,646,498
Professional fees (includes approx. $575,000 for the Judicial Review and Appeal)	$3,481,625
TOTAL	**$15,775,308**

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[30] The Monitor anticipates that, with cash on hand of approximately $4.8 million, the Petitioners will have sufficient funding through to the end of 2020 with this interim financing.

[31] Section 11.2(1) and (2) of the *CCAA* confirms the Court's jurisdiction to approve interim financing and approve a charge in priority to existing secured creditors:

> (1) On application by a debtor company and on notice to the secured creditors who are likely to be affected by the security or charge, a court may make an order declaring that all or part of the company's property is subject to a security or charge – in an amount that the court considers appropriate – in favour of a person specified in the order who agrees to lend the company an amount approved by the court as being required by the company, having regard to its cash-flow statement. The security or charge may not secure an obligation that exists before the order is made.
>
> (2) The court may order that the security or charge rank in priority over the claim of any secured creditor of the company.

[32] The Supreme Court of Canada recently commented on the importance of the relief available under s. 11.2, including the granting of an interim lenders' charge. In *9354-9186 Québec inc. v. Callidus Capital Corp.*, 2020 SCC 10 at para. 85-86, the Court confirmed that a court may exercise its discretion to approve such financing to achieve the important statutory objective under the *CCAA* of not only providing working capital, but also enabling the "preservation and realization of the value of a debtor's assets".

[33] The Court in *Callidus* also acknowledged that a court's ability to grant a charge in favour of an interim financier is often necessarily and practically the only way to secure this benefit:

> [89] Such charges, also known as "priming liens", reduce lenders' risks, thereby incentivizing them to assist insolvent companies. As a practical matter, these charges are often the only way to encourage this lending. Normally, a lender protects itself against lending risk by taking a security interest in the borrower's assets. However, debtor companies under *CCAA* protection will often have pledged all or substantially all of their assets to other creditors. Accordingly, without the benefit of a super-priority charge, an interim financing lender would rank behind those other creditors. Although super-priority charges do subordinate secured creditors' security positions to

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> the interim financing lender's — a result that was controversial at common law — Parliament has indicated its general acceptance of the trade-offs associated with these charges by enacting s. 11.2(2) [citations omitted].

[34] Section 11.2(4) of the *CCAA* sets out certain non-exhaustive factors to be considered by the court in deciding whether to approve interim financing and grant an interim lenders' charge:

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

[35] No one factor set out in s. 11.2(4) governs or limits the Court's consideration. The exercise is necessarily one of balancing the respective interests of the debtors and its stakeholders towards ensuring, if appropriate, that the financing will assist the debtor company to obtain the "breathing room" said to be needed to hopefully achieve a restructuring acceptable to the creditors and the court: *White Birch Paper Holding Co. (Re)*, 2010 QCCS 1176, at para. 33 and *Pacific Shores Resort & Spa Ltd. (Re)*, 2011 BCSC 1775 at para. 49.

[36] I will discuss the factors in turn.

[37] These proceedings were filed in mid-June 2020. Despite the Petitioners' initial intentions to undertake a restructuring process to mid-2022 under the Interim Lending Facility, their ambitions have been significantly curtailed, at least in the short term. Under the present proposal, the Petitioners seek only to extend these proceedings to December 2020, when hopefully there will be further clarity about how the restructuring may proceed. This shortened period will allow the Court, the

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Monitor and the stakeholders to get a sense of the Petitioners' progress toward assessing whether any further extension of the proceedings is justified.

[38] Nova Scotia submitted that, if the Court approved the interim financing and extended the stay, that stay period should only be to October 2020, when the Court could assess matters then.

[39] I would not accede to this submission. There is considerable cost and energy to bring matters forward to the Court, which may not necessarily be justified depending on the status of matters in October 2020. Rather, I accept that the financing is justified in order to allow further operations to December 2020. I have specifically ordered the Monitor to provide oversight with respect to the Petitioners' expenditures to ensure that they are consistent with the Interim Budget. In addition, I ordered that the Monitor file a formal report with the Court by no later than October 31, 2020 as to the status of the Petitioners' restructuring efforts and spending under the Interim Budget. That information will of course be available to the stakeholders. If anything arises from that report, the Monitor or any stakeholder may apply to the Court.

[40] Nova Scotia has raised, however obliquely, concerns regarding how the Petitioners' business and financial affairs will be managed during the proceedings. In my view, this largely arises from the great degree of mistrust and suspicion, if not downright animosity, that exists in the chasm that separates Nova Scotia and the Petitioners.

[41] Nova Scotia filed various affidavits in support of its opposition to this application, being those of Duff MacKay Montgomerie, Paul Bradley and Kenneth Swain. All of these affidavits were intended to provide Nova Scotia's side of the "story" and respond to Mr. Chapman's various affidavits. Mr. Chapman replied to the points raised in Nova Scotia's affidavits.

[42] Clearly, the disagreements between the Petitioners and Nova Scotia are many, and some long-standing. Two major issues relate to (a) payments made by

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the Petitioners to PEC as a shareholder some years ago when monies were owed to Nova Scotia, and (b) the use of monies advanced by Nova Scotia to the Petitioners for environmental expenses under a Contribution Agreement. I only note the existence of those disputes; in my view, there is no need at this time and in these proceedings to resolve those disputes. Whether those disputes need to be resolved in the fullness of time remains to be seen.

[43] I accept that Nova Scotia's concerns give rise to some question as to the future conduct of these proceedings. However, this question is largely answered by the Monitor, who raises no concerns regarding the conduct of the Petitioners' management from the time of the Initial Order. As stated in *Pacific Shores* at para. 31, the good faith requirement to support the relief on this application relates to conduct within the proceeding, not conduct pre-existing the filing. The Monitor continues to provide oversight with respect to the Petitioners' activities.

[44] One of the major factors is whether the loan would enhance the prospect of the Petitioners making a viable compromise or arrangement with their creditors.

[45] The result of not approving this financing is stark. The shutdown of the Pulp Mill has resulted in a complete cessation of any revenue. Both Mr. Chapman and the Monitor confirm that, without the financing, the Petitioners cannot continue any restructuring efforts or even the continued hibernation of the Pulp Mill. The Monitor confirms that a lack of funding would likely result in a receivership or bankruptcy, with the usual dire result of yielding nothing for the majority of the stakeholders.

[46] A large portion of the $15 million interim financing is earmarked for what Mr. Chapman calls "critical expenses" relating to the direct and indirect expenses of the hibernation of the Pulp Mill. In its opposition, Nova Scotia does not address what would happen in the event that PEC walked away from its investment in the Petitioners and the Pulp Mill. As best I can tell, Nova Scotia seems to be ready to test PEC's resolve to determine if PEC will, as the shareholder, fund the ongoing costs itself without any interim financing and related charge.

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[47] In my view, given the sensitive nature of the assets, and the potential and negative consequences particular to the environment and local population arising on a liquidation, I do not consider it is reasonable to allow a "game of chicken" to take place between Nova Scotia and PEC. It appears to be the case that even if a receivership takes place (perhaps at the behest of Nova Scotia), many of these costs would be incurred in any event: *Pacific Shores* at para. 49(f).

[48] Nova Scotia also takes issue with payment of pre-filing unsecured amounts, including amounts owed to employees and former employees, which the Petitioners seek to fund under the Financing Budget and the Interim Budget. I will address that issue separately below.

[49] Finally, Nova Scotia takes great umbrage in having an Interim Financing Charge placed ahead of its own charge when some of the funds under the Financing and Interim Budgets are to be used to some extent to advance litigation (or potential litigation) against it. Paragraph 10 of the Term Sheet provides that the purpose of the facility is in part to fund expenses associated with:

> … the evaluation, settlement or progression of claims and other legal remedies that may be available to the Borrowers and to pay transaction costs, fees and expenses [including all reasonable fees and expenses in connection with any other proceeding pursued or defended by the Borrowers relating to the Northern Pulp facility and business] …

[50] It is common ground that the "claims and other legal remedies" include the Judicial Review, the Appeal and the potential BH Claim against Nova Scotia. The estimated cost in the Interim Budget of professional fees toward those matters is approximately $575,000. Nova Scotia questions whether the Interim Financing Facility is simply to improve the Petitioners' negotiating position with Nova Scotia.

[51] The Petitioners state that they remain committed to pursuing the re-start of the Pulp Mill in an environmentally responsible manner by ultimately constructing the RETF and resuming operations. The Petitioners believe that a re-start of operations affords Nova Scotia the best opportunity to recover its secured claims for money

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advanced. Nova Scotia disagrees and appears to have considered the consequences of a complete and permanent shutdown of the Pulp Mill.

[52] The Petitioners say that they have continued the litigation – and are still considering the BH Claim – against Nova Scotia only as a backstop if they are not able to resolve their outstanding claims against Nova Scotia through negotiation and settlement. As noted by the Petitioners' counsel, the rights of the Petitioners under the Judicial Review, the Appeal and the BH Claim are choses in action and part of the Petitioners' assets. In *Callidus* at para. 96, the Court recognized that funding to preserve a "litigation asset" may be appropriate if it is intended to preserve and realize upon that asset for the benefit of the stakeholders.

[53] In my view, in the overall context, the limited amount of litigation funding proposed to be spent between now and December 2020 is justified in these circumstances. If the proceedings are extended beyond that date, and further funding for that purpose is requested, the Court may revisit the matter.

[54] Another factor is the nature and value of the Petitioners' property. The Monitor sets out in the First Report that the 2019 unaudited consolidated assets of the Petitioners (at book value) was approximately $343 million. The estimated liabilities as of mid-June 2020 were approximately $311 million. By any measure, most of the value of the Petitioners' assets, particularly the Pulp Mill, will only be realized if the Pulp Mill begins operations again. That necessarily involves the establishment of the RETF.

[55] The Interim Financing Facility, as limited by the initial draw under the Interim Budget, will allow the Petitioners a short period (some five months) to show real progress toward that objective of enhancing the value of their assets. I do not agree with Nova Scotia that the Petitioners have failed to identify any restructuring plan or that the Interim Financing Facility *is* the plan. The materials before the Court clearly show a "kernel of a plan" – namely the restart of the Pulp Mill and the Petitioners' operations, all intended to alleviate the dire financial circumstances here and allow the Petitioners to fashion a way forward with the support of their creditors. The

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Petitioners should be allowed some opportunity to advance their efforts to that end, if possible.

[56] Another significant factor here is whether any creditor would be materially prejudiced if the Interim Financing Charge is granted. Clearly, Nova Scotia, as the major and presently first ranking secured creditor thinks so. It is not difficult to discern that Nova Scotia faces a myriad of concerns with respect to the Petitioners and the Pulp Mill, including relating to the environment, employment of its citizens, the general welfare of the employees, obligations to the PLFN and the state of its economy.

[57] It is not my role on this application to judge how Nova Scotia has seen fit to balance its duties and obligations in this complex situation. Nova Scotia is clearly frustrated with the Petitioners, noting in particular that it has already contributed significant amounts of public money and other benefits to assist them in meeting their environmental obligations.

[58] I agree that Nova Scotia faces prejudice, although not to the degree submitted by its counsel. As stated above, it remains the case that, if a receivership occurs, a receiver would incur some of these expenses anyway. This is particularly so, with respect to the expenses (both direct and indirect) intended to protect the environment and the citizens of Pictou County in the Pulp Mill hibernation process.

[59] I have no concerns that Nova Scotia is anything but committed to the well-being of the environment and its citizens, particularly those living near the Pulp Mill, such as members of the PLFN. I acknowledge Nova Scotia's concerns, but they must be balanced against other stakeholder interests and prejudice faced by those stakeholders if the financing is not approved: *Pacific Shores* at para. 49.

[60] The final factor is whether the monitor supports the financing. That is clearly the case here. As stated above, the Monitor has attempt to bridge the gap between Nova Scotia's concerns and the objectives of the Petitioners. It has succeeded to some degree.

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[61] The Monitor has carefully analyzed the proposed financing terms. In its various reports, the Monitor has provided a detailed summary of the key elements of the Term Sheet, including specific terms that Nova Scotia questioned (including those provisions relating to payment-in-kind terms, change of control, right of first refusal and right to match, a prohibition on voluntary provisions and certain default terms). In light of submissions made by the Petitioners, and comments of the Monitor, I have no concerns regarding those matters.

[62] Nova Scotia also raised an issue with respect to possible action by the Interim Lenders if there is an Event of Default (para. 23 of the Term Sheet). Again, I had no concerns in that respect as those were normal terms. I ordered an amendment to the draft ARIO to ensure that it was consistent with the provisions in the Term Sheet.

[63] The Monitor recommends approval of the Interim Financing Facility, limited to the initial draw under the Interim Budget. I expect that the Monitor will work closely with the Petitioners in the next few months to ensure that proper expenditures are made in accordance with the Interim Budget. Such oversight will allow adequate protection to the stakeholders in this critical interim period while the Petitioners explore what options are available to them in the future with or without certain stakeholder support.

[64] I conclude that the Interim Financing Facility is reasonable and appropriate in the circumstances. I approve the interim draw of $15 million, as sought. This financing will provide a viable short term path forward to allow the Petitioners to explore restructuring options, all for the benefit of the entire large stakeholder group, including Nova Scotia, the employees (both past and present) and members of the PLFN, all of whom were represented on this application.

[65] As noted by Petitioners' counsel, no other viable alternatives are available to avoid the significant and negative social, economic and environmental consequences if the Petitioners do not receive the funding they need to advance their restructuring plan.

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SEVERANCE / SALARY CONTINUATION PAYMENTS

[66] The Initial Order provided that the Petitioners could pay certain employee expenses incurred prior to that date:

> 4. The Petitioners shall be entitled, but not required, to pay the following expenses which may have been incurred prior to the Order Date:
>
> (a) all outstanding wages, salaries, employee and pension benefits (including long and short term disability payments), vacation pay and expenses (but excluding severance pay) payable before or after the Order Date, in each case incurred in the ordinary course of business and consistent with the relevant compensation policies and arrangements existing at the time incurred …

[67] The pre-filing unsecured employee obligations fall into two categories:

a) 191 unionized employees were terminated before filing (or expect to be terminated shortly), trigging severance obligations under Unifor's collective bargaining agreements (the "Severance Obligations"). Before the filing, approximately half of that amount ($1.65 million) was paid, leaving approximately $1.94 million to be paid (some already due and the rest to be funded into July 2021); and

b) Between January and June 2020, 45 salaried employees were terminated. In that event, their employment agreements require payment of salary continuance (the "Salary Continuance"). Before the filing, $3.3 million of Salary Continuance was paid. Under the terms of the Initial Order, $370,000 was paid to these employees. The remaining estimated amount of Salary Continuance budgeted to be paid from August 2020 to September 2024 is approximately $3.5 million.

[68] The Interim Budget provides for payment of the Severance Obligations and the Salary Continuance, together with benefits to retired employees. The Petitioners seek an order allowing them to make such payments, estimated in total at $2.9 million to December 2020.

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[69] Unifor understandably supports the Petitioners' request to make pre-filing payments of the Severance Obligations in accordance with the Interim Budget.

[70] There is no dispute between the parties that I have the jurisdiction to authorize payment of pre-filing unsecured obligations. Section 11 of the *CCAA* provides a broad discretion to the Court to make any order as may be "appropriate in the circumstances". The more difficult question is whether I *should* exercise my discretion to allow such payments here.

[71] Nova Scotia disputes that these payments are appropriate in the circumstances. The Monitor presents, appropriately, a neutral exposition of the relevant circumstances, without recommendation.

[72] The Petitioners refer to *Cinram International Inc. (Re)*, 2012 ONSC 3767. In *Cinram*, the Court authorized payments to certain employees, including any obligations that arose prior to the filing. However, as noted at paras. 23 and 43, the Court did so in the context of Cinram's "ongoing business operations" and with respect to the "active employment of employees in the ordinary course".

[73] In this case, there are no ongoing business operations as discussed in *Cinram*; in addition, the payments are to be made to *former* employees who were terminated before the filing.

[74] The circumstances considered in *JTI-Macdonald Corp. (Re)*, 2019 ONSC 1625 are also unhelpful to the Petitioners. At paras. 24-25, the Court's discussion of payment of pre-filing employee claims took place within the context of "critical suppliers" and the need to ensure continued delivery of necessary goods and services for the debtor's operations and to support the restructuring. The Court accepted the recommendation of the proposed monitor that pre and post-filing "payroll and benefits" be paid. The monitor's reasons included that many of the relevant payments would have priority status and/or give rise to director liability if not paid. Further, in the proposed monitor's experience, it is common to pay pre-filing and post-filing obligations to employees in the normal course, to ensure continued

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and uninterrupted service by employees. Importantly, the debtor had sufficient cash on hand to pay these expenses, which is not the case here.

[75] The reasons advanced by the Petitioners in asserting that these payments are "critical" are much more ephemeral than the reasons advanced in *JTI-Macdonald*. The Petitioners argue that allowing payment of the pre-filing unsecured employee amounts (in addition to ongoing employee expenses) is necessary to:

a) preserve the Petitioners' going concern value;

b) ensure that the other activities provided for in the Interim Financing Budget can be carried out by the Petitioners' remaining employees;

c) mitigate the adverse effects of the Pulp Mill's closure in the communities in which the Petitioners operate. The Petitioners emphasize the significant negative consequences suffered by the lay-offs and terminations, particularly in the face of the COVID-19 pandemic;

d) preserve their relationships with the employees who are no longer working, many of whom are expected to be called upon to return to employment at the Pulp Mill in the future if the construction of the RETF is undertaken; and

e) preserve their relationship with Unifor. The Petitioners state that unions as a whole will inevitably be present in some form if the Petitioners resume operations. They say that preserving an effective working relationship with Unifor, consistent with Unifor's collective bargaining agreements, will provide an additional benefit to them, both during and after these proceedings.

[76] The Petitioners also reiterate that payment of these pre-filing employee amounts will signal their commitment to the stakeholders to develop and implement

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a plan to recommence the Pulp Mill's operations and in doing so, alleviate financial hardship within what they describe is a critical stakeholder group.

[77] I appreciate that court approval to allow payment to employees, even for pre-filing unsecured amounts, is often granted. When a debtor is conducting ongoing operations during a proceeding, it will often be necessary to ensure that employment relationships are not disrupted so as to hinder the restructuring efforts.

[78] However, the starting point for this discussion continues to be that *all* pre-filing unsecured amounts are not to be paid in a *CCAA* proceeding, even if owed to employees. All pre-filing creditors are covered under the general stay of proceedings; any payment is the exception to the general rule. That starting point is intended to preserve the *status quo* between creditors of the debtor pending the debtor advancing a fair and equitable proposal at the end of the day in respect of all of its obligations.

[79] At that later stage, it is generally anticipated that unsecured creditors will be treated fairly and equitably in any plan of arrangement, usually by way of a *pro rata* payment, subject to certain minimum requirements with respect to employee claims, as set out in s. 6(5) of the *CCAA*.

[80] Two Ontario decisions, cited by Nova Scotia, are of assistance.

[81] The first decision is *Nortel Networks Corp. (Re)*, [2009] O.J. No. 2558 (Ont. S.C.J.) aff'd *Sproule v. Nortel Networks Corp.*, 2009 ONCA 833. In the lower court, Justice Morawetz (as he then was) was addressing requests from the union and former employees for payment of their pre-filing claims for retirement allowance payments, voluntary retirement options, vacation pay, benefit options and termination and severance pay.

[82] At para. 51 of *Nortel*, Morawetz J. noted that it was necessary to take into account the overall financial picture of the applicants, who opposed the applications. There, as here, the debtor was not in a position to pay their obligations to all creditors and a number of defaults were present, including those relating to the

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unionized and former employees. At para. 57, Morawetz J. described that *Nortel* was not carrying on "business as usual", which is also the case here. The Court dismissed the application stating:

> [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.
>
> . . .
>
> [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.

[83] In *Sproule*, the Court of Appeal agreed that the stay applied to these types of claims:

> [39] The *CCAA* stay provision is a clear example of a case where the intent of Parliament, to allow the court to freeze the debt obligations owing to all creditors for past services (and goods) in order to permit a company to restructure for the benefit of all stakeholders, would be frustrated if the court's stay order could not apply to statutory termination and severance payments owed to terminated employees in respect of past services.

[84] The Court in *Nortel* asked the monitor to investigate whether an interim payment might be made to the employees in any event. That request was made, however, in very different circumstances where there were no significant secured creditors and a distribution to the unsecured creditors seemed likely in any event:

> [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.

[85] In *Windsor Machine & Stamping Ltd. (Re)*, [2009] O.J. No. 3195 (Ont. S.C.J.), the union brought an application to require the debtors to pay termination and

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severance pay owing as a result of post-filing terminations. The major secured creditor objected. Justice Morawetz similarly rejected this application, citing the priority of that secured creditor:

> [43] First, the priority of secured creditors must, in my view, be recognized. Counsel to the Union made the submission that the Applicants and the Bank are advancing a priority argument that may be relevant in a bankruptcy or receivership proceeding but not in a CCAA proceeding, as there is no priority distribution scheme in the CCAA. In my view this submission is misguided. Although there is no specific priority distribution scheme in the CCAA, that does not mean that priority issues should not be considered. An initial order under the CCAA usually results in a stay of proceedings as against secured creditors as well as unsecured creditors. The stay prevents secured creditors from taking enforcement proceedings which would confirm their priority position. The inability of a secured creditor to take such enforcement proceedings should not result in an enhanced position for unsecured creditors. There is no basis, in my view, for the argument that somehow the absence of a statutory distribution scheme entitles unsecured creditors to obtain enhanced priority over secured creditors for pre-filing obligations. To give effect to this argument would result in a situation where secured creditors would be prejudiced by participating in CCAA proceedings as opposed to receivership/bankruptcy proceedings. This could very well result in a situation where secured creditors would prefer the receivership/bankruptcy option as opposed to the CCAA option as it would recognize their priority position. Such an outcome would undermine certain key objectives of the CCAA, namely, (i) maintain the *status quo* during the proceedings; and (ii) to facilitate the ability of a debtor to restructure its affairs. In my view, it is essential, in a court supervised process, to give due consideration to the priority rights of secured creditors. In this case, the secured creditors have priority over the termination pay and severance pay claims of the Tilbury Union Employees and the Pellus Union Employees.
>
> [44] Second, counsel to the Union also submits that based on the rationale in the decision of the Court of Appeal in *Re 1231640 Ontario Inc. (State Group)* (2007), 37 C.B.R. (5th) 185 (Ont. C.A.), priority rules do not crystallize in a CCAA proceeding. I do not accept this argument. *State Group* addressed a priority issue as between competing PPSA secured creditors in the context of a interim receivership under s. 47 of the BIA. The issue in *State Group* was whether a s. 47 BIA receiver was a person who represents creditors of the debtor under s. 20(1)(b) of the PPSA. The Court of Appeal held that an interim receiver was not such a person. The issue in *State Group* governs the relationship as between competing interests under the PPSA. In my view, it does not stand for the proposition that the priority position of a secured creditor vis-à-vis unsecured creditors should not be recognized in the context of a CCAA proceeding.
>
> [45] Third, the Union put forth submissions to the effect that, in this particular situation, the amount of termination pay and severance pay is relatively low and the Applicants have the cash to pay the amounts owing and, further, that such payments would not jeopardize the Proposed Sale.

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> [46] In my view, the fact that the Applicants may have available cash does not mean that the Applicants can use the cash as they see fit. The asset is to be used in accordance with credit agreements and court authorized purposes, including those set out in the Amended and Restated Initial Order. I am in agreement with these submissions of counsel to the Applicants as set out at [15]. This Order placed restrictions on the use of cash, which restrictions are consistent with legal priorities. In my view, the fact that the Applicants have cash does not justify an alteration of legal priorities. The legal priority position is that the claims for termination pay and severance pay are unsecured claims which rank pari passu with other unsecured creditors and subordinate to the interests of the secured creditors. (See also *Indalex Limited*, [2009] O.J. No. 3165, CV-09-8122-00CL – July 24, 2009 on this point.)
>
> [47] I acknowledge that the situation facing the employees is unfortunate and that in *Nortel*, a hardship exception was made. However, this exception was predicated, in part, on the reasonable expectation that there will be a meaningful distribution to unsecured creditors, including the former employees. Such is not the case in this matter.

[86] The circumstances here are more resonant with the facts discussed in *Nortel* and *Windsor Machine*. Given that this proceeding is very much in its early days, I cannot conclude that a distribution to pre-filing unsecured claims (including to the employees) is likely at the end of the day. There are no ongoing operations; there is no cash with which to pay these amounts.

[87] Significantly, Nova Scotia, the major secured creditor, whose security would be primed by these payments, objects. In the absence of any objection by Nova Scotia, and with the general support of the Petitioners and the stakeholders appearing on this application, I might have come to a different conclusion.

[88] The Petitioners also argue that the Severance Obligations constitute inchoate priority charges under provisions of the Nova Scotia *Labour Standards Code*, R.S.N.S. 1989, c. 246 (the "*Code*"). They argue that these provisions would be triggered if an employee makes a successful claim to the Nova Scotia Labour Board (the "Board") and the Board issues an order. They refer to s. 88 of the *Code* that provides that amounts in an order are a debt due to the Board secured by a lien or mortgage that has priority over all other liens, charges, or mortgages. They also refer to ss. 90 and 90A of the *Code* with respect to potential actions by the Board. However, any such actions are currently stayed under the Initial Order, just as they

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are with respect to any action that might have been taken by Nova Scotia as a secured creditor.

[89] This is an unpersuasive argument by the Petitioners in any event. It is well taken that a province cannot create priorities that alter the federal scheme of distribution in the event of a bankruptcy: *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3, ss. 86-87, 136: *Husky Oil Operations Ltd. v. Minister of National Revenue*, [1995] 3 S.C.R. 453. Given that these proceedings are in their nascent days, it is anyone's guess on the outcome. A bankruptcy remains a possibility, however slight in the Petitioners' minds.

[90] I accept, without hesitation, that these hard working and dedicated employees will meet my decision with a great deal of disappointment, if not dismay. The reasons for the closure and shutdown are completely divorced from their commitment to their jobs. I also appreciate that this vulnerable group of stakeholders will suffer arising from my decision. I say this knowing that the Petitioners represented – or at least previously represented – a significant employer in the province and in Pictou County, particularly. I expect that many of these lost jobs, no doubt some with expertise involving work at pulp mills, cannot be easily replaced, if at all.

[91] The Petitioners have emphasized the need to maintain the goodwill of their workforce in the event that the RETF is constructed and operations recommence. Whether or not the Petitioners will achieve that objective is simply unknown at this time.

[92] Unfortunately, I conclude that there is no principled basis upon which I could exercise my discretion to grant this relief. The Petitioners have not advanced a persuasive case toward authorizing such payments in such nebulous circumstances, particularly when it would amount to prioritizing those unsecured creditors over the existing security of Nova Scotia and where Nova Scotia objects.

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TERRAPURE

[93] Before and after the *CCAA* filing, Envirosystems Inc., dba Terrapure Environmental ("Terrapure") provided services to the Petitioners relating to the removal of wastewater. The pre-filing debt owed to Terrapure for its services is approximately $1.1 million.

[94] The Petitioners do not seek any relief in favour of Terrapure, such as a declaration that it is a "critical supplier". Indeed, by the date of this application, the Petitioners had found an alternate means to remove the wastewater and they advised that it is unlikely they will need any further services from Terrapure.

[95] Terrapure's position on this application is to support the approval of the Interim Financing Facility and the payment of the unsecured pre-filing claims of the employees, but only if Terrapure is similarly paid its pre-filing unsecured claim.

[96] The general discussion above regarding the general application of the stay of proceedings with respect to unsecured creditors equally applies to Terrapure. Nova Scotia similarly objects to any payment to Terrapure, since the means to make any such payment could only arise from the Interim Financing Facility.

[97] In my view, there is no basis to prefer Terrapure in this case by allowing payment of its pre-filing unsecured claim. All claims by unsecured creditors are equally covered by the stay under the Initial Order, including the claims by employees, as discussed above, and Terrapure.

[98] In the event that the Court did not approve payment of its pre-filing debt, Terrapure requested the addition of a term in the ARIO to confirm that it has no further obligation to provide services to the Petitioners. No one raised any objections to that provision and I grant that relief.

KEY EMPLOYEE RETENTION PLAN (KERP)

[99] The Petitioners seek approval of a KERP and the granting of a Court ordered KERP charge to a maximum of $342,207 (the "KERP Charge"). They say that the

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KERP is for a select group of key employees to incentivize their continued retention, which is necessary if there is to be any viable prospect for the Petitioners to pursue their restructuring strategy.

[100] They propose that the KERP Charge rank directly below the Directors' Charge.

[101] The Court may exercise its discretion under its general statutory jurisdiction under s. 11 of the *CCAA* to approve a KERP and grant a KERP Charge: *U.S. Steel Canada Inc. (Re)*, 2014 ONSC 6145 at para. 27.

[102] As the Petitioners note, courts across Canada have approved key employee incentive plans in numerous *CCAA* proceedings: for example, *Nortel Networks Corp. (Re)*, [2009] O.J. No. 1044 (Ont. S.C.J.) and *U.S. Steel Canada*.

[103] In *Walter Energy Canada Holdings, Inc. (Re)*, 2016 BCSC 107, this Court stated:

> [58] Factors to be considered by the court in approving a KERP will vary from case to case, but some factors will generally be present. See for example, *Grant Forest Products Inc. (Re)* (2009), 57 C.B.R. (5th) 128 (Ont. S.C.J.); and *U.S. Steel Canada* at paras. 28-33.

[104] In *Walter Energy* at para. 59, I discussed the *Grant Forest Products* factors, as follows:

- Is this employee important to the restructuring process?
- Does the employee have specialized knowledge that cannot be easily replaced?
- Will the employee consider other employment options if the KERP is not approved?
- Was the KERP developed through a consultative process involving the Monitor and other professionals?; and
- Does the Monitor support the KERP and a charge?

[105] More recently, in *Aralez Pharmaceuticals Inc. (Re)*, 2018 ONSC 6980 at para. 30, Justice Dunphy stated that three criterion underlie all of the considerations of key employee retention and incentive programs in insolvency proceedings as

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discussed in the relevant case law: arm's length safeguards, necessity and reasonableness of design.

[106] As Mr. Chapman describes, the KERP has been designed to facilitate and encourage the continued participation of select key employees of the Petitioners who are contemplated to either (a) provide necessary services up to the expiry of the stay period (to December 2020); or (b) guide the business through the restructuring and preserve value for stakeholders over the length of the case.

[107] The KERP consists of two independent programs: the Key Management Employee Retention Plan (the "Management KERP") and the Key Technical Employee Retention Plan (the "Technical KERP"). These plans would apply to a small number of employees: five under the Management KERP; two under the Technical KERP. Payments under the Technical KERP are conditional on the proceedings continuing on the date that each payment is to be made and do not amount to a long-term payment commitment if the restructuring fails.

[108] The Petitioners' evidence on this application fully supports an affirmative answer to all of the above questions set out in *Walter Energy*. These employees are important to the restructuring process; the Monitor describes a "knowledge and operational void" if their employment is not further secured in some fashion. Given the nature of the assets in question, I agree that these employees, both management and technical, have specialized knowledge that cannot be easily replaced.

[109] There is no evidence on this application that any of these employees are considering other employment options if the KERP is not approved. However, that lack of evidence is not fatal to approval of the KERP since that very scenario is intended to be avoided by approval of the KERP.

[110] The KERP was developed through a consultative process involving the Monitor. The Monitor supports the KERP and the KERP Charge, noting that without

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securing this “human capital”, the ability of the Petitioners to restructure their affairs will be greatly impaired.

[111] The Monitor notes in particular that Mr. Chapman, a PEC employee and general manager of the Pulp Mill, is included in the KERP. The Monitor describes Mr. Chapman as a “key resource” and provides that his continued support is “critical” toward achieving a successful restructuring. Mr. Chapman has been the person providing significant evidence in support of the Petitioners in this proceeding to date, which speaks to that fact.

[112] No stakeholder opposes this relief. In my view, such relief is appropriate. I approve the KERP and I grant the KERP Charge on the terms sought.

ADMINISTRATION / DIRECTORS’ CHARGES

[113] The Petitioners have not sought an increase of the Administration Charge on this application. The Petitioners seek the continuation of the Administration Charge in its previously approved amount (not to exceed $500,000) to secure professional fees and disbursements of the Monitor, counsel to the Monitor and the Petitioners' counsel.

[114] The Petitioners have also determined that they do not require an increase of the Directors’ Charge at this time. The Petitioners seek the continuation of the Directors’ Charge in its previously approved amount (not to exceed $500,000) to secure the indemnity provided for in the Initial Order.

[115] Again, no opposition arises. In my view, continuing this relief from the Initial Order is appropriate and I grant it.

STAY EXTENSION

[116] The Petitioners seek an extension of the stay to December 31, 2020.

[117] Under s. 11.02(2) of the *CCAA*, the Court has broad jurisdiction to extend a stay of proceedings where the circumstances warrant and for any period the Court considers necessary. Baseline considerations include those set out in s. 11.02(3) of

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the *CCAA*, including confirmation that the debtor is acting with due diligence and in good faith and that the relief sought is appropriate.

[118] The comments of court in *Timminco Limited (Re)*, 2012 ONSC 2515 aptly set out the statutory objectives intended to be achieved by the stay:

> [15] The stay of proceedings is one of the main tools available to achieve the purpose of the CCAA. The stay provides the [debtors] with a degree of time in which to attempt to arrange an acceptable restructuring plan or sale of assets in order to maximize recovery for stakeholders. The court's jurisdiction in granting a stay extends to both preserving the *status quo* and facilitating a restructuring. See *Re Stelco Inc.*, (2005) O.J. No. 1171 (C.A.) at para. 36.

[119] Throughout this proceeding, and to this time, the Monitor confirms its view that the Petitioners have been working in good faith and with due diligence. The Monitor recommends the extension of the stay to December 31, 2020.

[120] It will be more than apparent from the discussion above and the orders I have granted, particularly as to the Interim Financing Facility, that I have concluded that an extension of the stay to December 31, 2020 is appropriate in the circumstances. As discussed above, there is somewhat of a "check" on the proceedings arising from the Monitor's report that will be filed before the end of October 2020.

[121] The stay period to December 2020 will allow the Petitioners to advance their objective of securing a restructuring option for the benefit of the stakeholders. I conclude that they should be afforded the opportunity to do so here.

UNIFOR APPLICATION

[122] Unifor seeks an order authorizing it to represent the current and former union members of the local, including pensioners, retirees, deferred vested participants, and their surviving spouses and dependants, employed or formerly employed by the Petitioners, in these proceedings. Unifor does not seek any court ordered funding to secure its participation or that of Pink Larkin, its counsel.

[123] The Petitioners support this relief and no stakeholder objects.

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[124] As with much of the above relief, the Court has jurisdiction to exercise its discretion to grant the order sought under its broad statutory jurisdiction found in s. 11 of the *CCAA*.

[125] In *Canwest Publishing Inc.*, 2010 ONSC 1328, the Court discussed the factors typically considered in granting such relief. Justice Pepall (as she then was) set those out as follows:

> [21] Factors that have been considered by courts in granting these orders include:
>
> - the vulnerability and resources of the group sought to be represented;
> - any benefit to the companies under *CCAA* protection;
> - any social benefit to be derived from representation of the group;
> - the facilitation of the administration of the proceedings and efficiency;
> - the avoidance of a multiplicity of legal retainers;
> - the balance of convenience and whether it is fair and just including to the creditors of the Estate;
> - whether representative counsel has already been appointed for those who have similar interests to the group seeking representation and who is also prepared to act for the group seeking the order; and
> - the position of other stakeholders and the Monitor.

See also *Target Canada Co. (Re)*, 2015 ONSC 303 at para. 61.

[126] I agree that these employees presently have a commonality of interest that is best represented in this proceeding as an entire group. Wanda Skinner is the president of the Unifor local. Ms. Skinner's affidavit #2 sworn July 28, 2020 supports the vulnerability of the unionized employees arising from the disastrous economic consequences to them of losing their jobs and benefits.

[127] Unifor clearly has a relationship with this cohort and is in the best position to advance the entire group's interests, at least at this time. That representation will be a benefit to the Petitioners in advancing this restructuring by facilitating discussions between them. The estate will incur no cost by reason of Unifor's representation, welcome news given the lack of cash resources available to the Petitioners.

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[128] The order sought by Unifor is consistent with the order granted in the Fraser Papers Inc. restructuring: see *Fraser Papers Inc. (Re)*, 2009 CanLII 55115 and 2009 CanLII 63589 (Ont. S.C.J.).

[129] I am satisfied that the terms of the order sought are appropriate, with one exception. In para. 3 of the draft order, Unifor seeks authority to "determine, file, advance or compromise" any claims of its current or former employees. The only change I would make to that provision is to amend it to provide that any compromise proposed to be made by Unifor will be subject to court approval. This will ensure some oversight in respect of any decisions that Unifor seeks to make for the employee group they will represent.

"Fitzpatrick J."

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IN THE SUPREME COURT OF BRITISH COLUMBIA

Citation: *Mountain Equipment Co-Operative (Re),* 2020 BCSC 1586

Date: 20201028
Docket: S209201
Registry: Vancouver

In the Matter of the *COMPANIES' CREDITORS ARRANGEMENT ACT,* R.S.C. 1985, C. C-36, as amended

- AND -

In the Matter of MOUNTAIN EQUIPMENT CO-OPERATIVE and 1314625 ONTARIO LIMITED

Petitioners

Before: The Honourable Madam Justice Fitzpatrick

Reasons for Judgment

Counsel for the Petitioners, Mountain Equipment Co-Operative and 1314625 Ontario Limited:	H. Gorman, Q.C. S. Boucher
Counsel for the Monitor, Alvarez & Marsal Canada Inc.:	H.L. Williams J. Enns
Counsel for Royal Bank of Canada, as Administrative Agent and Collateral Agent under Credit Agreement:	J. Sandrelli V. Cross
Counsel for Kingswood Capital Management LP, Kingswood Capital Opportunities Fund I, LP, Kingswood Capital Opportunities Fund I-A, LP and 1264686 B.C. Ltd.:	D. Chochla K. Jackson

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Counsel for Plateau Village Properties Inc.:	C. Ramsay K. Mak P. Cho N. Carlson
Counsel for Midtown Plaza Inc.:	K. McEwan, Q.C. C. Smith R. Atkins W. Stransky
Counsel for RioCan Real Estate Investment Trust Company:	L. Galessiere
Counsel for Crestpoint Real Estate Investments Ltd., as authorized asset manager of 0965311 B.C. Ltd.:	B. Wiffen
Counsel for Les Galeries de la Capitale Holdings Inc. and manager Oxford Properties Group:	F. Viau
Counsel for First Capital Holdings (Alta) Corp. and First Capital (Ontario) Corp.:	K. Hashmi
Counsel for Concert Properties Limited:	H. Meredith
Counsel for Kevin Harding, spokesperson for steering committee for “SaveMEC” campaign:	C. Gusikowski P. Reardon
Counsel for BC Co-op Association and Co-operatives and Mutuals Canada:	E. Bridgewater
Place and Date of Hearing:	Vancouver, B.C. September 28-30 and October 1, 2020
Place and Date of Decision with Written Reasons to Follow:	Vancouver, B.C. October 2, 2020
Place and Date of Written Reasons:	Vancouver, B.C. October 28, 2020

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INTRODUCTION

[1] On September 14, 2020, the petitioners, Mountain Equipment Co-operative and its wholly owned subsidiary, 1314625 Ontario Limited ("131"), sought and obtained relief pursuant to the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36 (the "*CCAA*"). I will refer to the petitioners jointly by the first petitioner's well-known acronym, "MEC".

[2] On September 14, 2020, I granted an Initial Order in favour of MEC that included a stay until September 24, 2020, although that was later extended to the time of this comeback hearing. I also approved an interim financing facility to a total of $100 million (the "Interim Financing"), although draws were then limited to $15 million, consistent with the test set out in s. 11.2(5) of the *CCAA*. I appointed Alvarez & Marsal Canada Inc. ("A&M") as the Monitor. Finally, I approved charges usually granted in these proceedings: an Administration Charge ($1 million), a D&O Charge ($4.5 million) and an Interim Financing Charge ($102 million).

[3] At this comeback hearing, MEC seeks an Amended and Restated Initial Order (ARIO) to continue the relief granted in the Initial Order, with approval to access the entire amount under the Interim Financing. In addition, MEC seeks approval of a Key Employee Retention Program (KERP) and a related charge. Finally, MEC seeks an order approving a sale of substantially all of its assets, pursuant to a Sale Approval and Vesting Order (SAVO).

[4] Since September 14, 2020, formidable opposition has formed in response to MEC's application for approval to sell its assets under the SAVO.

[5] Many parties now seek an adjournment of MEC's application for the SAVO, objecting to any sale at this time for various reasons. Those parties include two landlords, Plateau Village Properties Inc. ("Plateau") and Midtown Plaza Inc. ("Midtown"), and Kevin Harding, spokesperson for the steering committee for the "SaveMEC" campaign. Mr. Harding also seeks an order appointing his law firm as representative counsel for certain members of MEC, with an accompanying charge for their expenses.

[6] MEC contends that it is critical that the sale occur without delay. MEC opposes all of the relief sought by the objecting parties.

[7] On October 1, 2020, I concluded the comeback hearing. On October 2, 2020, I granted the orders sought by MEC, including the SAVO, and dismissed the relief sought by the objecting parties, with reasons to follow. These are my reasons.

BACKGROUND

[8] MEC is a co-operative association incorporated under the *Cooperative Association Act,* S.B.C. 1999, c. 28 (the "*Co-op Act*").

[9] In 1971, almost 50 years ago, MEC was formed from the passion of many Vancouverites who loved to spend time outdoors and appreciated having the right equipment and gear to do so. Since then, MEC has become an iconic retailer of outdoor activity equipment and clothing, serving the needs of the public who share that passion for the outdoors. MEC sells many well-known brands and also has its own very successful private label for many products.

[10] MEC's ownership is unique. MEC currently has approximately 5.8 million members, each having paid a $5 lifetime membership fee for the right to shop at MEC and participate in its governance as a co-operative member. Counsel advises that the breadth of MEC's membership in Canada is significant, representing some 22% of the Canadian working population.

[11] 131 owns a parcel of land that comprises the parking lot at the site of MEC's Ottawa Store. 131's assets are not significant in the overall circumstances. Similarly, MEC also owns an interest in a limited partnership which has nominal value.

[12] MEC has a significant history of community involvement. Since 1987, MEC has contributed approximately $44 million to organizations focused on conservation and outdoor recreation.

[13] MEC's head office is located at leased premises in Vancouver, BC. MEC operates online and also, operates 22 retail locations across Canada in BC, Alberta,

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Manitoba, Ontario, Quebec and Nova Scotia. MEC leases its eastern distribution centre in Brampton, Ontario and most (16) of its store operations. MEC owns six store locations and its western distribution centre in Surrey, BC.

[14] As of September 7, 2020, MEC has approximately 1,516 employees: 1,143 active employees, 176 laid off employees, 118 employees on the Canada Emergency Wage Subsidy program and 79 employees on unpaid leave.

[15] MEC's board of directors (the "Board") has eight directors. As of September 10, 2020, MEC's senior management consists of seven officers. Philippe Arrata is MEC's Chief Executive Officer who has provided most of the sworn evidence on behalf of MEC in this proceeding.

[16] In 2015, MEC embarked on a significant growth plan. That plan resulted in six new stores and two new relocated stores in Vancouver and Toronto, a new head office, a new eastern distribution centre as well as significant investments in online retail resources. MEC has commitments for two additional new stores (Calgary North West and Saskatoon) that have not yet opened, which is a point of controversy on this application. Over the ensuing years, this growth plan was successful from a market expansion and sales perspective, but it also resulted in a higher fixed cost structure and increased debt levels.

[17] In August 2017, MEC, as borrower, and 131, as guarantor, entered into a credit agreement with the Royal Bank of Canada (RBC), as agent, and RBC, Canadian Imperial Bank of Commerce and the Toronto-Dominion Bank (collectively, the Lenders") for a senior secured asset-based revolving credit facility (the "Credit Facility").

[18] The Credit Facility initially allowed MEC to borrow up to a maximum of $130 million with a maturity date of August 3, 2020. Through various amendments implemented over 2020, that borrowing maximum was reduced to its present level, $100 million. The Lenders hold first priority security over all of MEC's assets.

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[19] The results of MEC's growth strategy led to challenging fiscal circumstances. Since 2015, MEC's operating losses were approximately $80 million, offset to some extent by real estate transactions that realized capital gains. Even so, the net loss for the year ending February 23, 2020 was approximately $22.7 million, largely arising from increased costs, certain under-performing stores and liquidity strains.

[20] MEC's assets consist primarily of: owned and leased real property; equipment; inventory; accounts receivable; and intangible assets including certain trademarks on trade names, membership lists and goodwill. As of February 2020, MEC's recorded a book value of approximately $389 million in current and long-term assets.

[21] MEC's liabilities are comprised primarily of: amounts owed to suppliers; governments and employees; amounts owed to the Lenders under the Credit Facility; gift cards and provision for sales returns; lease obligations; and deferred lease liabilities. MEC's current and long-term liabilities, as reported in its February 2020 Financial Statements, totalled approximately $229.6 million.

EVENTS LEADING TO *CCAA* PROCEEDINGS

[22] In early 2020, MEC took steps to address its financial difficulties. MEC's Board brought in a new management team to focus on cost reduction and a return to profitability.

[23] On February 10, 2020, MEC engaged Alvarez and Marsal Canada Securities ULC ("A&M Securities") as a financial advisor to assist in a review of strategic alternatives, provide assistance to obtain and negotiate new financing. A&M Securities is an entity affiliated with A&M, the Monitor.

[24] In March 2020, the Board struck a special committee, comprised of three Board members (the **"**Special Committee"). The mandate of the Special Committee was to make recommendations to MEC's Board on strategic alternatives, including (a) transactions with a view to sell all or substantially all or any portion of MEC's assets (or a merger, amalgamation or some other strategic alliance involving MEC);

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(b) pursuit of organic growth; (c) recapitalization, restructuring or reorganization; or (d) any other strategic alternative in the best interests of MEC.

[25] The efforts of the new management team, the Special Committee and A&M Securities led eventually to the implementation of a Sales and Investment Solicitation Process (SISP) that resulted in the proposed sale that MEC now seeks to have court approved.

[26] Under its initial mandate, A&M Securities made efforts toward identifying a satisfactory refinancing, including: establishing a data room; contacting a number of lenders; and, entering into a number of Non-Disclosure Agreements (NDAs) with lenders. However, MEC and A&M Securities' efforts to find a solution to MEC's very difficult financial difficulties were hampered by the COVID-19 pandemic that hit Canada in March 2020. As one might expect, the pandemic had a significant and negative impact on the retail sector generally and on MEC's already struggling operations. All of MECs stores closed as of March 18, 2020.

[27] As the Monitor notes, MEC's insolvency arose from an unsustainable 25 "bricks and mortar" store operating model, the "disastrous" impact from the pandemic on sales and cash flow and inadequate financing capacity to sustain ongoing losses and provide working capital.

[28] Although A&M Securities received a number of term sheets for a refinancing, none of them provided for a complete refinancing of MEC's debt that solved its serious financial challenges.

[29] On June 1, 2020, as permitted by the BC Registrar for all cooperative associations, MEC announced that its Annual General Meeting (AGM) (originally scheduled for June 23, 2020) would be postponed by up to six months due to the impact of COVID-19 and to allow MEC to focus on the urgent financial challenges impacting its business. The AGM is scheduled for December 10, 2020.

[30] On June 10, 2020, with the support of the Lenders, MEC expanded A&M Securities' engagement to explore whether there were other potential viable

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refinancing options and to initiate a SISP. The Special Committee established guiding commercial principles in the design of the SISP to: provide maximum value to the broad stakeholder group; preserve the maximum number of store locations and jobs; and ensure that, if possible, the buyer preserved MEC's purpose, values and outreach programs.

[31] Again, A&M Securities followed the usual path in this effort, including establishing a data room, identifying potential interested purchasers, distributing an initial "teaser" letter to 158 parties and entering into confidentiality agreements with 39 interested parties. A&M Securities requested non-binding Letters of Intent (LOIs).

[32] By July 15, 2020, A&M Securities had received nine LOIs and reviewed and conducted due diligence on each of them. On July 16, 2020, A&M Securities presented the LOIs to the Special Committee for its consideration and later provided its recommendations with respect to having bidders move into "Phase 2" of the SISP process. On July 24, 2020, MEC's Board considered the Special Committee's recommendation with respect to the LOIs.

[33] On August 6, 2020, Phase 2 of the SISP process began with five recommended bidders who had submitted LOIs. The Phase 2 process established a final bid deadline of August 28, 2020. Four bids were received by that deadline, as were later reviewed by A&M Securities and the Special Committee.

[34] On September 4, 2020, MEC's Board, with the input of their advisors, identified Kingswood Capital Management LP ("Kingswood"), a US based private investment firm, as the successful bidder and negotiations began to finalize a purchase and sale agreement.

[35] As with many retailers, by mid-September 2020, the impact of the pandemic, which only exacerbated MEC's pre-existing difficulties, remained very relevant. In the months leading to September 2020, MEC realized a considerable increase in online sales, however, it still experienced a substantial reduction in sales compared to last year for that period ($98 million). By mid-September 2020, MEC has re-

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opened many of its stores, however, five remain closed because of the pandemic. The stores that had re-opened were operating at a reduced sales volume.

[36] As of September 4, 2020, and primarily due to the pandemic, MEC owed approximately $4.6 million in rent deferrals or arrears in respect of its leases, and MEC had agreed to rent deferral plans with some of its landlords to repay these arrears by late 2021. Further, MEC had significant past due amounts owed to merchandise suppliers and other vendors.

[37] As of September 11, 2020, MEC owed approximately $74 million under the Credit Facility, leaving approximately $19 million available under the borrowing base. At that time, MEC was unable to repay the Credit Facility by the maturity date of September 30, 2020.

[38] All of these factors, together with MEC's ongoing lease, contractual and trade creditor obligations, led MEC to decide that it had no alternative but to seek a formal restructuring of its affairs in court proceedings and seek to conclude the Kingswood sale in those proceedings.

[39] On September 11, 2020, MEC and Kingswood entered into an asset purchase and sale agreement (the "Sale Agreement"). Under the Sale Agreement, Kingswood, through a Canadian-based subsidiary, agreed to purchase substantially all of MEC's assets. The Sale Agreement is conditional on MEC obtaining court approval through this *CCAA* proceeding.

[40] By the date of the filing (September 14, 2020), RBC had formally notified MEC of defaults under the Credit Facility. Despite MEC's challenging financial affairs, the Lenders confirmed their support for MEC in this *CCAA* proceeding and they continue to support MEC in terms of the relief presently sought.

GERM OF THE PLAN

[41] When I granted the Initial Order, MEC had outlined a restructuring plan. During the course of these proceedings, MEC indicated its intention to:

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a) Immediately stabilize its cash flows and operations;

b) Develop a strategy that would address its liquidity issues and generate sufficient revenue to sustain operations through the *CCAA* process, including by streamlining operations;

c) Apply for the SAVO to approve the transaction with Kingswood, which would allow repayment to the Lenders and also allow MEC's business to emerge as a better capitalized operation with as little disruption as practicable; and

d) Establish and complete a claims process toward formulating a plan of compromise and arrangement for presentation to its creditors. The intention is to fund a plan from the proceeds arising from the Kingswood sale.

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FUTHER *CCAA* RELIEF SOUGHT

[42] As stated above, MEC seeks to continue the relief sought in the Initial Order, with additional relief relating to: full approval of draws under the Interim Financing, approval of a KERP, extending the stay to November 3, 2020 and granting the SAVO.

[43] MEC's application is supported by the Monitor's First Report dated September 24, 2020 (the "First Report").

Interim Financing

[44] At the commencement of these proceedings, MEC indicated that it required the Interim Financing to support its operations and restructuring efforts. It was and is very apparent that MEC needs the Interim Financing for those purposes.

[45] MEC secured a financing commitment from the Lenders pursuant to a restructuring support agreement dated September 11, 2020 (the "Restructuring Support Agreement"). It was a condition of the Lenders' support under the Restructuring Support Agreement that they obtain a court-ordered security interest,

lien and charge over all of MEC's assets. One of the key financial terms of the Interim Financing was that it was subject to a calculation of borrowing availability, with a maximum principal amount of $100 million under the combined Credit Facility and the Interim Financing, funded in progressive advances on an as-needed basis.

[46] Pursuant to the Initial Order, I approved the Interim Financing, with draws limited to $15 million to the time of the comeback hearing, and approved the Interim Financing Charge. During the course of this hearing, I increased the draw limit to $23 million.

[47] Firstly, I was satisfied that the Interim Financing Charge complied with s. 11.2(1) of the *CCAA* in that it did not secure any of MEC's pre-filing obligations to the Lenders, as prohibited by that provision.

[48] The Interim Financing agreements are amendments to the Credit Facility, pursuant to which the Lenders will provide further liquidity to MEC despite any defaults under the Credit Facility. It is an express term of the Interim Financing that advances made under the Interim Financing cannot be used to satisfy pre-filing obligations under the Credit Facility or any other pre-filing debt. In addition, the Interim Financing Charge does not secure any of MEC's pre-filing obligations and includes a "carve out" to ensure that other secured creditors (such as those with Purchase Money Security Interests (PMSIs)) are not primed by the Charge.

[49] While the terms of the Interim Financing provide that post-filing receipts collected by MEC will be applied to pay down MEC's pre-filing debt under the Credit Facility, I agreed with MEC that mechanisms in interim financing agreements by which pre-filing obligations are paid from proceeds derived by post-filing operations do not contravene s. 11.2(1) of the *CCAA*.

[50] In *Performance Sports Group Ltd. (Re*), 2016 ONSC 6800, Justice Newbould concluded that a similarly crafted interim lending facility did not offend s. 11.2(1):

> [22] Section 11.2(1) of the *CCAA* provides that security for a DIP facility may not secure an obligation that existed before the order authorizing the security was made. The effect of this provision is that advances under a DIP

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> facility may not be used to repay pre-filing obligations. In this case, the ABL DIP Facility is a revolving facility. Under its terms, receipts from operations of the PSG Entities post-filing may be used to pay down the existing ABL Facility. The applicants submit that in this case, the ABL DIP Facility preserves the pre-filing status quo by upholding the relative pre-stay priority position of each secured creditor. By requiring that the PSG Entities only use post-filing cash receipts to pay down the accrued balance under the revolving credit facility, the ABL DIP Lenders are in no better position with respect to the priority of their pre-filing debt relative to other creditors. I accept that no advances under the ABL DIP Facility will be used to pay pre-filing obligations and there has been inserted in the Initial Order a provision that expressly prevents that. The provision that receipts from operations of the PSG Entities post-filing may be used to pay down the existing ABL Facility is approved.

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[51] Similar conclusions were reached in *Comark Inc. (Re)*, 2015 ONSC 2010 at paras. 17-29. Regional Senior Justice Morawetz (as he then was) accepted that the proposed interim financing facility would not result in a greater level of secured debt than was contemplated under the pre-filing facilities and would not prime PMSIs. Effectively, the court found that, since the proposed charge would increase while the pre-filing facility would be paid down by the use of the debtor's cash generated from its business, the proposed charge only secured post-filing advances made under the interim facility in compliance with s. 11.2(1) of the *CCAA*.

[52] In May 2020, Justice Romaine reached the same conclusion in a recent *CCAA* proceeding involving ENTREC Corporation (Alta QB, Calgary Judicial Centre; File No. 2001 06423).

[53] Secondly, I was satisfied that a consideration of the factors set out in s. 11.2(4) of the *CCAA* supported that the Interim Financing (then with limited draws) was appropriate. Those factors are:

> a) the period during which the company is expected to be subject to proceedings under this Act;
>
> b) how the company's business and financial affairs are to be managed during the proceedings;
>
> c) whether the company's management has the confidence of its major creditors;
>
> d) whether the loan would enhance the prospects of a viable compromise or arrangement being made in respect of the company;
>
> e) the nature and value of the company's property;

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

g) the monitor's report referred to in paragraph 23(1)(b), if any.

[54] The governing factors at the time of the granting of the Initial Order were:

a) MEC anticipated that it would seek an extension of the stay of proceedings at the comeback hearing for a further amount of time to allow it to complete the sale process without having to seek a further extension;

b) MEC's business and financial affairs were to be managed by MEC's Board and key management employees in consultation with the (then) proposed Monitor;

c) MEC had the confidence of the Lenders, its senior secured creditors and the proposed Interim Lenders. The Lenders supported the approval of the Interim Financing and the granting of the Interim Financing Charge;

d) Without the Interim Financing, MEC was not able to fund its operations and continue its restructuring efforts, and the value of its assets would have diminished as a result. In fact, the Credit Facility matured on September 30, 2020;

e) I was satisfied that no secured creditor would be materially prejudiced by the Interim Financing Charge, as the charge includes the carve out and preserved the pre-filing status *quo*; and

f) The proposed Monitor supported the approval of the Interim Financing and granting of the Interim Financing Charge.

[55] Finally, in light of s. 11.2(5) of the *CCAA*, I was satisfied that the terms of the financing were limited to those reasonably necessary for MEC's continued operations in the ordinary course of business during the period to the comeback

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hearing. In addition, I was satisfied that the terms of the Interim Financing were consistent with ordinary commercial transactions of this nature, as also confirmed by the proposed Monitor. See *Miniso International Hong Kong Limited v. Migu Investments Inc.*, 2019 BCSC 1234 at paras 79-90.

[56] The Interim Financing provides for a maturity date that is the earlier of a) November 30, 2020; b) the completion of a "Transaction" in relation to all or substantially all of MEC's assets, and sufficient to repay the Lenders in full, and is approved by the Court; and c) at the Lenders' option, the occurrence of any Event of Default (other than the commencement of the *CCAA* proceedings).

[57] MEC now seeks approval of the Interim Financing generally, which would allow it to request subsequent advances up to the $100 million limit until the next extension period on November 3, 2020.

[58] No creditor or stakeholder objects to the Interim Financing sought by MEC.

[59] The Cash Flow Forecast prepared in mid-September 2020 readily supported that MEC is in urgent need of interim funding during the restructuring. In the First Report, the Monitor noted that the Lenders had already advanced $9.4 million under the Interim Facility and confirmed that the full amount of the funding under the Interim Financing was required. No other source of financing was available; the Credit Facility expired on September 30, 2020. No creditor will be prejudiced, let alone materially prejudiced, by this funding.

[60] MEC's financial circumstances continue to be very challenging, even in the short term. Ongoing weekly losses of approximately $1.1-1.6 million are being incurred. In October 2020 alone, MEC projects losses of over $15 million.

[61] Having considered all of the factors in s. 11.2(4) of the *CCAA*, I have no hesitation concluding that approval of the full amount of the Interim Financing is appropriate. Without the Interim Financing, MEC is unable to continue its operations, a result that would have disastrous consequences to the larger stakeholder group, whether or not the SAVO is granted.

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The KERP

[62] MEC seeks approval of a KERP. To secure obligations under the proposed KERP, MEC also seeks the granting of a third-priority court-ordered charge on MEC's assets in priority to all other charges, other than the Administration Charge and the D&O Charge (the "KERP Charge").

[63] MEC asserts that the KERP is necessary to allow it to maintain its business operations, complete the restructuring, including completing the sale to Kingswood and preserve asset value. MEC says that, without a KERP, its efforts would be seriously compromised.

[64] In July and September 2020, MEC's Board approved retention agreements (the "Retention Agreements") for eight key senior managers for total compensation of $778,000. The Retention Agreements were filed under seal in these proceedings, as summarized in Appendix E to the First Report.

[65] The Retention Agreements include provision for payment of compensation upon the earlier of certain dates, including a sale of all or substantially all of MEC's assets (or the merger, amalgamation or consolidation of MEC with another entity), the employee's termination without cause or, by certain dates in December 2020, depending on the employee. It is not certain that all executives offered Retention Agreements will remain with MEC through to conclusion of the restructuring.

[66] The Court may exercise its discretion under its general statutory jurisdiction under s. 11 of the *CCAA* to approve a KERP and grant a KERP Charge: *U.S. Steel Canada Inc. (Re)*, 2014 ONSC 6145 at para. 27.

[67] Courts across Canada have approved key employee incentive plans in numerous *CCAA* proceedings: for example, *Nortel Networks Corp. (Re)*, [2009] O.J. No. 1044 (Ont. S.C.J.) and *U.S. Steel Canada*. In *Walter Energy Canada Holdings, Inc. (Re)*, 2016 BCSC 107, this Court stated:

> [58] Factors to be considered by the court in approving a KERP will vary from case to case, but some factors will generally be present. See for

example, *Grant Forest Products Inc. (Re)* (2009), 57 C.B.R. (5th) 128 (Ont. S.C.J.); and U.S. Steel Canada at paras. 28-33.

[68] In *Walter Energy* at para. 59, I discussed the *Grant Forest Products* factors, as follows:

a) Is this employee important to the restructuring process?

b) Does the employee have specialized knowledge that cannot be easily replaced?

c) Will the employee consider other employment options if the KERP is not approved?

d) Was the KERP developed through a consultative process involving the Monitor and other professionals?; and

e) Does the Monitor support the KERP and a charge?

[69] In *Aralez Pharmaceuticals Inc. (Re)*, 2018 ONSC 6980 at para. 30, Justice Dunphy stated that three criterion underlie all of the considerations of key employee retention and incentive programs in insolvency proceedings as discussed in the relevant case law: a) arm's length safeguards, b) necessity, and c) reasonableness of design.

[70] The Monitor has reviewed the terms of the Retention Agreements and has concluded that the terms of the proposed KERP Charge are reasonable in the circumstances and customary in similar *CCAA* proceedings. The Monitor has also confirmed that the KERP will provide stability for MEC's business operations, particularly in the critical time period when MEC is attempting to stabilize its operations and, if the SAVO is granted, working to finalize the final negotiations with Kingswood, leading to a closing of that transaction. The Lenders have confirmed they are agreeable to the KERP and the KERP Charge as well.

[71] I accept the Monitor's assessment and conclusions with respect to the KERP. I conclude that the KERP is reasonable and necessary in the circumstances and I exercise my discretion to approve the KERP and grant the KERP Charge.

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The Stay

[72] Clearly, an extension of the stay is necessary to allow MEC's restructuring efforts to continue, whether the SAVO is granted or not.

[73] No stakeholder objects to MEC's application for the ARIO, including an extension of the stay of proceedings. The Monitor confirms its view that MEC is acting in good faith and with due diligence.

[74] I am satisfied that an extension of the stay is appropriate until November 3, 2020, in accordance with s. 11.02 of the *CCAA*.

SISP/SAVO

[75] The main focus on this application has been in relation to MEC's application for the granting of the SAVO in favour of Kingswood, pursuant to s. 36(1) of the *CCAA*. Section 36(3) of the *CCAA* lists the relevant non-exhaustive factors to be considered:

> (a) whether the process leading to the proposed sale or disposition was reasonable in the circumstances;
>
> (b) whether the monitor approved the process leading to the proposed sale or disposition;
>
> (c) whether the monitor filed with the court a report stating that in their opinion the sale or disposition would be more beneficial to the creditors than a sale or disposition under a bankruptcy;
>
> (d) the extent to which the creditors were consulted;
>
> (e) the effects of the proposed sale or disposition on the creditors and other interested parties; and
>
> (f) whether the consideration to be received for the assets is reasonable and fair, taking into account their market value.

[76] Mr. Harding, Plateau and Midtown all seek an adjournment of MEC's application for the SAVO for "at least" two weeks. Plateau and Midtown also seek orders that would allow them to obtain further document discovery and cross-examine MEC's deponents, including Mr. Arrata and Mr. Robert Wallis. The parties seeking an adjournment are supported by the BC Co-op Association and Cooperatives and Mutuals Canada (the "Co-op Associations").

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[77] I address the arguments advanced against MEC's application for the SAVO below. There is considerable overlap and interrelationship between the various categories below, so they should be read as a whole.

i) The Kingswood Sale Agreement

[78] MEC describes the key aims and elements of the Sale Agreement as:

a) Kingswood will continue to operate the business as a going concern under a similar name to MEC and will maintain the goodwill of the retail business;

b) the purchased assets comprise almost all of the assets currently used by MEC for the business;

c) Kingswood will retain at least 75% of the active employees of MEC;

d) Kingswood will acquire, or assume, the leases for at least 17 of MEC's retail locations. For those leases not being acquired or assumed, MEC has already or will provide disclaimers to the landlords;

e) Kingswood will assume liabilities including with respect to warranties, existing gift cards (estimated $13.2 million) and employees who accept offers of employment (estimated $2 million);

f) In order to protect goodwill with existing suppliers and contractors, Kingswood will assume liability for payments to certain inventory and other key vendors and suppliers (estimated $25 million) and will seek assignment of certain contracts; and

g) The Sale Agreement is not conditional on any financing or third-party approvals.

[79] The Court has had the benefit of reviewing certain confidential documents arising from the SISP, including the unredacted Sale Agreement and Confidential Appendix C to the First Report that were both filed under seal in this proceeding.

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[80] Significantly, the Sale Agreement provides for a sale price (base amount of $120 million, subject to certain adjustments) that will repay the Lenders in full, maximize the ongoing number of operating stores and retention of a majority number of employees, and leave MEC with additional funds to support a *CCAA* plan that would see a distribution to unsecured creditors. The Board and Special Committee consider that the Kingswood offer was consistent with the guiding principles of the SISP as had been earlier established.

[81] I have reviewed the details of the other three bids received and reviewed by the Special Committee and MEC's Board prior to acceptance of Kingswood's offer. I agree that the Kingswood offer is clearly the most advantageous one, both in terms of price, continuity of business operations, retention of stores, retention of employees and assumed liabilities.

ii) The Monitor Issue

[82] As part of Plateau's objection to the SAVO, it seeks an order replacing A&M as Monitor with Ernst & Young Inc., pursuant to s. 11.7(3) of the *CCAA*.

[83] Plateau argues that, since A&M Securities, A&M's affiliate, was involved in the SISP, A&M is not appropriate to continue as Monitor in these proceedings. Plateau argues that, in the circumstances, the Monitor cannot opine on the adequacy of the SISP as required under s. 36(3)(b) of the *CCAA*.

[84] I will note at the outset that no one on this application, let alone Plateau, questions the professionalism of A&M. Rather, Plateau asserts that there is a perception of bias in respect of the Monitor's views of the SISP, which cannot stand in the face of the clear requirement that a monitor be independent and impartial while exercising its fiduciary obligations to all stakeholders. Plateau cites various authorities including: *United Used Auto & Truck Parts Ltd. (Re)*, [1999] B.C.J. No. 2754 at para. 20 (S.C.); *Winalta Inc. (Re)*, 2011 ABQB 399; *Can-Pacific Farms Inc. (Re)*, 2012 BCSC 760; and *Walter Energy Canada Holdings Inc. (Re)*, 2017 BCSC 53 at paras. 24-25.

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[85] I have reviewed the terms of A&M Securities' engagements with MEC. As counsel note, s. 11.7(2) of the *CCAA* provides restrictions on who may be a monitor. A&M clearly did not fall within that restricted list and was able to accept an appointment as Monitor when the Initial Order was granted.

[86] Under the February 10, 2020 engagement, A&M Securities was providing consulting services with respect to identifying potential financing. A&M Securities' compensation was a fixed fee with hourly rates after a certain time period. I am unable to discern any conflict between that engagement and A&M's current one as Monitor that causes any concern.

[87] Similarly, the A&M Securities' June 10, 2020 engagement with MEC also provided for consulting services in respect of the SISP, also on an hourly basis.

[88] It is apparent that, by June 2020, MEC foresaw that it may be necessary to file under the *CCAA* in order to resolve the significant financial difficulties it faced. In the second engagement with A&M Securities, MEC specifically addressed that potential step. Paragraph 4 of the June 10, 2020 engagement agreement provided that MEC could choose to put A&M forward as the Monitor. MEC and A&M expressly agreed that no conflict would arise between the second engagement and that potential appointment. As the Monitor notes, this type of pre-planning for a potential monitor appointment is typically undertaken since it allows a debtor to seamless and efficiently transition into the restructuring process while taking advantage of efforts begun even prior to that time.

[89] Plateau places great emphasis on the reasoning and result found in *Nelson Education Ltd. (Re)*, 2015 ONSC 3580. In that case, Newbould J. considered an application to replace the monitor where the monitor was recommending a sale. The monitor had been a financial advisor to the company for two years prior to its appointment, and it had conducted a SISP prior to the *CCAA* filing that involved dealings with the second lien holders. Almost immediately after the filing, the debtor sought approval to sell the assets to the first lien holders, leaving nothing for the second lien holders.

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[90] Justice Newbould found that replacement of the monitor was necessary since firstly, the monitor was in no position to comment independently on the validity of the SISP and, secondly, there was an appearance of a lack of impartiality:

> [30] The problem is that Nelson has proposed a quick court approval of a transaction in which the first lien lenders will acquire the business of Nelson and in which essentially all creditors other than the second lien lenders will be taken care of. Nelson has asserted in its material that the SISP process undertaken by Nelson prior to the *CCAA* proceedings has established that there is no value in the Nelson business that could give rise to any payout to the second lien lenders. The SISP process was taken on the advice of A&M and under their direction. It was put in Nelson's factum that:
>
> > The Applicants, with the assistance of their advisors, conducted a comprehensive SISP which did not result in an executable transaction that would result in proceeds sufficient to repay the obligations under the First Lien Credit Agreement in full or would otherwise be supported by the First Lien Lenders;
>
> [31] Nelson intends to request Court approval of the proposed transaction. An issue that will be front and centre will be whether the SISP process prior to this *CCAA* proceeding can be relied on to establish that there is no value in the security of the second lien lenders and whether other steps could have been taken to obtain financing to assist Nelson in continuing in business other than a credit bid by the first lien lenders. A&M was centrally involved in that process. It is in no position to be providing impartial advice to the Court on the central issue before the Court.

[91] A&M Securities' involvement with MEC was clearly in the context of finding a solution to MEC's financial difficulties in the short term. It is common ground that MEC could most likely have obtained *CCAA* protection in early 2020 and then conducted the search for financing and/or the SISP within those proceedings. MEC states that it had good reason not to obtain court protection at that time, as I will discuss later in these reasons. This is a distinguishing factor from *Nelson Education*, where the monitor had a much more extensive and historical relationship with the debtor and other stakeholders.

[92] Further, I can discern no conflict, whether real or apparent, arising from A&M Securities' previous involvement. Importantly, there is no success fee or compensation built into the second engagement that could possibly stand as an incentive for the Monitor to recommend the Kingswood sale (or any other sale) for

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approval. Unlike *Nelson Education*, this is not a case where only one secured creditor is apparently benefitting from the proposed transaction. The Sale Agreement will benefit all the stakeholders generally, although in different degrees given their different priorities. Although clearly hindsight, I note that Newbould J. later approved the proposed transaction (*Nelson Education Ltd. (Re)*, 2015 ONSC 5557), about two-and-a-half months later, at no doubt considerable cost to the estate.

[93] In addition, as I will discuss in more detail below, there would be considerable cost and delay in replacing the Monitor at this time. The monitor engagement for MEC is not a simple affair and any new firm would take some time to fully assume that role and prepare a report – likely not even within "at least" two weeks, the delay sought by the objecting parties. Time is not on MEC's side in these urgent circumstances. See *Can-Pacific Farms* at para. 26.

[94] Finally, the s. 36(3)(b) factor – the monitor's approval of the process – is only one of the relevant factors that the court is to consider, among others. None of the s. 36(3) factors have primacy in respect of the court's consideration as to whether a sale should be approved. The previous involvement of the Monitor with MEC is a consideration, however, not a controlling one.

[95] Every sale approval application will be fact intensive toward ensuring that any proposed sale is fair and reasonable, after an appropriate sales process.

[96] I have no concerns arising from A&M's affiliate acting as MEC's financial advisor in the months leading to this proceeding. I decline to exercise my discretion to replace A&M as Monitor in these proceedings.

iii) The SISP

[97] Plateau and Midtown question the appropriateness of MEC filing for *CCAA* protection after having conducted the SISP. They say that the *CCAA* is being improperly used to approve a "quick slip sale" arising from a process that took place outside of the Court's supervision, without the Court's approval and without consultation with MEC's stakeholders.

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[98] MEC began taking steps toward finding a solution to its financial difficulties many months before the *CCAA* filing. MEC asserts that, while the Court did not pre-approve the SISP, the SISP was extensive and properly canvassed the market to identify the best and highest value for its business.

[99] As the parties note, this is a classic “pre-packaged” proceeding, or “pre-pack”, as it is colloquially known. As in many previous *CCAA* proceedings, most of MEC’s restructuring efforts have taken place before the filing of the court proceeding, and the most obvious restructuring path presented now by MEC is the sale to Kingswood arising from the SISP.

[100] There is nothing inherently flawed in a “pre-pack” approach. There are often good reasons why a debtor company may choose such a course of action, more often than not arising from the real or perceived threats or disruptions to a business by pursuing options within a proceeding. The Monitor confirms its own experience and views in that respect, particularly relating to retail operations where it is critical to preserve going concern value.

[101] Here, MEC contends it ran the SISP prior to any *CCAA* proceedings to maintain stability in its business and to promote a going concern solution, all as supported by the Lenders, who were increasingly concerned about their credit exposure in light of the financial crisis faced by MEC. I readily accept that running a retail operation within *CCAA* proceedings, particularly with the uncertainty in the marketplace, both from a general economic view and by reason of the pandemic, would give rise to risk and potential disruption to future operations. I also accept that MEC had good reason to seek to avoid further risks and disruptions to its operations, given its already fragile economic state.

[102] Similar circumstances were considered in *Sanjel Corp. (Re)*, 2016 ABQB 257, where a SISP conducted outside of the proceedings was challenged. In that case, the SISP was conducted by a financial advisor for about four months prior to the *CCAA* filing. At that time, the accounting firm was identified as the potential monitor

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and, when later appointed as monitor, recommended court approval of the sale that arose through the SISP.

[103] Justice Romaine discussed the concerns that arise where a court is presented with a "pre-pack" where court approval of a sale that arose from a pre-filing SISP is sought. Her comments are apt here and I would adopt them:

> [70] A pre-filing SISP is not of itself abusive of the *CCAA*. Nothing in the statute precludes it. Of course, a pre-filing SISP must meet the principles and requirements of section 36 of the *CCAA* and must be considered against the *Soundair* principles. The Trustee submits that such a SISP should be subject to heightened scrutiny. It may well be correct that a pre-filing SISP will be subject to greater challenges from stakeholders, and that it may be more difficult for the debtor company to establish that it was conducted in a fair and effective manner, given the lack of supervision by the Court and the Monitor, who as a court officer has statutory duties.
>
> [71] Without prior court approval of the process, conducting a SISP outside of the *CCAA* means that both the procedure and the execution of the SISP are open to attack by aggrieved stakeholders and bitter bidders, as has been the case here. Any evidence or reasonable allegations of impropriety would have to be investigated carefully, whereas in a court-approved process, comfort can be obtained through the Monitor's review and the Court's approval of the process in advance. However, in the end, it is the specific details of the SISP as conducted that will be scrutinized.

[104] Justice Romaine's reasoning was followed by this Court in *Feronia Inc. (Re)*, 2020 BCSC 1372 where Justice Milman accepted the proposal trustee's recommendation in support of a sale achieved through a pre-filing sales process (paras. 50-57). The proposal trustee's affiliate firm had been engaged to assist with that sales process.

[105] The court's comments in *Sanjel* about a pre-filing SISP being more open to attack is certainly evident here.

[106] I will now address the actual financing and SISP process in more detail. Evidence of MEC and A&M Securities' efforts is found in Mr. Arrata's evidence as was supplemented by Mr. Wallis' evidence. Mr. Wallis is a MEC director and Chair of the Special Committee. The Monitor also addresses the financing and SISP process in its First Report.

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[107] A&M Securities was engaged to secure new financing in February 2020, principally to replace the Credit Facility which was approaching maturity. Unfortunately, the pandemic wrought havoc with those efforts and MEC quickly moved to form a committee to address those issues. That informal committee was formally constituted as the Special Committee on March 27, 2020 with its mandate to pursue a broad range of strategic alternatives.

[108] Although the financing options being pursued were not successful, it was not for want of effort. The steps that A&M Securities designed to seek the financing, as listed above, can only be described as typical. Government aid programs were considered. Approximately 66 lenders were contacted; the listing of those lenders indicates a broad range of lending institutions, including two co-operatives. A May 12, 2020 term sheet provided to RBC by one lender was considerably below what the Lenders were owed and required first priority security that was not a realistic request from the Lenders' point of view given the financing amount.

[109] Mr. Harding, supported by the Co-op Associations, asserts that MEC could have asked its members for the necessary funding. Mr. Wallis addresses that matter, stating that the Special Committee considered but then rejected that option as impractical. In my view, his reasons are amply supportable and are reasonable in the circumstances: a public plea for such funding was unlikely to garner the very substantial amounts needed to repay the Lenders, even if it could be achieved, which was questionable, while creating negative impacts on MEC's business in the meantime.

[110] Finally, the Special Committee considered that the Lenders were very unlikely to grant an extension of the Credit Facility, without significant improvement in MEC's financial performance that, in the teeth of the pandemic, appeared also very unlikely.

[111] Having exhausted refinancing efforts, the Special Committee and the Board had no choice but to then consider a sale. After interviewing other financial advisors, the Special Committee decided that it was in MEC's best interests to continue with A&M Securities under the SISP, given its expertise and experience with MEC.

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[112] Again, the Special Committee and the Board expressly considered whether the SISP should be conducted prior to any *CCAA* proceeding. They decided to do so in order to avoid the likelihood of a distressed-assets sale situation and to preserve MEC's relationships with vendors, customers and service providers with respect to its ongoing business operations in order to preserve going concern value.

[113] As with the refinancing efforts, A&M Securities' design of the SISP included the usual features (as listed above), in that it was structured and implemented in the same or similar manner as is typically done in a SISP in the course of *CCAA* proceedings. No party appearing on this application contended that the SISP steps were inappropriate or lacking, resting on the contention only that they weren't consulted in its implementation.

[114] The list of persons contacted was extensive, including Canadian and US private investment firms, retail conglomerates and even REI, a US co-operative that was in fact the inspiration for MEC in the first place. As stated above, Kingswood's bid was clearly the best bid of the four that MEC received.

[115] The Lenders' support, including under the Interim Financing, is premised on MEC seeking approval of the Kingswood transaction. I note this as a factor, although the Lenders' support is not surprising since the proposed transaction will generate sufficient funds to pay the Lenders in full. The Monitor's liquidation analysis would also suggest that the Lenders would be paid in full under that scenario.

[116] Another relevant factor in the Court's consideration of the adequacy of the SISP is the level of oversight throughout the process.

[117] The Special Committee and MEC's Board, both comprised of well-qualified and experienced business professionals, oversaw A&M Securities' efforts. Both Mr. Arrata and Mr. Wallis fully endorse those efforts as having produced the very best alternative for MEC in the circumstances. I have no reason to question their commercial and business judgment: *AbitibiBowater Inc.*, 2010 QCCS 1742 at para. 71. Mr. Wallis confirms that, despite rumours in the community, no MEC Board

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members are receiving any incentives or compensation in respect of the Kingswood transaction. Further, the process was reviewed by the Lenders and their experienced professional advisors, again without objection.

[118] In my view, it is not surprising in the circumstances that the Monitor supports the SISP efforts as being sufficiently robust in the circumstances, particularly with its usual features and oversight. The Monitor states that the SISP is likely consistent with what the Monitor would have recommended in a court-supervised process, with which I agree. It is also worth emphasizing that the entire SISP process from June-September 2020 ran over a 100 day period, hardly a rushed process (i.e., even well beyond the "aggressive timelines" approved in *Sanjel* at paras. 75-77).

[119] I conclude that the SISP was a competitive process, was conducted in a fair and reasonable manner and adequately canvassed the market for options available to MEC.

iv) Harding / Co-Operative Association Issues

[120] Mr. Harding is the spokesperson for the steering committee of the "SaveMEC" campaign, involving who he describes as a "highly motivated, well organized group of Members, seeking to preserve MEC's status as a cooperative association with an operating business". They have been assisted through various online efforts, suggesting support from some 140,000 individuals, and contributions from 2,500 persons toward a legal fund of over $100,000. As I noted on October 2, 2020, the passion of the "SaveMEC" group members is evident, as it was with MEC's original founders.

[121] Like Plateau and Midtown, Mr. Harding seeks an adjournment of "at least" two weeks. He suggests that his group would like to explore opportunities to address MEC's liquidity crisis in the short term. He says that the very short notice given to MEC members in respect of these proceedings is challenging in terms of identifying alternatives; MEC gave notice to its members of this proceeding on September 14, 2020. Mr. Harding is supported in his submissions by the Co-op Associations' counsel.

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[122] Mr. Harding indicates some “definitive” sources of funding have already been identified by his group. Unfortunately, none even come close to resolving the very significant financial issues faced by MEC, particularly given the amounts owing to the ever increasingly concerned Lenders who are owed in excess of $80 million in a very uncertain retail environment, MEC’s ongoing losses and MEC’s required working capital.

[123] Mr. Harding’s most significant complaint against the SAVO is that the members will “lose” their substantial financial interest in MEC through their membership. He points to MEC’s February 2020 balance sheet that indicated the book value of members’ shares was in excess of $192 million.

[124] In my view, this argument has little merit. Each MEC member only stands to “lose” their $5 investment, although I appreciate that collectively, the investment is significant. Based on the evidence presented on this application, the best bid which was received from Kingswood is not sufficient to repay the unsecured creditors in full, let alone provide for any return to MEC’s members. Accordingly, assuming the SISP has produced the best financial result in the circumstances, which I accept, MEC members have no real financial interest at this time.

[125] I appreciate that Mr. Harding only seeks a short period of time to confirm whether other more advantageous options are available. This argument also is not persuasive. I consider that the chances of SaveMEC coming up with an option within two weeks to stave off the Lenders, secure funding the cover the losses and necessary working capital and pay the unpaid creditors to be an extremely outside one, however sincere that intention and those efforts may be.

[126] I completely disagree with Mr. Harding that there is no prejudice to MEC, Kingswood or the Lenders if the sale is delayed until his group has a chance to investigate other options. As Mr. Wallis states in his Affidavit, set out below, there is significant prejudice to MEC and its stakeholders in terms of delay, cost, ongoing losses and deal risk. Mr. Harding’s group is risking nothing at this point; to the contrary, other broad stakeholder interests are very much “in the money” under the

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Kingswood transaction in the sense of it providing recovery to creditors and preserving jobs and business relationships.

[127] I note that the broad stakeholder group who Mr. Harding seeks to represent includes many MEC members who stand to preserve their jobs and redeem the significant value in gift certificates, all by reason of the Kingswood sale.

[128] Mr. Harding also asserts that these *CCAA* proceedings must be conducted in a manner that respects the fundamental freedom of MEC members, namely the "freedom of association", that arises under s. 2(d) of the *Charter of Rights and Freedoms* (the "*Charter*").

[129] It is unusual to face *Charter* arguments in commercial matters or even *CCAA* proceedings. That said, I accept Mr. Harding's submissions that co-operatives provide important social and community benefits and that the right to join a co-operative and exercise collective rights through that means goes to the root of the protection offered by s. 2(d): *Mounted Police Association of Ontario v. Canada (Attorney General)*, 2015 SCC 1 at para. 54, citing *Reference re Public Service Employee Relations Act (Alberta)*, [1987] 1 S.C.R. 313. MEC is clearly an example of the exercise of that right, leading to it being, as Mr. Harding asserts, the largest co-operative in Canada.

[130] I cannot see, however, that MEC seeking court protection in its present circumstances offends any rights arising under s. 2(d) of the *Charter*. As MEC's counsel states, the *Charter* does not protect against an organization incurring losses and finding itself in insolvent circumstances, even if the organization is a co-operative.

[131] No one, including Mr. Harding, disputes that MEC qualified to seek court protection under the *CCAA*. Rather, he asserts that MEC members must be able to exercise their democratic right to shape the future of MEC, and particularly, he argues that any decision to sell MEC's assets cannot be made without the approval of MEC's members. The *Co-op Act*, s. 71(2), and MEC's Rules of Co-operation

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(8.11) both provide that a sale of the whole or substantially the whole of the co-operative's undertaking requires a special resolution of the members.

[132] Mr. Harding's complaint that the members have been unfairly and oppressively denied participation in this important decision to sell MEC's assets is understandable; however, it but does not change the fact that such participation is a very unwieldly step, particularly with the pandemic, it would delay matters where urgency is required, and its relevance is questionable in any event given that the best evidence is that the members have no financial interest in MEC.

[133] I disagree with counsel for the Co-op Associations that the application of the *CCAA* in the face of the *Co-op Act* is an "unsettled area of law". Cooperatives are able to avail themselves of the *CCAA* if they are insolvent and they otherwise meet the statutory requirements.

[134] The *CCAA* expressly recognizes that participation by corporate shareholders (the equivalent of MEC's members here) toward approving a sale of the assets, is not a requirement before the court can exercise its jurisdiction under s. 36(1):

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

[135] Mr. Harding suggests that MEC's affairs are being conducted in an oppressive manner by this attempt to sell MEC's assets without member approval. I see no utility in embarking upon an analysis of the oppression remedy under s. 156 of the *Co-op Act* in the present circumstances, although I would hasten to add that no such court ordered relief has been formally sought. Mr. Harding refers to the comments of this Court in *Radford v. MacMillan*, 2017 BCSC 1168, aff'd 2018 BCCA 335, concerning the assessment of reasonable expectations in the oppression analysis. In this Court in *Radford*, Justice Masuhara stated that expectations must be "realistic": para. 119.

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[136] I hardly think the MEC members could conceivably realistically consider that they, and they alone, would dictate whether a sale would occur, when the co-operative is insolvent and their memberships presently have no value.

[137] It is unfortunate that Mr. Harding appears to be singularly focussed on preserving MEC as a co-operative entity to continue its business. Given the co-operative principle of "concern for community" embraced by MEC as part of its DNA, the "SaveMEC" campaign group and the Co-op Associations might have given some consideration to the fact that the Kingswood sale will benefit many persons in the community. The sale will ensure ongoing employment to most MEC employees, the maintenance of business relationships which support other jobs and repayment of at least some portion of the debt that MEC owes to its many unsecured creditors.

[138] Mr. Harding's application for an adjournment is dismissed.

v) Disclaimed Lease Issues

[139] Plateau and Midtown both seek an adjournment of MEC's application for the SAVO for "at least" two weeks. In addition, both seek an order that MEC produce substantial further documents in relation to the refinancing and sale efforts. Finally, they seek to cross-examine Mr. Arrata and Mr. Wallis on their affidavits.

[140] Plateau and Midtown's objection to the SAVO derives from the extremely unfortunate circumstances that arise from MEC's disclaimer of their store leases (in Calgary North West and Saskatoon respectively).

[141] In its petition materials, MEC has earlier identified that the Sale Agreement with Kingswood did not include an assignment of three leases, including those for the Saskatoon and Calgary North West stores. The Saint-Denis store had already been permanently closed; the Saskatoon and Calgary North West stores had not yet opened.

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[142] In Mr. Arrata's Affidavit #1 sworn September 13, 2020, he stated that MEC expected to be disclaiming those leases, with the approval of the Monitor, in accordance with s. 32(1) of the *CCAA*.

[143] As forecast, after the Initial Order was granted, on September 15, 2020, MEC issued notices of intention to disclaim or resiliate all three leases. The Monitor approved these disclaimers in order to "reduce costs and downsize redundant operations". On September 22, 2020, MEC provided its reason for the disclaimer of Plateau's lease, citing its liquidity crisis, that Kingswood had decided not to acquire the leases and that the disclaimer was necessary to enhance the prospects of a viable compromise. The same considerations apply to Midtown's lease.

[144] In the First Report, the Monitor stated that it is also of the view that the disclaimers will enhance the prospect of a viable arrangement and further the restructuring of MEC, as contemplated by the Kingswood Sale Agreement.

[145] On September 30, 2020, Plateau filed a Notice of Application to prohibit the disclaimer of its lease by the deadline, and I assume that Midtown has done likewise.

[146] I agree that both Plateau and Midtown face challenging economic circumstances themselves by reason of the disclaimers. Both landlords have expended substantial sums of money in outfitting their developments for MEC, who was to have been the anchor tenant. Both landlords will suffer significant losses in respect of lost rental revenue and any indirect benefits that might have been derived by MEC's presence in their developments.

[147] Based on my conclusions that the SISP was fair and reasonable in the circumstances, I reject these landlords' request for any delay in approving the Kingswood sale and decline to exercise my discretion to do so. I see no reasonable prospect that these landlords will be in any better position after a delay of two weeks. I also see no need for further document production beyond the

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documentation that MEC provided on September 26, 2020 in response to Plateau and Midtown's applications.

[148] Kingswood's decision not to take up these leases was made independently of MEC and, on the face of things, aligns with what Kingswood envisions by way of its future operations. The Sale Agreement provides for a *contraction* of MEC's operating stores to at least 17 locations; in that event, it hardly makes business sense that, at the same time, Kingswood would also agree to incur the considerable expense of fixturing, outfitting, staffing and supplying one or two *new* locations. None of the other three bidders expressed any interest in these locations either.

[149] As with Mr. Harding's argument, I also reject Plateau and Midtown's assertions that little or no prejudice arises from any adjournment. To the contrary, the unsecured creditor pool will be enhanced by an expeditious sale which obviates any further weekly losses being incurred by MEC. These landlords stand to gain by that enhanced pool of money in respect of their claims that will no doubt be filed, claims that will not increase whether or not the SAVO is granted. Plateau and Midtown have solely focussed on process issues, to the exclusion of other interests at play. They have failed to justify their position.

[150] Plateau and Midtown's arguments appear to conflate MEC's application for the SAVO with their right to contest the disclaimers. They suggest that, effectively, no sale can be considered by the court until the disclaimer issue is determined. No authority was cited in support for this proposition. Indeed, the sale application might just as easily have been considered and the Kingswood sale approved even before any disclaimer notice was issued.

[151] As MEC's counsel notes, MEC decided to be forthright from the outset in signalling this very bad news to these landlords.

[152] I appreciate that granting the SAVO to allow a sale of substantially all of MEC's assets to Kingswood can be interpreted as effectively determining the disclaimer issue. It will be difficult for the landlords to argue that the disclaimer

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should be prohibited so as to allow MEC, which no longer operates its business, to take up the lease.

[153] However, this ignores the simple reality of the situation. MEC cannot force a buyer to take up these leases. In addition, MEC's dire financial circumstances, as revealed on this application, would hardly have supported a business decision to start up these stores even if the SAVO is not granted. There is no realistic chance that the Lenders would support such an endeavour under the Credit Agreement. Further, I see no basis upon which this Court would effectively require MEC to spend millions of dollars on these new stores under its *CCAA* jurisdiction. It is difficult to imagine that this Court would, in balancing the various interests at play in relation to the benefits of the Kingswood sale, require such a result to the detriment of the many stakeholders other than these two landlords.

[154] I would add that five other MEC landlords also appeared on this application. They indicated that they were not opposed to the granting of the SAVO or were not taking any position. I suspect that they are all hoping that their store locations will be viewed favourably by Kingswood when the at least 17 store "winners" are chosen to continue operations. If any of them are not in the "winner" category, any losses will be added to the unsecured creditor group to share in the net recovery under the Kingswood sale.

[155] Plateau and Midtown's applications for an adjournment, document discovery and cross-examination of Mr. Arrata and Mr. Wallis are dismissed.

vi) Should the Kingswood Transaction be Approved?

[156] The Court's approach in considering a proposed sale under s. 36 of the *CCAA* is informed by the *CCAA*'s statutory objectives, as was discussed in *Century Services Inc. v. Canada (Attorney General)*, 2010 SCC 60.

[157] The main objective is to avoid, if possible, the devastating social and economic costs of a liquidation of a debtor's assets: *Century Services* at para. 15. In achieving these remedial goals, the court must be cognizant of the various interests

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at stake, including the debtor, the creditors, employees, counterparties, directors and shareholders: *Century Services* at paras. 59-60. As evident from my discussion above, many of those stakeholder interests were represented on this application and expressed their views. However, the court must also recognize and give effect to, to the extent possible, all stakeholder interests whether present on this application or not.

[158] As with many applications for relief under the *CCAA*, the Court must strive to balance what are often competing interests and objectives. That exercise is often within the rubric of the need to conclude that the relief is "appropriate". Appropriateness is assessed by inquiring whether the purpose of the order sought and the means it employs advances the statutory objectives or remedial purpose of the *CCAA*. As Justice Deschamps stated in *Century Services* at para. 70, the chance of achieving that goal is enhanced when "all stakeholders are treated as advantageously and fairly as the circumstances permit" [Emphasis added.]

[159] The relevant factors to be balanced and considered under s. 36(3) are reflective of a consideration of what can be, and is on this application, a broad range of interests.

[160] I have concluded that the refinancing efforts and the SISP were conducted in a fair and reasonable manner. There is no basis upon which to second guess the adequacy of the substantial efforts that were made by the Board, the Special Committee and A&M Securities in that respect.

[161] The Kingswood transaction that arose from that competitive process was clearly the best from the few bids that were received. All other bids paled in comparison, particularly in relation to the purchase price and commitments to ongoing store operations and employee retention. As noted in the Monitor's First Report, the consideration that MEC will receive is substantial. While the base purchase price is $120 million, the total indicative purchase price is actually $150 million, after accounting for the substantial liabilities that Kingswood will

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assume in respect of vendor trade payables, employee obligations and gift card obligations.

[162] The process conducted outside of this *CCAA* proceeding was not a rushed affair. I accept that many of the stakeholders on this application consider that they have been ignored or disadvantaged by reason of the lack of prior consultation and the short notice given to them to respond to this application. In my view, MEC has provided reasonable and understandable explanations for proceeding in that manner. The Monitor provides further support in the First Report in stating that to proceed otherwise would have created significant uncertainty and disruption in MEC's day to day business and put MEC's business operations and a potential going concern sale at unnecessary risk.

[163] As the Monitor notes, the perfect financial storm faced by MEC, still exacerbated by the risks posed by the ongoing pandemic, does not give MEC the luxury of time here. What is needed is a timely solution, after, of course, the Court has fully reviewed the evidence and is satisfied that the requested relief is appropriate. There is no evidence to suggest that MEC's Board or Kingswood have manufactured the need for what is described as urgent relief by approval of the SAVO.

[164] I have also concluded that, although some minor delay could be accommodated with the time limits under the Restructuring Agreement and the Sale Agreement, the perceived benefits do not outweigh the risks that follow. I accept the evidence of Mr. Wallis as to why it is urgent to approve the Sale Agreement as soon as possible. He states:

> 45. [MEC] believe[s] that the approval of the Sale Agreement is a matter of urgency. Any extension or delay in obtaining Court approval and Closing may have serious and detrimental consequences for its business and stakeholders, including, but not limited to, its employees, members and suppliers. This is particularly the case given the extent of [MEC's] ongoing weekly operating losses, as shown in [MEC's] Cash Flow Forecast, and the importance that any potential purchaser of the Business would have to close this transaction in sufficient time to take advantage of the coming holiday sales period.

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> 46. The projections reflect an erosion of the borrowing base under the Interim Financing Facility and cash availability becomes very tight under the borrowing base calculation towards the end of October. It is therefore imperative that matters progress as quickly as possible so that MEC's customers, suppliers, landlords and employees have confidence that MEC will continue as a successful going concern.
>
> 47. Given the recent rise in COVID-19 transmissions across Canada, there is also a real and unpredictable risk that increased COVID-19 rates and/or restrictions would result in further deterioration in sales below those set out in the Updated Cash Flow Forecast provided by the Monitor, which would in turn jeopardize the availability of the Interim Financing Facility or ability to meet the closing condition of requiring repayment of the Credit Facility. The Lenders have confirmed they require a timely completion of the Transaction.

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[165] The work to be done to conclude all matters under the Sale Agreement and move toward a closing of the transaction will no doubt be complex and take some time. Many contractual matters need to be concluded by Kingswood with stakeholders, such as employees, landlords and suppliers, in advance of the closing. As noted by MEC and the Monitor, it is critical to the success of the ongoing business that the transaction close as soon as possible so that Kingswood can order additional inventory in advance of the "Black Friday" and holiday shopping season. Kingswood is able to close the transaction by mid-late October 2020.

[166] The Monitor has also conducted a liquidation analysis to compare the results of the Kingswood sale to that which might be achieved by an orderly liquidation of MEC's assets through a bankruptcy and/or receivership. Under the Kingswood sale, estimated recovery to unsecured creditors is between $0.30-50 on the dollar; in a liquidation, estimated recovery to unsecured creditors is between $0.30-60 on the dollar. What is significant as between these two scenarios, however, is that in a liquidation, there would be far greater creditor claims.

[167] The Kingswood sale avoids the devastating impact of a liquidation on employee's jobs, preserves many of the leases, trade supply agreements and service agreements, and provides value to many unsecured creditors by Kingswood's full assumption of liabilities. These latter considerations figure greatly in the Court's decision as to whether a sale should be approved. That decision is made

toward achieving the main statutory objectives under the *CCAA* which are to allow the business to continue, with all the economic, societal and community benefits that that option affords. Many of the indirect benefits are unquantifiable.

[168] I agree with the Monitor that, in all the circumstances, the Kingswood sale is commercially reasonable and, on balance, is more beneficial to MEC's stakeholders, and particularly its creditors, than any other alternative. I grant the SAVO on the terms sought.

Representative Counsel

[169] Mr. Harding also sought an order under s. 11 of the *CCAA* that Victory Square Law Office be appointed as representative counsel for MEC's members. He also sought a charge of $100,000 under s. 11.52 of the *CCAA* to secure anticipated fees in respect of participation, ranking behind the four court-ordered charges but ahead of the Lenders' security.

[170] I conclude that this relief might have been more seriously considered if there was any indicative value held by the MEC members and, if these proceedings had taken a different path where the members' interests were in play.

[171] Having concluded that the Kingswood sale should be approved, which will divest MEC of substantially all of its assets in the short term, I see little utility in granting this relief. As I discuss above, this sale will garner some net proceeds for the unsecured creditors, leaving no recovery for MEC's members.

[172] I would add that the Kingswood sale does not mean that MEC will cease to exist as a co-operative. It may be that MEC's members can still consider whether any options remain for them in that respect, particularly if a plan is approved and successfully executed to leave the co-operative intact in a legal sense but without the burden of any debt and, of course, with few assets.

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[173] Mr. Harding is, of course, welcome to continue to participate in these proceedings on behalf of the “SaveMEC” group, as he wishes, which I assume can be done with counsel given the funds already raised.

[174] Mr. Harding’s application for appointment of representative counsel and a related charge is dismissed.

FINAL THOUGHTS

[175] I accept that this decision is a disappointing conclusion to the fate of what was an iconic Canadian retailer who has inspired the passion and commitment of many Canadians for outdoor activity. Like many Canadian retailers, MEC has fallen victim to economic forces, and perhaps questionable business judgments made years ago, all exacerbated by the cataclysmic and unprecedented impact of the COVID-19 pandemic throughout most of 2020.

[176] This result, however, will ensure the continuation of MEC’s business, albeit in another organization. While this sale transaction is not wrapped in the Canadian flag, the best evidence is that Kingswood will continue to support MEC’s core values and principles, being community engagement and promotion of a healthy outdoor lifestyle. More importantly, the ongoing operations will support Canadian individuals and their families and also businesses where jobs are disappearing quickly given ongoing economic disruptions. Creditors will be paid, or paid a substantial portion of what they are owed, no doubt to the relief of many.

[177] This is the core objective under a *CCAA* proceeding, and while that objective was not achieved here in a perfect manner, it was still achieved in a reasonable manner. That is all that anyone can ask.

“Fitzpatrick J.”

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IN THE SUPREME COURT OF BRITISH COLUMBIA

Citation: *Walter Energy Canada Holdings, Inc. (Re),* 2016 BCSC 107

Date: 20160126
Docket: S1510120
Registry: Vancouver

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

And

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

And

In the Matter of a Plan of Compromise or Arrangement of Walter Energy Canada Holdings, Inc. and the Other Petitioners Listed on Schedule "A"

Before: The Honourable Madam Justice Fitzpatrick

Reasons for Judgment

Counsel for the Petitioners:	Marc Wasserman Mary I.A. Buttery Tijana Gavric Joshua Hurwitz
Counsel for United Mine Workers of America 1974 Pension Plan and Trust:	John Sandrelli Tevia Jeffries
Counsel for Steering Committee of First Lien Creditors of Walter Energy, Inc.:	Matthew Nied
Counsel for Her Majesty the Queen in Right of the Province of British Columbia:	Aaron Welch
Counsel for Morgan Stanley Senior Funding, Inc.:	Kathryn Esaw

Counsel for KPMG Inc., Monitor:	Peter Reardon Wael Rostom Caitlin Fell
Counsel for Canada Revenue Agency:	Neva Beckie
Counsel for the United States Steel Workers, Local 1-424:	Stephanie Drake
Place and Date of Hearing and Ruling given to Parties with Written Reasons to Follow:	Vancouver, B.C. January 5, 2016
Place and Date of Written Reasons:	Vancouver, B.C. January 26, 2016

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Introduction and Background

[1] On December 7, 2015, I granted an initial order in favour of the petitioners, pursuant to the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36, as amended ("*CCAA*").

[2] The "Walter Group" is a major exporter of metallurgical coal for the steel industry, with mines and operations in the U.S., Canada and the U.K. The petitioners comprise part of the Canadian arm of the Walter Group and are known as the "Walter Canada Group". The Canadian entities were acquired by the Walter Group only recently in 2011.

[3] The Canadian operations principally include the Brule and Willow Creek coal mines, located near Chetwynd, B.C., and the Wolverine coal mine, near Tumbler Ridge, B.C. The mine operations are conducted through various limited partnerships. The petitioners include the Canadian parent holding company and the general partners of the partnerships. Given the complex corporate structure of the Walter Canada Group, the initial order also included stay provisions relating to the partnerships: *Lehndorff General Partner Ltd. (Re)* (1993), 9 B.L.R. (2d) 275 (Ont. Gen. Div.); *Asset Engineering LP v. Forest & Marine Financial Limited Partnership*, 2009 BCCA 319 at para. 21.

[4] The timing of the Canadian acquisition could not have been worse. Since 2011, the market for metallurgical coal has fallen dramatically. This in turn led to financial difficulties in all three jurisdictions in which the Walter Group operated. The three Canadian mines were placed in care and maintenance between April 2013 and June 2014. The mines remain in this state today, at an estimated annual cost in excess of $16 million. Similarly, the U.K. mines were idled in 2015. In July 2015, the U.S. companies in the Walter Group filed and sought creditor protection by filing a proceeding under Chapter 11 of the U.S. *Bankruptcy Code*. It is my understanding that the U.S. entities have coal mining operations in Alabama and West Virginia.

[5] From the time of the granting of the initial order, it was apparent that the outcome of the U.S. proceedings would have a substantial impact on the Walter

Canada Group. A sales process completed in the U.S. proceeding is anticipated to result in a transfer of the U.S. assets to a stalking horse bidder sometime early this year. This is significant because the U.S. companies have historically supported the Canadian operations with funding and provided essential management services. This is a relevant factor in terms of the proposed relief, as I will discuss below.

[6] The Walter Canada Group faces various significant contingent liabilities. The various entities are liable under a 2011 credit agreement of approximately $22.6 million in undrawn letters of credit for post-mining reclamation obligations. Estimated reclamation costs for all three mines exceed this amount. Further obligations potentially arise with respect to the now laid-off employees of the Wolverine mine, who are represented by the United Steelworkers, Local 1-424 (the "Union"). If these employees are not recalled before April 2016, the Wolverine partnership faces an estimated claim of $11.3 million. As I will discuss below, an even more significant contingent liability has also recently been advanced.

[7] This anticipated "parting of the ways" as between the U.S. and Canadian entities in turn prompted the filing of this proceeding, which is intended to provide the petitioners with time to develop a restructuring plan. The principal goal of that plan, as I will describe below, is to complete a going concern sale of the Canadian operations as soon as possible. Fortunately, as of early December 2015, the Walter Canada Group has slightly in excess of US$40.5 million in cash resources to fund the restructuring efforts. However, ongoing operating costs remain high and are now compounded by the restructuring costs.

[8] As was appropriate, the petitioners did not seek extensive orders on December 7, 2015, given the lack of service on certain major stakeholders. A stay was granted on that date, together with other ancillary relief. KPMG Inc. was appointed as the monitor (the "Monitor").

[9] The petitioners now seek relief that will set them on a path to a potential restructuring; essentially, an equity and/or debt restructuring or alternatively, a sale and liquidation of their assets. That relief includes approving a sale and solicitation

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process and the appointment of further professionals to manage that process and complete other necessary management functions. They also seek a key employee retention plan. Finally, the petitioners seek an extension of the stay to early April 2016.

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[10] For obvious reasons, the financial and environmental issues associated with the coal mines loom large in this matter. For that reason, the Walter Canada Group has engaged in discussions with the provincial regulators, being the B.C. Ministry of Energy and Mines and the B.C. Ministry of the Environment, concerning the environmental issues and the proposed restructuring plan. No issues arise from the regulators' perspective at this time in terms of the relief on this application. Other stakeholders have responded to the application and contributed to the final terms of the relief sought.

[11] The stakeholders appearing on this application are largely supportive of the relief sought, save for two.

[12] Firstly, the United Mine Workers of America 1974 Pension Plan and Trust (the "1974 Pension Plan") opposes certain aspects of the relief sought as to who should be appointed to conduct the sales process.

[13] The status of the 1974 Pension Plan arises from somewhat unusual circumstances. One of the U.S. entities, Jim Walter Resources, Inc. ("JWR") is a party to a collective bargaining agreement with the 1974 Pension Plan (the "CBA"). In late December 2015, the U.S. bankruptcy court issued a decision that allowed JWR to reject the CBA. The court also ordered that the sale of the U.S. assets would be free and clear of any liabilities under the CBA. As a result, the 1974 Pension Plan has filed a proof of claim in the U.S. proceedings advancing a contingent claim against JWR with respect to a potential "withdrawal liability" under U.S. law of approximately US$900 million. The U.S. law in question is the *Employee Retirement Income Security Act of 1974*, 29 USC § 101, as amended, which is commonly referred to as "*ERISA*".

[14] The 1974 Pension Plan alleges that it is only a matter of time before JWR formally rejects the CBA. In that event, the 1974 Pension Plan contends that *ERISA* provides that all companies under common control with JWR are jointly and severally liable for this withdrawal liability, and that some of the entities in the Walter Canada Group come within this provision.

[15] It is apparent at this time that neither the Walter Canada Group nor the Monitor has had an opportunity to assess the 1974 Pension Plan's contingent claim. No claims process has even been contemplated at this time. Nevertheless, the standing of the 1974 Pension Plan to make submissions on this application is not seriously contested.

[16] Secondly, the Union only opposes an extension of the stay of certain proceedings underway in this court and the Labour Relations Board in relation to some of its employee claims, which it wishes to continue to litigate.

[17] At the conclusion of the hearing, I granted the orders sought by the petitioners, with reasons to follow. Hence, these reasons.

The Sale and Investment Solicitation Process ("SISP")

[18] The proposed SISP has been developed by the Walter Canada Group in consultation with the Monitor. By this process, bidders may submit a letter of intent or bid for a restructuring, recapitalization or other form of reorganization of the business and affairs of the Walter Canada Group as a going concern, or a purchase of any or all equity interests held by Walter Energy Canada. Alternatively, any bid may relate to a purchase of all or substantially all, or any portion of the Walter Canada Group assets (including the Brule, Willow Creek and Wolverine mines).

[19] It is intended that the SISP will be led by a chief restructuring officer (the "CRO"), implemented by a financial advisor (both as discussed below) and supervised by the Monitor.

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[20] Approvals of SISPs are a common feature in *CCAA* restructuring proceedings. The Walter Canada Group refers to *CCM Master Qualified Fund v. blutip Power Technologies*, 2012 ONSC 1750. At para. 6, Brown J. (as he then was) stated that in reviewing a proposed sale process, the court should consider:

> (i) the fairness, transparency and integrity of the proposed process;
>
> (ii) the commercial efficacy of the proposed process in light of the specific circumstances facing the receiver; and,
>
> (iii) whether the sales process will optimize the chances, in the particular circumstances, of securing the best possible price for the assets up for sale.

[21] Although the court in *CCM Master Qualified Fund* was considering a sales process proposed by a receiver, I agree that these factors are also applicable when assessing the reasonableness of a proposed sales process in a *CCAA* proceeding: see *PCAS Patient Care Automation Services Inc. (Re)*, 2012 ONSC 2840 at paras. 17-19.

[22] In this case, the proposed timelines would see a deadline of March 18 for letters of intent, due diligence thereafter with a bid deadline of May 27 and a target closing date of June 30, 2016. In my view, the timeline is reasonable, particularly with regard to the need to move as quickly as possible to preserve cash resources pending a sale or investment; or, in the worst case scenario, to allow the Walter Canada Group to close the mines permanently. There is sufficient flexibility built into the SISP to allow the person conducting it to amend these deadlines if the circumstances justify it.

[23] The SISP proposed here is consistent with similar sales processes approved in other Canadian insolvency proceedings. In addition, I agree with the Monitor's assessment that the SISP represents the best opportunity for the Walter Canada Group to successfully restructure as a going concern, if such an opportunity should arise.

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[24] No stakeholder, including the 1974 Pension Plan, opposed this relief. All concerned recognize the need to monetize, if possible, the assets held by the Walter Canada Group. I conclude that the proposed SISP is reasonable and it is approved.

Appointment of Financial Advisor and CRO

[25] The more contentious issues are who should conduct the SISP and manage the operations of the Walter Canada Group pending a transaction and what their compensation should be.

[26] The Walter Canada Group seeks the appointment of a financial advisor and CRO to assist with the implementation of the SISP.

[27] In restructuring proceedings it is not unusual that professionals are engaged to advance the restructuring where the existing management is either unable or unwilling to bring the required expertise to bear. In such circumstances, courts have granted enhanced powers to the monitor; otherwise, the appointment of a CRO and/or financial advisor can be considered.

[28] A consideration of this issue requires some context in terms of the current governance status of the Walter Canada Group. At present, there is only one remaining director, who is based in West Virginia. The petitioners' counsel does not anticipate his long-term involvement in these proceedings and expects he will resign once the U.S. sale completes. Similarly, the petitioners have been largely instructed to date by William Harvey. Mr. Harvey is the executive vice-president and chief financial officer of Walter Energy Canada Holdings, Inc., one of the petitioners. He lives in Birmingham, Alabama. As with the director, the petitioners' counsel expects him to resign in the near future.

[29] The only other high level employee does reside in British Columbia, but his expertise is more toward operational matters, particularly regarding environmental and regulatory issues.

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[30] Accordingly, there is a legitimate risk that the Walter Canada Group ship may become rudderless in the midst of these proceedings and most significantly, in the midst of the very important sales and solicitation process. This risk is exacerbated by the fact that the management support traditionally provided by the U.S. entities will not be provided after the sale of the U.S. assets. Significant work must be done to effect a transition of those shared services in order to allow the Canadian operations to continue running smoothly. It is anticipated that the CRO will play a key role in assisting in this transition of the shared services.

[31] In these circumstances, I am satisfied that professional advisors are not just desirable, but indeed necessary, in order to have a chance for a successful restructuring. Both appointments ensure that the SISP will be implemented by professionals who will enhance the likelihood that it generates maximum value for the Walter Canada Group's stakeholders. In addition, the appointment of a CRO will allow the Canadian operations to continue in an orderly fashion, pending a transaction.

[32] The proposal is to retain PJT Partners LP ("PJT") as a financial advisor and investment banker to implement the SISP. PJT is a natural choice given that it had already been retained in the context of the U.S. proceedings to market the Walter Group's assets, which of course indirectly included the Walter Canada Group's assets. As such, PJT is familiar with the assets in this jurisdiction, knowledge that will no doubt be of great assistance in respect of the SISP.

[33] In addition, the proposal is to retain BlueTree Advisors Inc. as the CRO, by which it would provide the services of William E. Aziz. Mr. Aziz is a well-known figure in the Canadian insolvency community; in particular, he is well known for having provided chief restructuring services in other proceedings (see for example *Mobilicity Group (Re)*, 2013 ONSC 6167 at para. 17). No question arises as to his extensive qualifications to fulfil this role.

[34] The materials as to how Mr. Aziz was selected were somewhat thin, which raised some concerns from the 1974 Pension Plan as to the appropriateness of his

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involvement. However, after submissions by the petitioners' counsel, I am satisfied that there was a thorough consideration of potential candidates and their particular qualifications to undertake what will no doubt be a time-consuming and complex assignment. In that regard, I accept the recommendations of the petitioners that Mr. Aziz is the most qualified candidate.

[35] The Monitor was involved in the process by which PJT and BlueTree/Mr. Aziz were selected. It has reviewed both proposals and supports that both PJT and BlueTree are necessary appointments that will result in the Walter Canada Group obtaining the necessary expertise to proceed with its restructuring efforts. In that sense, such appointments fulfill the requirements of being "appropriate", in the sense that that expertise will assist the debtor in achieving the objectives of the *CCAA*: see s. 11; *ICR Commercial Real Estate (Regina) Ltd. v. Bricore Land Group Ltd*., 2007 SKQB 121 at para. 19.

[36] The 1974 Pension Plan does not mount any serious argument against the need for such appointments, other than to note that the costs of these retainers will result in a very expensive process going forward. The matter of PJT and the CRO's compensation was the subject of some negative comment by the 1974 Pension Plan. However, the 1974 Pension Plan did not suggest any alternate way of proceeding with the SISP and the operations generally. When pressed by the Court on the subject, the 1974 Pension Plan acknowledged that time was of the essence in implementing the SISP and it did not contend that a further delay was warranted to canvas other options.

[37] PJT is to receive a monthly work fee of US$100,000, although some savings are achieved since this amount will not be charged until the completion of the U.S. sale. In addition, PJT will receive a capital raising fee based on the different types of financing that might be arranged. Lastly, PJT is entitled to a transaction or success fee, based on the consideration received from any transaction.

[38] At the outset of the application, the proposed compensation for the CRO was similar to that of PJT. The CRO was to obtain a monthly work fee of US$75,000. In

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addition, the CRO was to receive a transaction or success fee based on the consideration received from any transaction. After further consideration by the petitioners and BlueTree, this proposed compensation was subsequently renegotiated so as to limit the success fee to $1 million upon the happening of a "triggering event" (essentially, a recapitalization, refinancing, acquisition or sale of assets or liabilities).

[39] To secure the success fees of PJT and the CRO, the Walter Canada Group seeks a charge of up to a maximum of $10 million, with each being secured to a limit of half that amount. Any other fees payable by the Walter Canada Group to PJT and the CRO would be secured by the Administration Charge granted in the initial order.

[40] The jurisdiction to grant charges for such professional fees is found in s. 11.52 of the *CCAA*:

> 11.52(1) On notice to the secured creditors who are likely to be affected by the security or charge, the court may make an order declaring that all or part of the property of a debtor company is subject to a security or charge — in an amount that the court considers appropriate — in respect of the fees and expenses of
>
> (a) the monitor, including the fees and expenses of any financial, legal or other experts engaged by the monitor in the performance of the monitor's duties;
>
> (b) any financial, legal or other experts engaged by the company for the purpose of proceedings under this Act; and
>
> (c) any financial, legal or other experts engaged by any other interested person if the court is satisfied that the security or charge is necessary for their effective participation in proceedings under this Act.

[41] In *U.S. Steel Canada Inc. (Re)*, 2014 ONSC 6145 at para. 22, Justice Wilton-Siegel commented on the necessity of such a charge in a restructuring, as it is usually required to ensure the involvement of these professionals and achieve the best possible outcome for the stakeholders. I concur in that sentiment here, as the involvement of PJT and BlueTree is premised on this charge being granted.

[42] In *Canwest Publishing Inc*., 2010 ONSC 222 at para. 54, Justice Pepall (as she then was) set out a non-exhaustive list of factors to consider when determining

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whether the proposed compensation is appropriate and whether charges should be granted for that compensation:

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

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

(c) whether there is an unwarranted duplication of roles;

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

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

(f) the position of the Monitor.

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[43] I am satisfied that the Walter Canada Group's assets and operations are significantly complex so as to justify both these appointments and the proposed compensation. I have already referred to the significant regulatory and environmental issues that arise. In addition, relevant employment issues are already present. Any transaction relating to these assets and operations will be anything but straightforward.

[44] The factors relating to the proposed role of the professionals and whether there is unwarranted duplication can be addressed at the same time. As conceded by the petitioners' and Monitor's counsel, there will undoubtedly be some duplication with the involvement of the Monitor, PJT and the CRO. However, the issue is whether there is *unwarranted* duplication of effort. I am satisfied that the process has been crafted in a fashion that recognizes the respective roles of these professionals but also allows for a coordinated effort that will assist each of them in achieving their specific goals. Each has a distinct focus and I would expect that their joint enterprise will produce a better result overall.

[45] Any consideration of compensation will inevitably be driven by the particular facts that arise in the proceedings in issue. Even so, I have not been referred to any material that indicates that the proposed compensation and charge in favour of PJT and the CRO are inconsistent with compensation structures and protections approved in other similarly complex insolvency proceedings. In that regard, I accept

the petitioners' submissions that the task ahead justifies both the amount of the fees to be charged and the protections afforded by the charge. In short, I find that the proposed compensation is fair and reasonable in these circumstances.

[46] The secured creditors likely to be affected by the charges for PJT and the CRO's fees have been given notice and do not oppose the relief being sought.

[47] Finally, the Monitor is of the view that the agreed compensation of PJT and the CRO and the charge in their favour are appropriate.

[48] In summary, all circumstances support the relief sought. Accordingly, I conclude that it is appropriate to appoint the CRO and approve the engagement of PJT on the terms sought. In addition, I grant a charge in favour of PJT and the CRO to a maximum of $10 million to secure their compensation beyond the monthly work fees, subject to the Administration Charge, the Director's Charge and the KERP Charge (as discussed below).

Key Employee Retention Plan ("KERP")

[49] The Walter Canada Group also seeks approval of a KERP, for what it describes as a "key" employee needed to maintain the Canadian operations while the SISP is being conducted. In addition, Mr. Harvey states that this employee has specific information which the CRO, PJT and the Monitor will need to draw on during the implementation of the SISP.

[50] The detailed terms of the KERP are contained in a letter attached to Mr. Harvey's affidavit #3 sworn December 31, 2015. In the course of submissions, the Walter Canada Group sought an order to seal this affidavit, on the basis that the affidavit and attached exhibit contained sensitive information, being the identity of the employee and the compensation proposed to be paid to him.

[51] I was satisfied that a sealing order should be granted with respect to this affidavit, based on the potential disclosure of this personal information to the public: see *Sierra Club of Canada v. Canada (Minister of Finance)*, 2002 SCC 41 at

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para. 53; *Sahlin v. The Nature Trust of British Columbia*, 2010 BCCA 516 at para. 6. A sealing order was granted on January 5, 2016.

[52] The proposed KERP must be considered in the context of earlier events. This individual was to receive a retention bonus from the U.S. entities; however, this amount is now not likely to be paid. In addition, just prior to the commencement of these proceedings, this person was given a salary increase to reflect his additional responsibilities, including those arising from the loss of support and the shared services from the U.S. entities. This new salary level has not been disclosed to the court or the stakeholders.

[53] The Walter Canada Group has proposed that this employee be paid a retention bonus on the occurrence of a "triggering event", provided he remains an active employee providing management and other services. The defined triggering events are such that the retention bonus is likely to be paid whatever the outcome might be. In addition, to secure the payment of the KERP to this employee, Walter Energy Canada seeks a charge up to the maximum amount of the retention bonus.

[54] The amount of the retention bonus is large. It has been disclosed in the sealed affidavit but has not been disclosed to certain stakeholders, including the 1974 Pension Plan. The Monitor states in its report:

> The combination of the salary increase and proposed retention bonus … were designed to replace the retention bonus previously promised to the KERP Participant by Walter Energy U.S.

[55] I did not understand the submissions of the 1974 Pension Plan to be that the granting of a KERP for this employee was inappropriate. Rather, the concern related to the amount of the retention bonus, which is to be considered in the context of the earlier salary raise. At the end of the day, the 1974 Pension Plan was content to leave a consideration of the level of compensation to the Court, given the sealing of the affidavit.

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[56] The authority to approve a KERP is found in the courts' general statutory jurisdiction under s. 11 of the *CCAA* to grant relief if "appropriate": see *U.S. Steel Canada* at para. 27.

[57] As noted by the court in *Timminco Ltd. (Re)*, 2012 ONSC 506 at para. 72, KERPs have been approved in numerous insolvency proceedings, particularly where the retention of certain employees was deemed critical to a successful restructuring.

[58] Factors to be considered by the court in approving a KERP will vary from case to case, but some factors will generally be present. See for example, *Grant Forest Products Inc. (Re)* (2009), 57 C.B.R. (5th) 128 (Ont. S.C.J.); and *U.S. Steel Canada* at paras. 28-33.

[59] I will discuss those factors and the relevant evidence on this application, as follows:

a) Is this employee important to the restructuring process?: In its report, the Monitor states that this employee is the most senior remaining executive in the Walter Canada Group, with extensive knowledge of its assets and operations. He was involved in the development of the Wolverine mine and has extensive knowledge of all three mines. He also has strong relationships in the communities in which the mines are located, with the Group's suppliers and with the regulatory authorities. In that sense, this person's expertise will enhance the efforts of the other professionals to be involved, including PJT, the CRO and the Monitor: *U.S. Steel* at para. 28;

b) Does the employee have specialized knowledge that cannot be easily replaced?: I accept that the background and expertise of this employee is such that it would be virtually impossible to replace him if he left the employ of the Walter Canada Group: *U.S. Steel* at para. 29;

c) Will the employee consider other employment options if the KERP is not approved?: There is no evidence here on this point, but I presume

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that the KERP is more a prophylactic measure, rather than a reactionary one. In any event, this is but one factor and I would adopt the comments of Justice Newbould in *Grant Forest Products* at paras. 13-15, that a "potential" loss of this person's employment is a factor to be considered;

d) Was the KERP developed through a consultative process involving the Monitor and other professionals?: The Monitor has reviewed the proposed KERP, but does not appear to have been involved in the process. Mr. Harvey confirms the business decision of the Walter Canada Group to raise this employee's salary and propose the KERP. The business judgment of the board and management is entitled to some deference in these circumstances: *Grant Forest Products* at para. 18; *U.S. Steel Canada* at para. 31; and

e) Does the Monitor support the KERP and a charge?: The answer to this question is a resounding "yes". As to the amount, the Monitor notes that the amount of the retention bonus is at the "high end" of other KERP amounts of which it is aware. However, the Monitor supports the KERP amount even in light of the earlier salary increase and after considering the value and type of assets under this person's supervision and the critical nature of his involvement in the restructuring. As this Court's officer, the views of the Monitor are also entitled to considerable deference by this Court: *U.S. Steel* at para. 32.

[60] In summary, the petitioners' counsel described the involvement of this individual in the *CCAA* restructuring process as "essential" or "critical". These sentiments are echoed by the Monitor, who supports the proposed KERP and charge to secure it. The Monitor's report states that this individual's ongoing employment will be "highly beneficial" to the Walter Canada Group's restructuring efforts, and that this employee is "critical" to the care and maintenance operations at

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the mines, the transitioning of the shared services from the U.S. and finally, assisting with efforts under the SISP.

[61] What I take from these submissions is that a loss of this person's expertise either now or during the course of the *CCAA* process would be extremely detrimental to the chances of a successful restructuring. In my view, it is more than evident that there is serious risk to the stakeholders if this person does not remain engaged in the process. Such a result would be directly opposed to the objectives of the *CCAA*. I find that such relief is appropriate and therefore, the KERP and charge to secure the KERP are approved.

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Cash Collateralization / Intercompany Charge

[62] Pursuant to the initial order, the Walter Canada Group was authorized and directed to cash collateralize all letters of credit secured by the 2011 credit agreement within 15 days of any demand to do so from the administrative agent, Morgan Stanley Senior Funding Inc. ("Morgan Stanley"). This order was made on the basis of representations by the Monitor's counsel that it had obtained a legal opinion that the security held by Morgan Stanley was valid and enforceable against the Walter Canada Group.

[63] On December 9, 2015, Morgan Stanley demanded the cash collateralization of approximately $22.6 million of undrawn letters of credit. On December 21, 2015, Morgan Stanley requested that the Walter Canada Group enter into a cash collateral agreement (the "Cash Collateral Agreement") to formalize these arrangements.

[64] The Walter Canada Group seeks the approval of the Cash Collateral Agreement, which provides for the establishment of a bank account containing the cash collateral and confirms Morgan Stanley's pre-filing first-ranking security interest in the cash in the bank account. The cash collateralization is intended to relate to letters of credit issued on behalf of Brule Coal Partnership, Walter Canadian Coal Partnership, Wolverine Coal Partnership and Willow Creek Coal Partnership. However, only the Brule Coal Partnership has sufficient cash to collateralize all these letters of credit.

[65] Accordingly, the Walter Canada Group seeks an intercompany charge in favour of Brule Coal Partnership, and any member of the Walter Canada Group, to the extent that a member of the Walter Canada Group makes any payment or incurs or discharges any obligation on behalf of any other member of the Walter Canada Group in respect of obligations under the letters of credit. The intercompany charge is proposed to rank behind all of the other court-ordered charges granted in these proceedings, including the charges for PJT and the CRO and the KERP.

[66] No objection is raised in respect of this relief. The Monitor is of the view that the intercompany charge is appropriate.

[67] In my view, this relief is simply a formalization of the earlier authorization regarding the trusting up of these contingent obligations. On that basis, I approve the Cash Collateral Agreement. I also approve the intercompany charge in favour of the Brule Coal Partnership, on the basis that it is necessary to preserve the *status quo* as between the various members of the Walter Canada Group who will potentially benefit from the use of this Partnership's funds. Such a charge will, as stated by the Monitor, protect the interests of creditors as against the individual entities within the Walter Canada Group.

Stay Extension

[68] In order to implement the SISP, and further its restructuring efforts in general, the Walter Canada Group is seeking an extension of the stay and other relief granted in the initial order until April 5, 2016.

[69] Section 11.02(2) and (3) of the *CCAA* authorizes the court to make an order extending a stay of proceedings granted in the initial application. In this case, the evidence, together with the conclusions of the Monitor, support that an extension is appropriate and that the petitioners are acting in good faith and with due diligence. No stakeholder has suggested otherwise.

[70] As noted above, it is anticipated that the Walter Canada Group will have sufficient liquidity to continue operating throughout the requested stay period.

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[71] Further, as the Phase 1 deadline in the SISP is March 18 2016, an extension of the stay until April 5, 2016 will provide sufficient time for PJT to solicit, and the CRO (in consultation with the Monitor and PJT) to consider, any letters of intent. At that time, the process may continue to Phase 2 of the SISP, if the CRO, in consultation with the Monitor and PJT, deems it advisable. In any event, at the time of the next court date, there will be a formal update to the court and the stakeholders on the progress under the SISP.

[72] The only issue relating to the extension of the stay arises from the submissions of the Union, who represents the employees at the Wolverine mine owned and operated by the Wolverine Coal Partnership ("Wolverine LP"). The Union wishes to continue with certain outstanding legal proceedings outstanding against Wolverine LP, as follows:

a) In June 2015, the B.C. Labour Relations Board (the "Board") found that Wolverine LP was in breach of s. 54 of the *Labour Relations Code,* R.S.B.C. 1996, c. 224 (the "*Code*"). The Board ordered Wolverine LP to pay $771,378.70 into trust by way of remedy. This was estimated to be the amount of damages owed by Wolverine LP, but the Union took the position that further amounts are owed. In any event, this amount was paid and is currently held in trust;

b) In November 2015, Wolverine LP filed a proceeding in this court seeking a judicial review of the Board's decision on the s. 54 issue. As a result, the final determination of the damages arising from the *Code* breach has not yet occurred and may never occur if Wolverine LP succeeds in its judicial review; and

c) Following layoffs in April 2014, the Union claimed that a "northern allowance" was payable by Wolverine LP to the employees, including those on layoff. This claim was rejected at arbitration, and upheld on review at the Board. In February 2015, the Union filed a proceeding in this court seeking a judicial review of the Board's decision.

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[73] The Union's counsel has referred me to my earlier decision in *Yukon Zinc Corporation (Re)*, 2015 BCSC 1961. There, I summarized the principles that govern applications by a creditor to lift the stay of proceedings to litigate claims:

> [26] There is also no controversy concerning the principles which govern applications by creditors under the *CCAA* to lift the stay of proceedings to litigate claims in other courts or forums, other than by the procedures in place in the restructuring proceedings:
>
> a) the lifting of the stay is discretionary: *Canwest Global Communications Corp.*, 2011 ONSC 2215, at paras. 19, 27;
>
> b) there are no statutory guidelines and the applicant faces a "very heavy onus" in making such an application: *Canwest Global Communications Corp. (Re)* (2009), 61 C.B.R. (5th) 200, at para. 32, 183 A.C.W.S. (3d) (Ont. S.C.J.) ("*Canwest* (2009)"), as applied in *Azure Dynamics Corporation (Re)*, 2012 BCSC 781, at para. 5 and *505396 B.C. Ltd. (Re)*, 2013 BCSC 1580, at para. 19;
>
> c) there are no set circumstances where a stay will or will not be lifted, although examples of situations where the courts have lifted stay orders are set out in *Canwest* (2009) at para. 33;
>
> d) relevant factors will include the status of the *CCAA* proceedings and what impact the lifting of the stay will have on the proceedings. The court may consider whether there are sound reasons for doing so consistent with the objectives of the *CCAA*, including a consideration of the relative prejudice to parties and, where relevant, the merits of the proposed action: *Canwest* (2009) at para. 32;
>
> e) particularly where the issue is one which is engaged by a claims process in place, it must be remembered that one of the objectives of the *CCAA* is to promote a streamlined process to determine claims that reduces expense and delay; and
>
> f) as an overarching consideration, the court must consider whether it is in the interests of justice to lift the stay: *Canwest* (2009); *Azure Dynamics* at para. 28.

[74] I concluded that the Union had not met the "heavy onus" on it to justify the lifting of the stay to allow these various proceedings to continue. My specific reasons are:

a) The Union argues that the materials are essentially already assembled and that these judicial reviews can be scheduled for short chambers matters. As such, the Union argues that there is "minimal prejudice" to Wolverine LP. While this may be so, proceeding with these matters will

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inevitably detract both managerial and legal focus from the primary task at hand, namely to implement the SISP, and as such, potentially interfere with the restructuring efforts;

b) The Union argues that any purchaser of Wolverine LP's mine will inherit outstanding employee obligations pursuant to the *Code*. Accordingly, the Union argues that it will be more attractive to a buyer for the mine to have all outstanding employee claims resolved. Again, while this may come to pass, such an argument presupposes an outcome that is anything less than clear at this time. Such a rationale is clearly premature;

c) The Union argues that it is unable to distribute the $771,378.70 to its members until Wolverine LP's judicial review is addressed. Frankly, I see this delay as the only real prejudice to the Union members. However, on the other hand, one might argue that the Union members are in a favourable position with these monies being held in trust as opposed to being unsecured creditors of Wolverine. In any event, the Union's claim to these monies has not yet been determined and arises from a dispute that dates back to April 2014. Therefore, there is no settled liability that would allow such payment to be made; and

d) The Union claims that these matters must be determined "in any event" and that they should be determined "sooner rather than later". However, the outcome of the SISP may significantly affect what recovery any creditor may hope to achieve in this restructuring. In the happy circumstance where there will be monies to distribute, I expect that a claims process will be implemented to determine valid claims, not only in respect of the Union's claims, but all creditors.

[75] In summary, there is nothing to elevate the Union's claims such that it is imperative that they be determined now. There is nothing to justify the distraction and expense of proceeding with these actions to the detriment of the restructuring

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efforts. If it should come to pass that monies will be distributed to creditors, such as the Union, then I expect that the usual claims process will be implemented to decide the validity of those claims.

[76] In the meantime, if it becomes necessary to determine the validity of these claims quickly (such as to clarify potential successor claims for a purchaser), the Union will be at liberty to renew its application to lift the stay for that purpose.

[77] Accordingly, I grant an extension of the stay of proceedings and other ancillary relief until April 5, 2016.

"Fitzpatrick J."

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CITATION: Cinram International Inc. (Re), 2012 ONSC 3767
COURT FILE NO.: CV-12-9767-00CL
DATE: 20120626

SUPERIOR COURT OF JUSTICE – ONTARIO
(COMMERCIAL LIST)

2012 ONSC 3767 (CanLII)

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 CINRAM INTERNATIONAL INC., CINRAM INTERNATIONAL INCOME FUND, CII TRUST AND THE COMPANIES LISTED IN SCHEDULE "A", Applicants

BEFORE: **MORAWETZ J.**

COUNSEL: **Robert J. Chadwick, Melaney Wagner and Caroline Descours, for the Applicants**

Steven Golick, for Warner Electra-Atlantic Corp.

Steven Weisz, for Pre-Petition First Lien Agent, Pre-Petition Second Lien Agent and DIP Agent

Tracy Sandler, for Twentieth Century Fox Film Corporation

David Byers, for the Proposed Monitor, FTI Consulting Inc.

HEARD &
ENDORSED: **JUNE 25, 2012**

REASONS: **JUNE 26, 2012**

ENDORSEMENT

[1] Cinram International Inc. ("CII"), Cinram International Income Fund ("Cinram Fund"), CII Trust and the Companies listed in Schedule "A" (collectively, the "Applicants") brought this application seeking an initial order (the "Initial Order") pursuant to the *Companies' Creditors Arrangement Act* ("CCAA"). The Applicants also request that the court exercise its jurisdiction to extend a stay of proceedings and other benefits under the Initial Order to Cinram International Limited Partnership ("Cinram LP", collectively with the Applicants, the "CCAA Parties").

[2] Cinram Fund, together with its direct and indirect subsidiaries (collectively, "Cinram" or the "Cinram Group") is a replicator and distributor of CDs and DVDs. Cinram has a diversified operational footprint across North America and Europe that enables it to meet the replication and logistics demands of its customers.

[3] The evidentiary record establishes that Cinram has experienced significant declines in revenue and EBITDA, which, according to Cinram, are a result of the economic downturn in Cinram's primary markets of North America and Europe, which impacted consumers' discretionary spending and adversely affected the entire industry.

[4] Cinram advises that over the past several years it has continued to evaluate its strategic alternatives and rationalize its operating footprint in order to attempt to balance its ongoing operations and financial challenges with its existing debt levels. However, despite cost reductions and recapitalized initiatives and the implementation of a variety of restructuring alternatives, the Cinram Group has experienced a number of challenges that has led to it seeking protection under the CCAA.

[5] Counsel to Cinram outlined the principal objectives of these CCAA proceedings as:

(i) to ensure the ongoing operations of the Cinram Group;

(ii) to ensure the CCAA Parties have the necessary availability of working capital funds to maximize the ongoing business of the Cinram Group for the benefit of its stakeholders; and

(iii) to complete the sale and transfer of substantially all of the Cinram Group's business as a going concern (the "Proposed Transaction").

[6] Cinram contemplates that these CCAA proceedings will be the primary court supervised restructuring of the CCAA Parties. Cinram has operations in the United States and certain of the Applicants are incorporated under the laws of the United States. Cinram, however, takes the position that Canada is the nerve centre of the Cinram Group.

[7] The Applicants also seek authorization for Cinram International ULC ("Cinram ULC") to act as "foreign representative" in the within proceedings to seek a recognition order under Chapter 15 of the United States Bankruptcy Code ("Chapter 15"). Cinram advises that the proceedings under Chapter 15 are intended to ensure that the CCAA Parties are protected from creditor actions in the United States and to assist with the global implementation of the Proposed Transaction to be undertaken pursuant to these CCAA proceedings.

[8] Counsel to the Applicants submits that the CCAA Parties are part of a consolidated business in Canada, the United States and Europe that is headquartered in Canada and operationally and functionally integrated in many significant respects. Cinram is one of the world's largest providers of pre-recorded multi-media products and related logistics services. It has facilities in North America and Europe, and it:

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(i) manufactures DVDs, blue ray disks and CDs, and provides distribution services for motion picture studios, music labels, video game publishers, computer software companies, telecommunication companies and retailers around the world;

(ii) provides various digital media services through One K Studios, LLC; and

(iii) provides retail inventory control and forecasting services through Cinram Retail Services LLC (collectively, the "Cinram Business").

[9] Cinram contemplates that the Proposed Transaction could allow it to restore itself as a market leader in the industry. Cinram takes the position that it requires CCAA protection to provide stability to its operations and to complete the Proposed Transaction.

[10] The Proposed Transaction has the support of the lenders forming the steering committee with respect to Cinram's First Lien Credit Facilities (the "Steering Committee"), the members of which have been subject to confidentiality agreements and represent 40% of the loans under Cinram's First Lien Credit Facilities (the "Initial Consenting Lenders"). Cinram also anticipates further support of the Proposed Transaction from additional lenders under its credit facilities following the public announcement of the Proposed Transaction.

[11] Cinram Fund is the direct or indirect parent and sole shareholder of all of the subsidiaries in Cinram's corporate structure. A simplified corporate structure of the Cinram Group showing all of the CCAA Parties, including the designation of the CCAA Parties' business segments and certain non-filing entities, is set out in the Pre-Filing Report of FTI Consulting Inc. (the "Monitor") at paragraph 13. A copy is attached as Schedule "B".

[12] Cinram Fund, CII, Cinram International General Partner Inc. ("Cinram GP"), CII Trust, Cinram ULC and 1362806 Ontario Limited are the Canadian entities in the Cinram Group that are Applicants in these proceedings (collectively, the "Canadian Applicants"). Cinram Fund and CII Trust are both open-ended limited purpose trusts, established under the laws of Ontario, and each of the remaining Canadian Applicants is incorporated pursuant to Federal or Provincial legislation.

[13] Cinram (US) Holdings Inc. ("CUSH"), Cinram Inc., IHC Corporation ("IHC"), Cinram Manufacturing, LLC ("Cinram Manufacturing"), Cinram Distribution, LLC ("Cinram Distribution"), Cinram Wireless, LLC ("Cinram Wireless"), Cinram Retail Services, LLC ("Cinram Retail") and One K Studios, LLC ("One K") are the U.S. entities in the Cinram Group that are Applicants in these proceedings (collectively, the "U.S. Applicants"). Each of the U.S. Applicants is incorporated under the laws of Delaware, with the exception of One K, which is incorporated under the laws of California. On May 25, 2012, each of the U.S. Applicants opened a new Canadian-based bank account with J.P. Morgan.

[14] Cinram LP is not an Applicant in these proceedings. However, the Applicants seek to have a stay of proceedings and other relief under the CCAA extended to Cinram LP as it forms

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part of Cinram's income trust structure with Cinram Fund, the ultimate parent of the Cinram Group.

[15] Cinram's European entities are not part of these proceedings and it is not intended that any insolvency proceedings will be commenced with respect to Cinram's European entities, except for Cinram Optical Discs SAC, which has commenced insolvency proceedings in France.

[16] The Cinram Group's principal source of long-term debt is the senior secured credit facilities provided under credit agreements known as the "First-Lien Credit Agreement" and the "Second-Lien Credit Agreement" (together with the First-Lien Credit Agreement, the "Credit Agreements").

[17] All of the CCAA Parties, with the exception of Cinram Fund, Cinram GP, CII Trust and Cinram LP (collectively, the "Fund Entities"), are borrowers and/or guarantors under the Credit Agreements. The obligations under the Credit Agreements are secured by substantially all of the assets of the Applicants and certain of their European subsidiaries.

[18] As at March 31, 2012, there was approximately $233 million outstanding under the First-Lien Term Loan Facility; $19 million outstanding under the First-Lien Revolving Credit Facilities; approximately $12 million of letter of credit exposure under the First-Lien Credit Agreement; and approximately $12 million outstanding under the Second-Lien Credit Agreement.

[19] Cinram advises that in light of the financial circumstances of the Cinram Group, it is not possible to obtain additional financing that could be used to repay the amounts owing under the Credit Agreements.

[20] Mr. John Bell, Chief Financial Officer of CII, stated in his affidavit that in connection with certain defaults under the Credit Agreements, a series of waivers was extended from December 2011 to June 30, 2012 and that upon expiry of the waivers, the lenders have the ability to demand immediate repayment of the outstanding amounts under the Credit Agreements and the borrowers and the other Applicants that are guarantors under the Credit Agreements would be unable to meet their debt obligations. Mr. Bell further stated that there is no reasonable expectation that Cinram would be able to service its debt load in the short to medium term given forecasted net revenues and EBITDA for the remainder of fiscal 2012, fiscal 2013, and fiscal 2014. The cash flow forecast attached to his affidavit indicates that, without additional funding, the Applicants will exhaust their available cash resources and will thus be unable to meet their obligations as they become due.

[21] The Applicants request a stay of proceedings. They take the position that in light of their financial circumstances, there could be a vast and significant erosion of value to the detriment of all stakeholders. In particular, the Applicants are concerned about the following risks, which, because of the integration of the Cinram business, also apply to the Applicants' subsidiaries, including Cinram LP:

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(a) the lenders demanding payment in full for money owing under the Credit Agreements;

(b) potential termination of contracts by key suppliers; and

(c) potential termination of contracts by customers.

[22] As indicated in the cash flow forecast, the Applicants do not have sufficient funds available to meet their immediate cash requirements as a result of their current liquidity challenges. Mr. Bell states in his affidavit that the Applicants require access to Debtor-In-Possession ("DIP") Financing in the amount of $15 millions to continue operations while they implement their restructuring, including the Proposed Transaction. Cinram has negotiated a DIP Credit Agreement with the lenders forming the Steering Committee (the "DIP Lenders") through J.P. Morgan Chase Bank, NA as Administrative Agent (the "DIP Agent") whereby the DIP Lenders agree to provide the DIP Financing in the form of a term loan in the amount of $15 million.

[23] The Applicants also indicate that during the course of the CCAA proceedings, the CCAA Parties intend to generally make payments to ensure their ongoing business operations for the benefit of their stakeholders, including obligations incurred prior to, on, or after the commencement of these proceedings relating to:

(a) the active employment of employees in the ordinary course;

(b) suppliers and service providers the CCAA Parties and the Monitor have determined to be critical to the continued operation of the Cinram business;

(c) certain customer programs in place pursuant to existing contracts or arrangements with customers; and

(d) inter-company payments among the CCAA Parties in respect of, among other things, shared services.

[24] Mr. Bell states that the ability to make these payments relating to critical suppliers and customer programs is subject to a consultation and approval process agreed to among the Monitor, the DIP Agent and the CCAA Parties.

[25] The Applicants also request an Administration Charge for the benefit of the Monitor and Moelis and Company, LLC ("Moelis"), an investment bank engaged to assist Cinram in a comprehensive and thorough review of its strategic alternatives.

[26] In addition, the directors (and in the case of Cinram Fund and CII Trust, the Trustees, referred to collectively with the directors as the "Directors/Trustees") requested a Director's Charge to provide certainty with respect to potential personal liability if they continue in their current capacities. Mr. Bell states that in order to complete a successful restructuring, including the Proposed Transaction, the Applicants require the active and committed involvement of their

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Directors/Trustees and officers. Further, Cinram's insurers have advised that if Cinram was to file for CCAA protection, and the insurers agreed to renew the existing D&O policies, there would be a significant increase in the premium for that insurance.

[27] Cinram has also developed a key employee retention program (the "KERP") with the principal purpose of providing an incentive for eligible employees, including eligible officers, to remain with the Cinram Group despite its financial difficulties. The KERP has been reviewed and approved by the Board of Trustees of the Cinram Fund. The KERP includes retention payments (the "KERP Retention Payments") to certain existing employees, including certain officers employed at Canadian and U.S. Entities, who are critical to the preservation of Cinram's enterprise value.

[28] Cinram also advises that on June 22, 2012, Cinram Fund, the borrowers under the Credit Agreements, and the Initial Consenting Lenders entered into a support agreement pursuant to which the Initial Consenting Lenders agreed to support the Proposed Transaction to be pursued through these CCAA proceedings (the "Support Agreement").

[29] Pursuant to the Support Agreement, lenders under the First-Lien Credit Agreement who execute the Support Agreement or Consent Agreement prior to July 10, 2012 (the "Consent Date") are entitled to receive consent consideration (the "Early Consent Consideration") equal to 4% of the principal amount of loans under the First-Lien Credit Agreement held by such consenting lenders as of the Consent Date, payable in cash from the net sale proceeds of the Proposed Transaction upon distribution of such proceeds in the CCAA proceedings.

[30] Mr. Bell states that it is contemplated that the CCAA proceedings will be the primary court-supervised restructuring of the CCAA Parties. He states that the CCAA Parties are part of a consolidated business in Canada, the United States and Europe that is headquartered in Canada and operationally and functionally integrated in many significant respects. Mr. Bell further states that although Cinram has operations in the United States, and certain of the Applicants are incorporated under the laws of the United States, it is Ontario that is Cinram's home jurisdiction and the nerve centre of the CCAA Parties' management, business and operations.

[31] The CCAA Parties have advised that they will be seeking a recognition order under Chapter 15 to ensure that they are protected from creditor actions in the United States and to assist with the global implementation of the Proposed Transaction. Thus, the Applicants seek authorization in the Proposed Initial Order for:

> Cinram ULC to seek recognition of these proceedings as "foreign main proceedings" and to seek such additional relief required in connection with the prosecution of any sale transaction, including the Proposed Transaction, as well as authorization for the Monitor, as a court-appointed officer, to assist the CCAA Parties with any matters relating to any of the CCAA Parties' subsidiaries and any foreign proceedings commenced in relation thereto.

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[32] Mr. Bell further states that the Monitor will be actively involved in assisting Cinram ULC as the foreign representative of the Applicants in the Chapter 15 proceedings and will assist in keeping this court informed of developments in the Chapter 15 proceedings.

[33] The facts relating to the CCAA Parties, the Cinram business, and the requested relief are fully set out in Mr. Bell's affidavit.

[34] Counsel to the Applicants filed a comprehensive factum in support of the requested relief in the Initial Order. Part III of the factum sets out the issues and the law.

[35] The relief requested in the form of the Initial Order is extensive. It goes beyond what this court usually considers on an initial hearing. However, in the circumstances of this case, I have been persuaded that the requested relief is appropriate.

[36] In making this determination, I have taken into account that the Applicants have spent a considerable period of time reviewing their alternatives and have done so in a consultative manner with their senior secured lenders. The senior secured lenders support this application, notwithstanding that it is clear that they will suffer a significant shortfall on their positions. It is also noted that the Early Consent Consideration will be available to lenders under the First-Lien Credit Agreement who execute the Support Agreement prior to July 10, 2012. Thus, all of these lenders will have the opportunity to participate in this arrangement.

[37] As previously indicated, the Applicants' factum is comprehensive. The submissions on the law are extensive and cover all of the outstanding issues. It provides a fulsome review of the jurisprudence in the area, which for purposes of this application, I accept. For this reason, paragraphs 41-96 of the factum are attached as Schedule "C" for reference purposes.

[38] The Applicants have also requested that the confidential supplement – which contains the KERP summary listing the individual KERP Payments and certain DIP Schedules – be sealed. I am satisfied that the KERP summary contains individually identifiable information and compensation information, including sensitive salary information, about the individuals who are covered by the KERP and that the DIP schedules contain sensitive competitive information of the CCAA Parties which should also be treated as being confidential. Having considered the principals of *Sierra Club of Canada v. Canada (Minister of Finance)*, (2002) 2 S.C.R. 522, I accept the Applicants' submission on this issue and grant the requested sealing order in respect of the confidential supplement.

[39] Finally, the Applicants have advised that they intend to proceed with a Chapter 15 application on June 26, 2012 before the United States Bankruptcy Court in the District of Delaware. I am given to understand that Cinram ULC, as proposed foreign representative, will be seeking recognition of the CCAA proceedings as "foreign main proceedings" on the basis that Ontario, Canada is the Centre of Main Interest or "COMI" of the CCAA Applicants.

[40] In his affidavit at paragraph 195, Mr. Bell states that the CCAA Parties are part of a consolidated business that is headquartered in Canada and operationally and functionally

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integrated in many significant respects and that, as a result of the following factors, the Applicants submit the COMI of the CCAA Parties is Ontario, Canada:

(a) the Cinram Group is managed on a consolidated basis out of the corporate headquarters in Toronto, Ontario, where corporate-level decision-making and corporate administrative functions are centralized;

(b) key contracts, including, among others, major customer service agreements, are negotiated at the corporate level and created in Canada;

(c) the Chief Executive Officer and Chief Financial Officer of CII, who are also directors, trustees and/or officers of other entities in the Cinram Group, are based in Canada;

(d) meetings of the board of trustees and board of directors typically take place in Canada;

(e) pricing decisions for entities in the Cinram Group are ultimately made by the Chief Executive Officer and Chief Financial Officer in Toronto, Ontario;

(f) cash management functions for Cinram's North American entities, including the administration of Cinram's accounts receivable and accounts payable, are managed from Cinram's head office in Toronto, Ontario;

(g) although certain bookkeeping, invoicing and accounting functions are performed locally, corporate accounting, treasury, financial reporting, financial planning, tax planning and compliance, insurance procurement services and internal audits are managed at a consolidated level in Toronto, Ontario;

(h) information technology, marketing, and real estate services are provided by CII at the head office in Toronto, Ontario;

(i) with the exception of routine maintenance expenditures, all capital expenditure decisions affecting the Cinram Group are managed in Toronto, Ontario;

(j) new business development initiatives are centralized and managed from Toronto, Ontario; and

(k) research and development functions for the Cinram Group are corporate-level activities centralized at Toronto, Ontario, including the Cinram Group's corporate-level research and development budget and strategy.

[41] Counsel submits that the CCAA Parties are highly dependent upon the critical business functions performed on their behalf from Cinram's head office in Toronto and would not be able to function independently without significant disruptions to their operations.

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[42] The above comments with respect to the COMI are provided for informational purposes only. This court clearly recognizes that it is the function of the receiving court – in this case, the United States Bankruptcy Court for the District of Delaware – to make the determination on the location of the COMI and to determine whether this CCAA proceeding is a "foreign main proceeding" for the purposes of Chapter 15.

[43] In the result, I am satisfied that the Applicants meet all of the qualifications established for relief under the CCAA and I have signed the Initial Order in the form submitted, which includes approvals of the Charges referenced in the Initial Order.

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MORAWETZ J.

Date: June 26, 2012

SCHEDULE "A"

ADDITIONAL APPLICANTS

Cinram International General Partner Inc.

Cinram International ULC

1362806 Ontario Limited

Cinram (U.S.) Holdings Inc.

Cinram, Inc.

IHC Corporation

Cinram Manufacturing LLC

Cinram Distribution LLC

Cinram Wireless LLC

Cinram Retail Services, LLC

One K Studios, LLC

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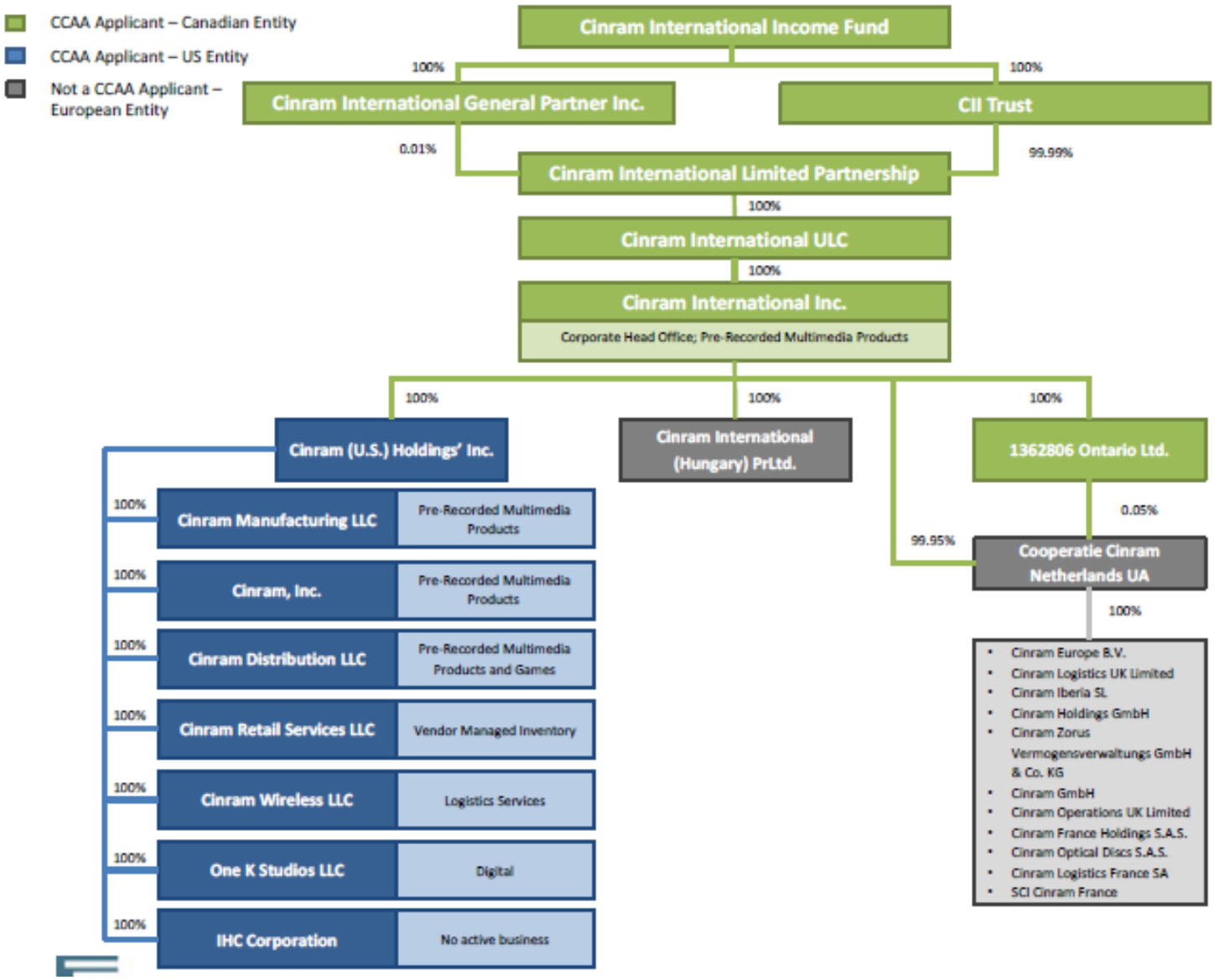
SCHEDULE "B"



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SCHEDULE "C"

A. THE APPLICANTS ARE "DEBTOR COMPANIES" TO WHICH THE CCAA APPLIES

41. The CCAA applies in respect of a "debtor company" (including a foreign company having assets or doing business in Canada) or "affiliated debtor companies" where the total of claims against such company or companies exceeds $5 million.

> CCAA, Section 3(1).

42. The Applicants are eligible for protection under the CCAA because each is a "debtor company" and the total of the claims against the Applicants exceeds $5 million.

(1) The Applicants are Debtor Companies

43. The terms "company" and "debtor company" are defined in Section 2 of the CCAA as follows:

> "company" means any company, corporation or legal person incorporated by or under an Act of Parliament or of the legislature of a province and any incorporated company having assets or doing business in Canada, wherever incorporated, and any income trust, but does not include banks, authorized foreign banks within the meaning of section 2 of the *Bank Act*, railway or telegraph companies, insurance companies and companies to which the *Trust and Loan Companies Act* applies.
>
> "debtor company" means any company that:
>
> (a) is bankrupt or insolvent;
>
> (b) has committed an act of bankruptcy within the meaning of the *Bankruptcy and Insolvency Act* or is deemed insolvent within the meaning of the *Winding-Up and Restructuring Act*, whether or not proceedings in respect of the company have been taken under either of those Acts;
>
> (c) has made an authorized assignment or against which a receiving order has been made under the *Bankruptcy and Insolvency Act*; or

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(d) is in the course of being wound up under the *Winding-Up and Restructuring Act* because the company is insolvent.

CCAA, Section 2 ("company" and "debtor company").

44. The Applicants are debtor companies within the meaning of these definitions.

(2) The Applicants are "companies"

45. The Applicants are "companies" because:

a. with respect to the Canadian Applicants, each is incorporated pursuant to federal or provincial legislation or, in the case of Cinram Fund and CII Trust, is an income trust; and

b. with respect to the U.S. Applicants, each is an incorporated company with certain funds in bank accounts in Canada opened in May 2012 and therefore each is a company having assets or doing business in Canada.

Bell Affidavit at paras. 4, 80, 84, 86, 91, 94, 98, 102, 105, 108, 111, 114, 117, 120, 123, 212; Application Record, Tab 2.

46. The test for "having assets or doing business in Canada" is disjunctive, such that either "having assets" in Canada or "doing business in Canada" is sufficient to qualify an incorporated company as a "company" within the meaning of the CCAA.

47. Having only nominal assets in Canada, such as funds on deposit in a Canadian bank account, brings a foreign corporation within the definition of "company". In order to meet the threshold statutory requirements of the CCAA, an applicant need only be in technical compliance with the plain words of the CCAA.

Re Canwest Global Communications Corp. (2009), 59 C.B.R. (5th) 72 (Ont. Sup. Ct. J. [Commercial List]) at para. 30 [*Canwest Global*]; Book of Authorities of the Applicants ("**Book of Authorities**"), Tab 1.
Re Global Light Telecommunications Ltd. (2004), 2 C.B.R. (5th) 210 (B.C.S.C.) at para. 17 [*Global Light*]; Book of Authorities, Tab 2.

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48. The Courts do not engage in a quantitative or qualitative analysis of the assets or the circumstances in which the assets were created. Accordingly, the use of "instant" transactions immediately preceding a CCAA application, such as the creation of "instant debts" or "instant assets" for the purposes of bringing an entity within the scope of the CCAA, has received judicial approval as a legitimate device to bring a debtor within technical requirements of the CCAA.

> *Global Light*, *supra* at para. 17; Book of Authorities, Tab 2.
> *Re Cadillac Fairview Inc.* (1995), 30 C.B.R. (3d) 29 (Ont. Gen. Div. [Commercial List]) at paras. 5-6; Book of Authorities, Tab 3.
> *Elan Corporation v. Comiskey (Trustee of)* (1990), 1 O.R. (3d) 289 (Ont. C.A.) at paras. 74, 83; Book of Authorities, Tab 4.

(3) The Applicants are insolvent

49. The Applicants are "debtor companies" as defined in the CCAA because they are companies (as set out above) and they are insolvent.

50. The insolvency of the debtor is assessed as of the time of filing the CCAA application. The CCAA does not define insolvency. Accordingly, in interpreting the meaning of "insolvent", courts have taken guidance from the definition of "insolvent person" in Section 2(1) of the *Bankruptcy and Insolvency Act* (the "BIA"), which defines an "insolvent person" as a person (i) who is not bankrupt; and (ii) who resides, carries on business or has property in Canada; (iii) whose liabilities to creditors provable as claims under the BIA amount to one thousand dollars; and (iv) who is "insolvent" under one of the following tests:

a. is for any reason unable to meet his obligations as they generally become due;

b. has ceased paying his current obligations in the ordinary course of business as they generally become due; or

c. the aggregate of his property is not, at a fair valuation, sufficient, or if disposed of at a fairly conducted sale under legal process, would not be sufficient to enable payment of all his obligations, due and accruing due.

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BIA, Section 2 ("insolvent person").

Re Stelco Inc. (2004), 48 C.B.R. (4th) 299 (Ont. Sup. Ct. J.[Commercial List]); leave to appeal to C.A. refused [2004] O.J. No. 1903; leave to appeal to S.C.C. refused [2004] S.C.C.A. No. 336, at para. 4 [*Stelco*]; Book of Authorities, Tab 5.

51. These tests for insolvency are disjunctive. A company satisfying any one of these tests is considered insolvent for the purposes of the CCAA.

Stelco, supra at paras. 26 and 28; Book of Authorities, Tab 5.

52. A company is also insolvent for the purposes of the CCAA if, at the time of filing, there is a reasonably foreseeable expectation that there is a looming liquidity condition or crisis that would result in the company being unable to pay its debts as they generally become due if a stay of proceedings and ancillary protection are not granted by the court.

Stelco, supra at para. 40; Book of Authorities, Tab 5.

53. The Applicants meet both the traditional test for insolvency under the BIA and the expanded test for insolvency based on a looming liquidity condition as a result of the following:

a. The Applicants are unable to comply with certain financial covenants under the Credit Agreements and have entered into a series of waivers with their lenders from December 2011 to June 30, 2012.

b. Were the Lenders to accelerate the amounts owing under the Credit Agreements, the Borrowers and the other Applicants that are Guarantors under the Credit Agreements would be unable to meet their debt obligations. Cinram Fund would be the ultimate parent of an insolvent business.

d. The Applicants have been unable to repay or refinance the amounts owing under the Credit Agreements or find an out-of-court transaction for the sale of the Cinram Business with proceeds that equal or exceed the amounts owing under the Credit Agreements.

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e. Reduced revenues and EBITDA and increased borrowing costs have significantly impaired Cinram's ability to service its debt obligations. There is no reasonable expectation that Cinram will be able to service its debt load in the short to medium term given forecasted net revenues and EBITDA for the remainder of fiscal 2012 and for fiscal 2013 and 2014.

f. The decline in revenues and EBITDA generated by the Cinram Business has caused the value of the Cinram Business to decline. As a result, the aggregate value of the Property, taken at fair value, is not sufficient to allow for payment of all of the Applicants' obligations due and accruing due.

g. The Cash Flow Forecast indicates that without additional funding the Applicants will exhaust their available cash resources and will thus be unable to meet their obligations as they become due.

Bell Affidavit, paras. 23, 179-181, 183, 197-199; Application Record, Tab 2.

(4) The Applicants are affiliated companies with claims outstanding in excess of $5 million

54. The Applicants are affiliated debtor companies with total claims exceeding 5 million dollars. Therefore, the CCAA applies to the Applicants in accordance with Section 3(1).

55. Affiliated companies are defined in Section 3(2) of the CCAA as follows:

a. companies are affiliated companies if one of them is the subsidiary of the other or both are subsidiaries of the same company or each is controlled by the same person; and

b. two companies are affiliated with the same company at the same time are deemed to be affiliated with each other.

CCAA, Section 3(2).

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56. CII, CII Trust and all of the entities listed in Schedule "A" hereto are indirect, wholly owned subsidiaries of Cinram Fund; thus, the Applicants are "affiliated companies" for the purpose of the CCAA.

Bell Affidavit, paras. 3, 71; Application Record, Tab 2.

57. All of the CCAA Parties (except for the Fund Entities) are each a Borrower and/or Guarantor under the Credit Agreements. As at March 31, 2012 there was approximately $252 million of aggregate principal amount outstanding under the First Lien Credit Agreement (plus approximately $12 million in letter of credit exposure) and approximately $12 million of aggregate principal amount outstanding under the Second Lien Credit Agreement. The total claims against the Applicants far exceed $5 million.

Bell Affidavit, paras. 75; Application Record, Tab 2.

B. THE RELIEF IS AVAILABLE UNDER THE CCAA AND CONSISTENT WITH THE PURPOSE AND POLICY OF THE CCAA

(1) The CCAA is Flexible, Remedial Legislation

58. The CCAA is remedial legislation, intended to facilitate compromises and arrangements between companies and their creditors as an alternative to bankruptcy. In particular during periods of financial hardship, debtors turn to the Court so that the Court may apply the CCAA in a flexible manner in order to accomplish the statute's goals. The Court should give the CCAA a broad and liberal interpretation so as to encourage and facilitate successful restructurings whenever possible.

Elan Corp. v. Comiskey, supra at paras. 22 and 56-60; Book of Authorities, Tab 4.
Re Lehndorff General Partners Ltd. (1993), 17 C.B.R. (3d) 24 at para. 5 (Ont. Gen. Div. [Commercial List]); Book of Authorities, Tab 6.
Re Chef Ready Foods Ltd; Chef Ready Foods Ltd. v. Hongkong Bank of Canada (1990), 4 C.B.R. (3d) 311 (B.C.C.A.) at pp. 4 and 7; Book of Authorities, Tab 7.

59. On numerous occasions, courts have held that Section 11 of the CCAA provides the courts with a broad and liberal power, which is at their disposal in order to achieve the overall

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objective of the CCAA. Accordingly, an interpretation of the CCAA that facilitates restructurings accords with its purpose.

> *Re Sulphur Corporation of Canada Ltd.* (2002), 35 C.B.R. (4th) 304 (Alta Q.B.) ("*Sulphur*") at para. 26; Book of Authorities, Tab 8.

60. Given the nature and purpose of the CCAA, this Honourable Court has the authority and jurisdiction to depart from the Model Order as is reasonable and necessary in order to achieve a successful restructuring.

(2) The Stay of Proceedings Against Non-Applicants is Appropriate

61. The relief sought in this application includes a stay of proceedings in favour of Cinram LP and the Applicants' direct and indirect subsidiaries that are also party to an agreement with an Applicant (whether as surety, guarantor or otherwise) (each, a "Subsidiary Counterparty"), including any contract or credit agreement. It is just and reasonable to grant the requested stay of proceedings because:

a. the Cinram Business is integrated among the Applicants, Cinram LP and the Subsidiary Counterparties;

b. if any proceedings were commenced against Cinram LP, or if any of the third parties to such agreements were to commence proceedings or exercise rights and remedies against the Subsidiary Counterparties, this would have a detrimental effect on the Applicants' ability to restructure and implement the Proposed Transaction and would lead to an erosion of value of the Cinram Business; and

c. a stay of proceedings that extends to Cinram LP and the Subsidiary Counterparties is necessary in order to maintain stability with respect to the Cinram Business and maintain value for the benefit of the Applicants' stakeholders.

> Bell Affidavit, paras. 185-186; Application Record, Tab 2.

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62. The purpose of the CCAA is to preserve the *status quo* to enable a plan of compromise to be prepared, filed and considered by the creditors:

> In the interim, a judge has great discretion under the CCAA to make order so as to effectively maintain the status quo in respect of an insolvent company while it attempts to gain the approval of its creditors for the proposed compromise or arrangement which will be to the benefit of both the company and its creditors.
>
> *Lehndorff General Partner Ltd., Re, supra* at para. 5; Book of Authorities, Tab 6.
> *Canwest Global, supra* at para. 27; Book of Authorities, Tab 1.
> CCAA, Section 11.

63. The Court has broad inherent jurisdiction to impose stays of proceedings that supplement the statutory provisions of Section 11 of the CCAA, providing the Court with the power to grant a stay of proceedings where it is just and reasonable to do so, including with respect to non-applicant parties.

> *Lehndorff, supra* at paras. 5 and 16; Book of Authorities, Tab 6.
> *T. Eaton Co., Re* (1997), 46 C.B.R. (3d) 293 (Ont. Gen. Div.) at para. 6; Book of Authorities, Tab 9.

64. The Courts have found it just and reasonable to grant a stay of proceedings against third party non-applicants in a number of circumstances, including:

a. where it is important to the reorganization process;

b. where the business operations of the Applicants and the third party non-applicants are intertwined and the third parties are not subject to the jurisdiction of the CCAA, such as partnerships that do not qualify as "companies" within the meaning of the CCAA;

c. against non-applicant subsidiaries of a debtor company where such subsidiaries were guarantors under the note indentures issued by the debtor company; and

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d. against non-applicant subsidiaries relating to any guarantee, contribution or indemnity obligation, liability or claim in respect of obligations and claims against the debtor companies.

Re Woodward's Ltd. (1993), 17 C.B.R. (3d) 236 (B.C. S.C.) at para. 31; Book of Authorities, Tab 10.
Lehndorff, supra at para. 21; Book of Authorities, Tab 6.
Canwest Global, supra at paras. 28 and 29; Book of Authorities, Tab 1.
Re Sino-Forest Corp. 2012 ONSC 2063 (Commercial List) at paras. 5, 18, and 31; Book of Authorities, Tab 11.
Re MAAX Corp, Initial Order granted June 12, 2008, Montreal 500-11-033561-081, (Que. Sup. Ct. [Commercial Division]) at para. 7; Book of Authorities, Tab 12.

65. The Applicants submit the balance of convenience favours extending the relief in the proposed Initial Order to Cinram LP and the Subsidiary Counterparties. The business operations of the Applicants, Cinram LP and the Subsidiary Counterparties are intertwined and the stay of proceedings is necessary to maintain stability and value for the benefit of the Applicants' stakeholders, as well as allow an orderly, going-concern sale of the Cinram Business as an important component of its reorganization process.

(3) Entitlement to Make Pre-Filing Payments

66. To ensure the continued operation of the CCAA Parties' business and maximization of value in the interests of Cinram's stakeholders, the Applicants seek authorization (but not a requirement) for the CCAA Parties to make certain pre-filing payments, including: (a) payments to employees in respect of wages, benefits, and related amounts; (b) payments to suppliers and service providers critical to the ongoing operation of the business; (c) payments and the application of credits in connection with certain existing customer programs; and (d) intercompany payments among the Applicants related to intercompany loans and shared services. Payments will be made with the consent of the Monitor and, in certain circumstances, with the consent of the Agent.

67. There is ample authority supporting the Court's general jurisdiction to permit payment of pre-filing obligations to persons whose services are critical to the ongoing operations of the debtor companies. This jurisdiction of the Court is not ousted by Section 11.4 of the CCAA, which became effective as part of the 2009 amendments to the CCAA and codified the Court's

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practice of declaring a person to be a critical supplier and granting a charge on the debtor's property in favour of such critical supplier. As noted by Pepall J. in *Re Canwest Global*, the recent amendments, including Section 11.4, do not detract from the inherently flexible nature of the CCAA or the Court's broad and inherent jurisdiction to make such orders that will facilitate the debtor's restructuring of its business as a going concern.

Canwest Global supra, at paras. 41 and 43; Book of Authorities, Tab 1.

68. There are many cases since the 2009 amendments where the Courts have authorized the applicants to pay certain pre-filing amounts where the applicants were not seeking a charge in respect of critical suppliers. In granting this authority, the Courts considered a number of factors, including:

a. whether the goods and services were integral to the business of the applicants;

b. the applicants' dependency on the uninterrupted supply of the goods or services;

c. the fact that no payments would be made without the consent of the Monitor;

d. the Monitor's support and willingness to work with the applicants to ensure that payments to suppliers in respect of pre-filing liabilities are minimized;

e. whether the applicants had sufficient inventory of the goods on hand to meet their needs; and

f. the effect on the debtors' ongoing operations and ability to restructure if they were unable to make pre-filing payments to their critical suppliers.

Canwest Global supra, at para. 43; Book of Authorities, Tab 1.
Re Brainhunter Inc., [2009] O.J. No. 5207 (Sup. Ct. J. [Commercial List]) at para. 21 [*Brainhunter*]; Book of Authorities, Tab 13.
Re Priszm Income Fund (2012), 75 C.B.R. (5th) 213 (Ont. Sup. Ct. J.) at paras. 29-34; Book of Authorities, Tab 14.

69. The CCAA Parties rely on the efficient and expedited supply of products and services from their suppliers and service providers in order to ensure that their operations continue in an

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efficient manner so that they can satisfy customer requirements. The CCAA Parties operate in a highly competitive environment where the timely provision of their products and services is essential in order for the company to remain a successful player in the industry and to ensure the continuance of the Cinram Business. The CCAA Parties require flexibility to ensure adequate and timely supply of required products and to attempt to obtain and negotiate credit terms with its suppliers and service providers. In order to accomplish this, the CCAA Parties require the ability to pay certain pre-filing amounts and post-filing payables to those suppliers they consider essential to the Cinram Business, as approved by the Monitor. The Monitor, in determining whether to approve pre-filing payments as critical to the ongoing business operations, will consider various factors, including the above factors derived from the caselaw.

Bell Affidavit, paras. 226, 228, 230; Application Record, Tab 2.

70. In addition, the CCAA Parties' continued compliance with their existing customer programs, as described in the Bell Affidavit, including the payment of certain pre-filing amounts owing under certain customer programs and the application of certain credits granted to customers pre-filing to post-filing receivables, is essential in order for the CCAA Parties to maintain their customer relationships as part of the CCAA Parties' going concern business.

Bell Affidavit, paras. 234; Application Record, Tab 2.

71. Further, due to the operational integration of the businesses of the CCAA Parties, as described above, there is a significant volume of financial transactions between and among the Applicants, including, among others, charges by an Applicant providing shared services to another Applicant of intercompany accounts due from the recipients of those services, and charges by a Applicant that manufactures and furnishes products to another Applicant of inter-company accounts due from the receiving entity.

Bell Affidavit, paras. 225; Application Record, Tab 2.

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72. Accordingly, the Applicants submit that it is appropriate in the present circumstances for this Honourable Court to exercise its jurisdiction and grant the CCAA Parties the authority to make the pre-filing payments described in the proposed Initial Order subject to the terms therein.

(4) The Charges Are Appropriate

73. The Applicants seek approval of certain Court-ordered charges over their assets relating to their DIP Financing (defined below), administrative costs, indemnification of their trustees, directors and officers, KERP and Support Agreement. The Lenders and the Administrative Agent under the Credit Agreements, the senior secured facilities that will be primed by the charges, have been provided with notice of the within Application. The proposed Initial Order does not purport to give the Court-ordered charges priority over any other validly perfected security interests.

(A) DIP Lenders' Charge

74. In the proposed Initial Order, the Applicants seek approval of the DIP Credit Agreement providing a debtor-in-possession term facility in the principal amount of $15 million (the "DIP Financing"), to be secured by a charge over all of the assets and property of the Applicants that are Borrowers and/or Guarantors under the Credit Agreements (the "Charged Property") ranking ahead of all other charges except the Administration Charge.

75. Section 11.2 of the CCAA expressly provides the Court the statutory jurisdiction to grant a debtor-in-possession ("DIP") financing charge:

> 11.2(1) *Interim financing* - On application by a debtor company and on notice to the secured creditors who are likely to be affected by the security or charge, a court may make an order declaring that all or part of the company's property is subject to a security or charge — in an amount that the court considers appropriate — in favour of a person specified in the order who agrees to lend to the company an amount approved by the court as being required by the company, having regard to its cash-flow statement. The security or charge may not secure an obligation that exists before the order is made.

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> 11.2(2) *Priority* – secured creditors – The court may order that the security or charge rank in priority over the claim of any secured creditor of the company.
>
> *Re Timminco Ltd*. (2012), 211 A.C.W.S. (3d) 881(Ont. Sup. Ct. J. [Commercial List]) at para. 31; Book of Authorities, Tab 15. CCAA, Section 11.2(1) and (2).

76. Section 11.2 of the CCAA sets out the following factors to be considered by the Court in deciding whether to grant a DIP financing charge:

> 11.2(4) Factors to be considered – In deciding whether to make an order, the court is to consider, among other things,
>
> (*a*) the period during which the company is expected to be subject to proceedings under this Act;
>
> (*b*) how the company's business and financial affairs are to be managed during the proceedings;
>
> (*c*) whether the company's management has the confidence of its major creditors;
>
> (*d*) whether the loan would enhance the prospects of a viable compromise or arrangement being made in respect of the company;
>
> (*e*) the nature and value of the company's property;
>
> (*f*) whether any creditor would be materially prejudiced as a result of the security or charge; and
>
> (*g*) the monitor's report referred to in paragraph 23(1)(*b*), if any.
>
> CCAA, Section 11.2(4).

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77. The above list of factors is not exhaustive, and it may be appropriate for the Court to consider additional factors in determining whether to grant a DIP financing charge. For example, in circumstances where funds to be borrowed pursuant to a DIP facility were not expected to be immediately necessary, but applicants' cash flow statements projected the need for additional liquidity, the Court in granting the requested DIP charge considered the fact that the applicants' ability to borrows funds that would be secured by a charge would help retain the confidence of their trade creditors, employees and suppliers.

> *Re Canwest Publishing Inc./Publications Canwest Inc.* (2010), 63 C.B.R. (5th) 115 (Ont. Sup. Ct. J. [Commercial List]) at paras. 42-43 [*Canwest Publishing*]; Book of Authorities, Tab 16.

78. Courts in recent cross-border cases have exercised their broad power to grant charges to DIP lenders over the assets of foreign applicants. In many of these cases, the debtors have commenced recognition proceedings under Chapter 15.

> *Re Catalyst Paper Corporation*, Initial Order granted on January 31, 2012, Court File No. S-120712 (B.C.S.C.) [*Catalyst Paper*]; Book of Authorities, Tab 17.
> *Angiotech, supra*, Initial Order granted on January 28, 2011, Court File No. S-110587; Book of Authorities, Tab 18
> *Re Fraser Papers Inc.*, Initial Order granted on June 18, 2009, Court File No. CV-09-8241-00CL; Book of Authorities, Tab 19.

79. As noted above, pursuant to Section 11.2(1) of the CCAA, a DIP financing charge may not secure an obligation that existed before the order was made. The requested DIP Lenders' Charge will not secure any pre-filing obligations.

80. The following factors support the granting of the DIP Lenders' Charge, many of which incorporate the considerations enumerated in Section 11.2(4) listed above:

a. the Cash Flow Forecast indicates the Applicants will need additional liquidity afforded by the DIP Financing in order to continue operations through the duration of these proposed CCAA Proceedings;

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b. the Cinram Business is intended to continue to operate on a going concern basis during these CCAA Proceedings under the direction of the current management with the assistance of the Applicants' advisors and the Monitor;

c. the DIP Financing is expected to provide the Applicants with sufficient liquidity to implement the Proposed Transaction through these CCAA Proceedings and implement certain operational restructuring initiatives, which will materially enhance the likelihood of a going concern outcome for the Cinram Business;

d. the nature and the value of the Applicants' assets as set out in their consolidated financial statements can support the requested DIP Lenders' Charge;

e. members of the Steering Committee under the First Lien Credit Agreement, who are senior secured creditors of the Applicants, have agreed to provide the DIP Financing;

f. the proposed DIP Lenders have indicated that they will not provide the DIP Financing if the DIP Lenders' Charge is not approved;

g. the DIP Lenders' Charge will not secure any pre-filing obligations;

h. the senior secured lenders under the Credit Agreements affected by the charge have been provided with notice of these CCAA Proceedings; and

i. the proposed Monitor is supportive of the DIP Facility, including the DIP Lenders' Charge.

Bell Affidavit, paras. 199-202, 205-208; Application Record, Tab 2.

(B) Administration Charge

81. The Applicants seek a charge over the Charged Property in the amount of CAD$3.5 million to secure the fees of the Monitor and its counsel, the Applicants' Canadian and U.S. counsel, the Applicants' Investment Banker, the Canadian and U.S. Counsel to the DIP Agent,

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the DIP Lenders, the Administrative Agent and the Lenders under the Credit Agreements, and the financial advisor to the DIP Lenders and the Lenders under the Credit Agreements (the "Administration Charge"). This charge is to rank in priority to all of the other charges set out in the proposed Initial Order.

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82. Prior to the 2009 amendments, administration charges were granted pursuant to the inherent jurisdiction of the Court. Section 11.52 of the CCAA now expressly provides the court with the jurisdiction to grant an administration charge:

> 11.52(1) *Court may order security or charge to cover certain costs*
> On notice to the secured creditors who are likely to be affected by the security or charge, the court may make an order declaring that all or part of the property of a debtor company is subject to a security or charge -- in an amount that the court considers appropriate – in respect of the fees and expenses of
> (a) the monitor, including the fees and expenses of any financial, legal or other experts engaged by the monitor in the performance of the monitor's duties;
>
> (b) any financial, legal or other experts engaged by the company for the purpose of proceedings under this Act; and
>
> (c) any financial, legal or other experts engaged by any other interested person if the court is satisfied that the security or charge is necessary for their effective participation in proceedings under this Act.
>
> 11.52(2) *Priority*
> The court may order that the security or charge rank in priority over the claim of any secured creditor of the company.
>
> CCAA, Section 11.52(1) and (2).

82. Administration charges were granted pursuant to Section 11.52 in, among other cases, *Timminco*, *Canwest Global* and *Canwest Publishing*.

> *Canwest Global*, *supra*; Book of Authorities, Tab 1.
> *Canwest Publishing*, *supra*; Book of Authorities, Tab 16.
> *Re Timminco Ltd.*, 2012 ONSC 106 (Commercial List) [*Timminco*]; Book of Authorities, Tab 20.

84. In *Canwest Publishing*, the Court noted Section 11.52 does not contain any specific criteria for a court to consider in granting an administration charge and provided a list of non-exhaustive factors to consider in making such an assessment. These factors were also considered by the Court in *Timminco*. The list of factors to consider in approving an administration charge include:

a. the size and complexity of the business being restructured;

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

c. whether there is unwarranted duplication of roles;

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

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

f. the position of the Monitor.

Canwest Publishing supra, at para. 54; Book of Authorities, Tab 16.

Timminco, supra, at paras. 26-29; Book of Authorities, Tab 20.

85. The Applicants submit that the Administration Charge is warranted and necessary, and that it is appropriate in the present circumstances for this Honourable Court to exercise its jurisdiction and grant the Administration Charge, given:

a. the proposed restructuring of the Cinram Business is large and complex, spanning several jurisdictions across North America and Europe, and will require the extensive involvement of professional advisors;

b. the professionals that are to be beneficiaries of the Administration Charge have each played a critical role in the CCAA Parties' restructuring efforts to date and will continue to be pivotal to the CCAA Parties' ability to pursue a successful restructuring going forward, including the Investment Banker's involvement in the completion of the Proposed Transaction;

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c. there is no unwarranted duplication of roles;

d. the senior secured creditors affected by the charge have been provided with notice of these CCAA Proceedings; and

e. the Monitor is in support of the proposed Administration Charge.

Bell Affidavit, paras. 188, 190; Application Record, Tab 2.

(C) Directors' Charge

86. The Applicants seek a Directors' Charge in an amount of CAD$13 over the Charged Property to secure their respective indemnification obligations for liabilities imposed on the Applicants' trustees, directors and officers (the "Directors and Officers"). The Directors' Charge is to be subordinate to the Administration Charge and the DIP Lenders' Charge but in priority to the KERP Charge and the Consent Consideration Charge.

87. Section 11.51 of the CCAA affords the Court the jurisdiction to grant a charge relating to directors' and officers' indemnification on a priority basis:

> 11.51(1) *Security or charge relating to director's indemnification*
> On application by a debtor company and on notice to the secured creditors who are likely to be affected by the security or charge -- in an amount that the court considers appropriate -- in favour of any director or officer of the company to indemnify the director or officer against obligations and liabilities that they may incur as a director or officer of the company after the commencement of proceedings under this Act.
>
> 11.51(2) *Priority*
> The court may order that the security or charge rank in priority over the claim of any secured creditors of the company
>
> 11.51(3) *Restriction* -- indemnification insurance
> The court may not make the order if in its opinion the company could obtain adequate indemnification insurance for the director or officer at a reasonable cost.
>
> 11.51(4) *Negligence, misconduct or fault*
> The court shall make an order declaring that the security or charge

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> does not apply in respect of a specific obligation or liability incurred by a director or officer if in its opinion the obligation or liability was incurred as a result of the director's or officer's gross negligence or wilful misconduct or, in Quebec, the director's or officer's gross or intentional fault.
>
> CCAA, Section 11.51.

88. The Court has granted director and officer charges pursuant to Section 11.51 in a number of cases. In *Canwest Global*, the Court outlined the test for granting such a charge:

> I have already addressed the issue of notice to affected secured creditors. I must also be satisfied with the amount and that the charge is for obligations and liabilities the directors and officers may incur after the commencement of proceedings. It is not to extend to coverage of wilful misconduct or gross negligence and no order should be granted if adequate insurance at a reasonable cost could be obtained.
>
> *Canwest Global, supra* at paras 46-48; Book of Authorities, Tab 1.
> *Canwest Publishing, supra* at paras. 56-57; Book of Authorities, Tab 16.
> *Timminco, supra* at paras. 30-36; Book of Authorities, Tab 20.

89. The Applicants submit that the D&O Charge is warranted and necessary, and that it is appropriate in the present circumstances for this Honourable Court to exercise its jurisdiction and grant the D&O Charge in the amount of CAD$13 million, given:

a. the Directors and Officers of the Applicants may be subject to potential liabilities in connection with these CCAA proceedings with respect to which the Directors and Officers have expressed their desire for certainty with respect to potential personal liability if they continue in their current capacities;

b. renewal of coverage to protect the Directors and Officers is at a significantly increased cost due to the imminent commencement of these CCAA proceedings;

c. the Directors' Charge would cover obligations and liabilities that the Directors and Officers, as applicable, may incur after the commencement of these CCAA Proceedings and is not intended to cover wilful misconduct or gross negligence;

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d. the Applicants require the continued support and involvement of their Directors and Officers who have been instrumental in the restructuring efforts of the CCAA Parties to date;

e. the senior secured creditors affected by the charge have been provided with notice of these CCAA proceedings; and

f. the Monitor is in support of the proposed Directors' Charge.

Bell Affidavit, paras. 249, 250, 254-257 ; Application Record, Tab 2.

(D) KERP Charge

90. The Applicants seek a KERP Charge in an amount of CAD$3 million over the Charged Property to secure the KERP Retention Payments, KERP Transaction Payments and Aurora KERP Payments payable to certain key employees of the CCAA Parties crucial for the CCAA Parties' successful restructuring.

91. The CCAA is silent with respect to the granting of KERP charges. Approval of a KERP and a KERP charge are matters within the discretion of the Court. The Court in *Re Grant Forest Products Inc.* considered a number of factors in determining whether to grant a KERP and a KERP charge, including:

a. whether the Monitor supports the KERP agreement and charge (to which great weight was attributed);

b. whether the employees to which the KERP applies would consider other employment options if the KERP agreement were not secured by the KERP charge;

c. whether the continued employment of the employees to which the KERP applies is important for the stability of the business and to enhance the effectiveness of the marketing process;

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d. the employees' history with and knowledge of the debtor;

e. the difficulty in finding a replacement to fulfill the responsibilities of the employees to which the KERP applies;

f. whether the KERP agreement and charge were approved by the board of directors, including the independent directors, as the business judgment of the board should not be ignored;

g. whether the KERP agreement and charge are supported or consented to by secured creditors of the debtor; and

h. whether the payments under the KERP are payable upon the completion of the restructuring process.

Re Grant Forest Products Inc. (2009), 57 C.B.R. (5th) 128 (Ont. Sup. Ct. J [Commercial List]) at para. 8-24 [*Grant Forest*]; Book of Authorities, Tab 21.
Canwest Publishing supra, at paras 59; Book of Authorities, Tab 16.
Canwest Global supra, at para. 49; Book of Authorities, Tab 1.
Re Timminco Ltd. (2012), 95 C.C.P.B. 48 (Ont. Sup. Ct. J [Commercial List]) at paras. 72-75; Book of Authorities, Tab 22.

92. The purpose of a KERP arrangement is to retain key personnel for the duration of the debtor's restructuring process and it is logical for compensation under a KERP arrangement to be deferred until after the restructuring process has been completed, with "staged bonuses" being acceptable. KERP arrangements that do not defer retention payments to completion of the restructuring may also be just and fair in the circumstances.

Grant Forest, *supra* at para. 22-23; Book of Authorities, Tab 21.

93. The Applicants submit that the KERP Charge is warranted and necessary, and that it is appropriate in the present circumstances for this Honourable Court to exercise its jurisdiction and grant the KERP Charge in the amount of CAD$3 million, given:

a. the KERP was developed by Cinram with the principal purpose of providing an incentive to the Eligible Employees, the Eligible Officers, and the Aurora

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Employees to remain with the Cinram Group while the company pursued its restructuring efforts;

b. the Eligible Employees and the Eligible Officers are essential for a restructuring of the Cinram Group and the preservation of Cinram's value during the restructuring process;

c. the Aurora Employees are essential for an orderly transition of Cinram Distribution's business operations from the Aurora facility to its Nashville facility;

d. it would be detrimental to the restructuring process if Cinram were required to find replacements for the Eligible Employees, the Eligible Officers and/or the Aurora Employees during this critical period;

e. the KERP, including the KERP Retention Payments, the KERP Transaction Payments and the Aurora KERP Payments payable thereunder, not only provides appropriate incentives for the Eligible Employees, the Eligible Officers and the Aurora Employees to remain in their current positions, but also ensures that they are properly compensated for their assistance in Cinram's restructuring process;

f. the senior secured creditors affected by the charge have been provided with notice of these CCAA proceedings; and

g. the KERP has been reviewed and approved by the board of trustees of Cinram Fund and is supported by the Monitor.

Bell Affidavit, paras. 236-239, 245-247; Application Record, Tab 2.

(E) Consent Consideration Charge

94. The Applicants request the Consent Consideration Charge over the Charged Property to secure the Early Consent Consideration. The Consent Consideration Charge is to be subordinate

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in priority to the Administration Charge, the DIP Lenders' Charge, the Directors' Charge and the KERP Charge.

95. The Courts have permitted the opportunity to receive consideration for early consent to a restructuring transaction in the context of CCAA proceedings payable upon implementation of such restructuring transaction. In *Sino-Forest*, the Court ordered that any noteholder wishing to become a consenting noteholder under the support agreement and entitled to early consent consideration was required to execute a joinder agreement to the support agreement prior to the applicable consent deadline. Similarly, in these proceedings, lenders under the First Lien Credit Agreement who execute the Support Agreement (or a joinder thereto) and thereby agree to support the Proposed Transaction on or before July 10, 2012, are entitled to Early Consent Consideration earned on consummation of the Proposed Transaction to be paid from the net sale proceeds.

> *Sino-Forest, supra*, Initial Order granted on March 30, 2012, Court File No. CV-12-9667-00CL at para. 15; Book of Authorities, Tab 23. Bell Affidavit, para. 176; Application Record, Tab 2.

96. The Applicants submit it is appropriate in the present circumstances for this Honourable Court to exercise its jurisdiction and grant the Consent Consideration Charge, given:

a. the Proposed Transaction will enable the Cinram Business to continue as a going concern and return to a market leader in the industry;

b. Consenting Lenders are only entitled to the Early Consent Consideration if the Proposed Transaction is consummated; and

c. the Early Consent Consideration is to be paid from the net sale proceeds upon distribution of same in these proceedings.

> Bell Affidavit, para. 176; Application Record, Tab 2.

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