CITATION: PCAS Patient Care Automation Services Inc. (Re), 2012 ONSC 3367
COURT FILE NO.: CV-12-9656-00CL
DATE: 20120609

SUPERIOR COURT OF JUSTICE – ONTARIO

COMMERCIAL LIST

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 PCAS Patient Care Automation Services Inc. and 2163279 Ontario Inc., Applicants

BEFORE: D. M. Brown J.

COUNSEL: S. Babe and I. Aversa, for the Applicants

M. Wasserman and J. MacDonald, for the Monitor, PricewaterhouseCoopers Inc.

J. Porter and A. Shepherd, for 2320714 Ontario Inc., the DIP Lender

B. O'Neill, for Castcan Investments (secured creditor)

R. M. Slattery, for Royal Bank of Canada (secured creditor)

M. Laugesen and G. Finlayson, for the Successful Bidder, DashRx, LLC

C. Besant, for Walgreen Co.

A. Scotchmer, for Lanworks Inc.

P. Saunders, a shareholder, for himself and other shareholders

B. Jaffe, for Merge, a potential bidder

S-A. Wilson, for Dan Brintnell, a shareholder

HEARD: June 5 and 6, 2012

REASONS FOR DECISION

I. Request for sale approval, vesting and distribution orders under the *CCAA*

[1] PCAS Patient Care Automation Services Inc. and 2163279 Ontario Inc. move under the *Companies' Creditors Arrangement Act* for orders approving the agreement of purchase and sale between the Applicants and DashRx, LLC ("DashRx") dated May 29, 2012 (the "Purchase

Agreement"), vesting the Purchased Assets in DashRx and distributing the sale proceeds, together with certain other related orders, including the termination of this *CCAA* proceeding.

[2] At the continuation of the hearing on June 6, 2012, I granted the requested orders. These are my reasons for so doing.

II. The proposed sale

A. The sales and investor solicitation process

[3] The Applicants are healthcare technology companies which were developing an automated pharmacy dispensing platform. They were in the pre-commercialization phase of operations and encountered financing difficulties. The Initial Order under the *CCAA* was made by Morawetz J. on March 23, 2012; it appointed PricewaterhouseCoopers Inc. as Monitor.

[4] The subsequent history of this matter is set out my previous Reasons.[1]

[5] On May 14, 2012, I approved a sale and investor solicitation process ("SISP"). The Applicants developed the SISP with the assistance of the Monitor, the Monitor's agent, PricewaterhouseCoopers Corporate Finance Inc. ("PwCCF") and the DIP Lender. The SISP sought to maximize stakeholder value either through (i) a going concern sale of the Applicants' business and assets or (ii) new investment and a plan of compromise or arrangement. The SISP set out the procedural and substantive requirements for a qualified purchase or investment bid (a "Qualified Bid").

[6] A feature of the approved SISP was the DIP Lender's "stalking horse" bid under which the DIP Lender would pay the Stalking Horse Price by a release of the DIP Indebtedness and the assumption of the outstanding senior secured claims. The terms of the Stalking Horse Bid were not required to be emulated in other Qualified Bids; the Stalking Horse Bid served to set a floor price in the SISP. The Stalking Horse Agreement was posted in the Applicants' data-room.

[7] The SISP was conducted by the Applicants with the support and assistance of the Monitor. Under the terms of the SISP, bids were due by 12:00 p.m. on May 24, 2012. Two bids, including the DashRx bid, were received before the Bid Deadline, and one further bid was received on May 24, 2012, but after the Bid Deadline. These three bids were reviewed in a series of meetings held by the Applicants, the DIP Lender, the Monitor and their counsel on May 24 and May 25, 2012.

[8] In a Confidential Appendix to its Seventh Report the Monitor described the financial terms of each bid and disclosed the materials filed by each bidder, as well as the written communications with each bidder.

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[1] April 20, 2012 (2012 ONSC 2423); May 5, 2012 (2012 ONSC 2714); May 8 (2012 ONSC 2778); May 14, 2012 (2012 ONSC 2840); May 28, 2012 (2012 ONSC 3147).

B. The Unsuccessful Bids

[9] As described in detail in the evidence, the bid submitted by Unsuccessful Bidder 1 was received the evening of May 24, but provided no cash consideration to the Applicants. On the evening of May 25, 2012, Applicants' counsel sent a letter to Unsuccessful Bidder 1 advising that its bid was not a Qualified Bid and that certain additional details would need to be provided before it could be considered a Qualified Bid. Unsuccessful Bidder 1 did not respond to the request for clarification and its bid was not treated as a Qualified Bid.

[10] By letter dated May 23 Unsuccessful Bidder 2 offered to buy PCAS for cash. On May 23 the Applicants wrote to Unsuccessful Bidder 2 about how it would need to alter its bid to satisfy the requirements for a Qualified Bid in the SISP. Notwithstanding follow-up communications, Unsuccessful Bidder 2 did not respond to the Applicants' inquiries until Sunday, May 27, 2012 and it did not provide any material new information. The bid by Unsuccessful Bidder 2 therefore was not treated as a Qualified Bid under the SISP.

C. The Successful Bid

The purchaser

[11] DashRx is a Delaware limited liability corporation formed by a large, California-based investment fund to purchase the assets of the Applicants. The fund's Investment Manager has approximately US$500 million in assets under management, almost exclusively in the health care and pharmaceutical sectors.

[12] On May 24, 2012, prior to the bid deadline, DashRx submitted a version of the Purchase Agreement. It was the only bid received in the form of a formal asset purchase agreement. DashRx also remitted a cash deposit to the Monitor.

[13] The Investment Manager had been performing due diligence and engaging in talks with the Applicants for several months prior to the commencement of the *CCAA* proceedings with an aim to investing in or purchasing PCAS. A major U.S. retail pharmacy chain, Walgreen Co. is participating in the Successful Bid as a substantial investor in DashRx. Walgreen was the potential large U.S. customer identified in previous evidence in this proceeding.

[14] The Monitor requested that it be allowed to reveal the name of the Investment Manager; the latter expressed a strong preference that its identity not be disclosed. Against that background the Monitor reported that it had requested independent evidence of the financial position of the Investment Manager:

> [T]he Monitor has received additional information regarding the Investment Manager and is satisfied that the Purchaser should have the financial wherewithal to close the transaction. The Purchaser and Walgreens have shown their commitment by jointly paying the deposit and agreeing to fund the operating needs of the Company to June 6, 2012 (with a cap of $250,000). The Monitor also notes that Walgreens' participation provides another source of financial support to the Purchaser.

[15] By May 27, 2012, following further negotiations and an enhancement of the DashRx bid to permit some recovery for unsecured creditors, the material terms of the DashRx Purchase Agreement were settled to a point that the Applicants, in consultation with the DIP Lender and the Monitor, were prepared to recognize the Purchase Agreement as a Qualified Bid, as a bid superior to the Stalking Horse Bid, and to identify it as the Successful Bid under the SISP, subject to final negotiation of the APA.

[16] The Purchase Agreement was finalized, executed and delivered by the parties on June 1, 2012. DashRx committed to provide $250,000 to fund the Applicants' operations from May 31, 2012 until closing on June 6. That funding was received on May 31, 2012.

Purchased and Excluded Assets

[17] Under the Purchase Agreement the purchaser will acquire Purchased Assets on an "as is, where is" basis. Certain tax credit entitlements are treated as Excluded Assets.

The purchase price and consideration

[18] The consideration payable under the Purchase Agreement is a combination of the assumption of secured liabilities, cash, and the issuance of secured and unsecured convertible promissory notes to the Applicants' creditors, including unsecured creditors. The Applicants do not expect that there will be any surplus proceeds from the transaction for PCAS shareholders.

[19] The cash portion of the purchase price is designated for:

(i) distribution in payment of all statutory priority claims, comprised of approximately $235,000 in accrued and unpaid vacation pay;

(ii) distribution to the DIP Lender to be used by the DIP Lender:

a. first, to obtain the consent of the Senior Secured Creditors, RBC and Castcan, to the discharge of their security interests and charges over the Purchased Assets and to obtain their consent for the issuance of an approval and vesting order in respect of the Sale Agreement; and,

b. as to the balance, in partial satisfaction of the DIP Indebtedness;

(iii) payment of the amounts payable under the court-approved key employee retention plan; and

(iv) payment of $100,000 to the Applicants, in trust for a trustee in bankruptcy to be appointed in respect of the Applicants, and the other direct and indirect subsidiaries of PCAS, to pay for the costs of administering their anticipated bankruptcies

[20] The non-cash portion of the purchase price in the transaction will be comprised of:

(i) the assumption of the secured obligations to IBM;

(ii) interest-bearing promissory notes issued in favour of the DIP Lender, secured against the assets of DashRx and ranking junior only to the secured assumed obligations to IBM ("Secured Note"); and,

(iii) interest-bearing unsecured promissory notes issued to the Applicants, in trust, for the pool of unsecured creditors of the Applicants ("Unsecured Note").

[21] At the commencement of the hearing on June 5 one unsecured creditor, Lanworks, raised concerns about the lack of transparency regarding the terms of the Unsecured Notes. The details of the terms of the Notes had been placed in the Monitor's Confidential Appendix. Prior to the resumption of the hearing on June 6 Lanworks was provided with information about the terms of the Unsecured Note, as a result of which Lanworks indicated that it neither consented to nor opposed the orders sought. The terms of the Secured and Unsecured Notes were finalized by the time of the continuation of the hearing on June 6.

Proposed releases

[22] In its Seventh Report the Monitor noted that under the terms of the Purchase Agreement certain claims against former employees of the Applicants were included in the Purchased Assets and the Agreement required the Applicants to deliver a broad release in favour of the Purchaser and related parties. The Monitor observed that the releases were negotiated as part of the comprehensive arrangements in respect of the transactions contemplated by the Agreement.

Proposed occupancy agreements

[23] A condition of the Sale Agreement was that PCAS provided DashRx with post-Closing occupancy and access to the Applicants' leased premises at 2440 Winston Park Drive. DashRx will pay all rent and other occupancy costs and will indemnify the Applicants. The Applicants are seeking approval of, and authorization to enter into, an occupancy agreement with DashRx.

III. The proposed distribution of sale proceeds

[24] The Applicants seek an order under which the sale proceeds would be distributed to the following persons or groups:

(i) To use $235,315 to satisfy statutory priority claims relating to employee accrued and unpaid vacation pay claims;

(ii) To pay the cash component of the purchase price to the DIP Lender to be used by the DIP Lender (i) to obtain the consent of the secured creditors, RBC and Castcan Investments Inc., to discharge their security interests and charges over the Purchased Assets and (ii) as to the balance, to make partial repayment of the DIP Lending Facility;

(iii) To distribute $261,000 to the beneficiaries of the KERP Charge; and,

(iv) To pay $100,000 to PwC, the proposed Trustee in Bankruptcy, for fees in connection with the anticipated bankruptcies of the Applicants.

Payment to the DIP Lender

[25] The only parties claiming interests in priority to the DIP Lender are IBM, RBC and Castcan. The Purchaser will assume the liability for IBM. As to RBC and Castcan, at the time the DIP Lending Facility was put in place the DIP Lender negotiated a Pari Passu Agreement with RBC and Castcan. An issue arose concerning the validity of the security taken by Castcan in respect of certain assets, specifically Harmonized Sales Tax Refunds (the "HST Refunds"). I will discuss that issue in more detail below. For present purposes, suffice it to say that the Applicants propose that upon paying out the claims of the Senior Secured Creditors from the cash proceeds received on Closing, the DIP Lender will be subrogated to and/or take an assignment of the Senior Secured Creditor's claims. The Applicants are expected to receive sizable tax credit entitlements within a matter of weeks. Those entitlements are Excluded Assets under the Purchase Agreement. As a result, any claims on them will not be vested out by operation of the proposed Approval and Vesting Order.

[26] Against this background the Applicants seek an order authorizing and directing them, and any Trustee, to distribute to the DIP Lender amounts equal to any specified tax credit entitlements received. Such distributions would enable the DIP Lender to recoup part of the purchase price it will flow through to one of the Senior Secured Creditors – Castcan - on Closing.

[27] If the aggregate amount of all tax credit entitlements received by the Applicants/Trustee post-Closing and distributed to the DIP Lender end up being less than the aggregate amount that the DIP Lender paid to RBC and Castcan out of the cash proceeds of the Transaction on Closing, then the DIP Lender will be issued an Additional Secured Note to cover the difference. The amount of the Additional Secured Note will come out of the pool of funds otherwise set aside for the unsecured creditors of the Applicants. The Unsecured Note therefore will be less than the total pool of possible proceeds for unsecured creditors, and an additional Unsecured Note will be issued to the Trustee for the benefit of the unsecured creditors once the face amount of the Additional Secured Note is known.

[28] Although the DIP Indebtedness is not being paid out in full on Closing, the DIP Lender has consented to the payments of cash on account of the KERP and the future costs of bankruptcy estate administration.

[29] Under the Initial Order the Directors' Charge ranked ahead of the KERP Charge. The Applicants asked the Court to terminate the Directors' Charge. Those benefiting from the Directors' Charge did not oppose that request.

KERP employees

[30] The KERP originally benefitted twenty employees and allowed for a total maximum allocation of $500,000. The KERP was to be paid in the following installments: (i) 20% upon the raising of $8,000,000 for funding the DIP Facility, and PCAS receiving the authorization of this Court to borrow up to or in excess of that amount; (ii) 20% at the midway mark of the SISP; and, (iii) the balance of 60% upon the earliest of (i) the closing of a

sale of all or substantially all of the assets, property and undertaking of the Applicants, or (ii) Court approval and sanction of a plan of arrangement or compromise in the *CCAA* Proceedings.

[31] The commitment under the DIP Facility never reached $8 million, so the initial payment was not made. The second scheduled 20% payment was made on May 25, 2012. Payment of the 60% balance will be made from the cash proceeds on closing. Due to attrition, only sixteen employees remain in the KERP. The final 60% installment payable from the transaction proceeds will total $242,100, resulting in total KERP payments of $322,800.

IV. Positions of the Parties

[32] The Senior Secured Creditors supported the orders sought by the Applicants. The Monitor recommended that the Court grant the orders. As noted, one unsecured creditor, Lanworks, sought to obtain further information and, on so doing, advised that it neither consented to nor opposed the orders sought. No other creditors appeared on the return of the motion.

[33] The hearing of the motion started at 4:45 p.m. on June 5, 2012. At that time Mr. Peter Saunders, a shareholder, stated that he appeared on behalf of himself and other shareholders. He read a statement which expressed concern about the bidding process, and Mr. Saunders indicated that he and other shareholders would be meeting with counsel at 8:00 a.m. on June 6. Over the opposition of the Applicants and the Purchaser, I adjourned the hearing to June 6 at 10:00 a.m.

[34] On June 6 Mr. Saunders returned, but without counsel. Ms. Wilson appeared for the first time on behalf of another shareholder, Mr. Dan Brintnell, and asked to make submissions. Also, Mr. Jaffe appeared on behalf of a potential bidder, Merge, which had not participated in the SISP and asked for leave to submit an offer. What then transpired was described in the following portions of my handwritten endorsement of June 6:

> This is the continuation of the approval/vesting/distribution motion commenced yesterday @ 4:45 p.m. At yesterday's hearing I asked questions of counsel for the applicants, Monitor and DIP lender on certain points and was provided answers.
>
> …
>
> Yesterday Mr. Peter Saunders, a shareholder, on behalf of himself and some other SHs, read a statement dated June 5/12 expressing concern about the bidding process. Mr. Saunders indicated they would be meeting counsel today @ 8 a.m. I adj'd the matter to 10 a.m. today to facilitate that meeting. This morning Mr. Saunders advised that counsel was unable to meet them; they plan to meet this afternoon. Mr. Saunders indicated that their counsel would like a 5-day adjm't of this motion.
>
> I will not grant the requested adjm't. By reasons dated May 14/12 I approved the SISP. By reasons dated May 28 I granted an extension of the stay until June 6. Both Reasons made clear the urgent nature of the SISP in the particular circumstances of these companies. No appeal was taken from, nor stay sought in respect of, either order. The public portion of the present motion materials provide detailed information about the

conduct of the SISP and the bids. The portions sought to be sealed meet the test in *Sierra Club*. From previous motions I am aware that the applicants have communicated frequently with shareholders; the Monitor has posted all materials on its website.

I am satisfied in the circumstances reasonable notice of this motion and the SISP has been given to all affected parties. The shareholders have not previously participated; that was their choice. It is unreasonable for them to seek to adjourn matters at this stage. The applicants run out of money tomorrow; the shareholders offer no concrete alternative.

After writing these Reasons, on my return to Court, I was advised by counsel for Merge that they only learned of the sale process on May 30 and now wish to tender an Offer. I did not accept the Offer. The SISP was an open and transparent process. The OCA in *Soundair* spoke about the need to maintain the integrity of a court-approved sale process.[2] I am not prepared to accept an offer at this late stage. I note [that] Merge did not have counsel at yesterday's hearing.

Ms. Wilson appeared for a SH, Dan Brintnell. After obtaining instructions, Ms. Wilson advised she had no further submissions.

V. Analysis of the proposed sale transaction

A. Guiding legal principles

[35] In most circumstances resort is made to the *CCAA* to "permit the debtor to continue to carry on business and, where possible, avoid the social and economic costs of liquidating its assets" and to create "conditions for preserving the *status quo* while attempts are made to find common ground amongst stakeholders for a reorganization that is fair to all". The reality, however, is that "reorganizations of differing complexity require different legal mechanisms." This has led courts to recognize that the *CCAA* may be used to sell substantially all of the assets of a debtor company to preserve it as a going concern under new ownership, or to wind-up or liquidate it.[3]

[36] The portions of section 36 of the *CCAA* relevant to this proposed sale to a non-related person are as follows:

> 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.

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[2] *Royal Bank v. Soundair* (1991), 4 O.R. (3d) 1 (C.A.). See in particular the Reasons of Galligan J.A. at pp. 7d to 10c.

[3] See the cases summarized in *First Leaside Wealth Management Inc. (Re)*, 2012 ONSC 1299, para. 32.

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

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

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

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

(*c*) whether the monitor filed with the court a report stating that in their opinion the sale or disposition would be more beneficial to the creditors than a sale or disposition under a bankruptcy;

(*d*) the extent to which the creditors were consulted;

(*e*) the effects of the proposed sale or disposition on the creditors and other interested parties; and

(*f*) whether the consideration to be received for the assets is reasonable and fair, taking into account their market value.

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

(7) The court may grant the authorization only if the court is satisfied that the company can and will make the payments that would have been required under paragraphs 6(4)(*a*) and (5)(*a*) if the court had sanctioned the compromise or arrangement.

B. Consideration of the factors

Was notice of the application given to the secured creditors who are likely to be affected by the proposed sale or disposition?

[37] The applicants have satisfied this requirement. The Purchaser will assume the liability owing to IBM Canada. The other two secured creditors, RBC and Castcan, support the proposed transaction.

The reasonableness of the process leading to the proposed sale

[38] The SISP was approved by this Court by order made May 14, 2012. In my Reasons of that date I stated:

> Given the extensive efforts to date by management of the applicants to solicit interest in the business and given the liquidity crunch facing the applicants, I was satisfied that the

> proposed SISP would result, in the specific circumstances of this case, in a fair, transparent and commercially efficacious process which should allow a sufficient opportunity for interested parties to come forward with a superior offer and thereby optimize the chances of securing the best possible price for the assets up for sale or the best possible investment in the continuing operations of the applicants. For those reasons I approved the SISP.[4]

[39] Although the applicants took the lead in running the SISP, the evidence disclosed that the Monitor was involved in all stages of the process.

[40] Before the commencement of these *CCAA* proceedings, members of the PCAS Board of Directors had engaged in separate dialogues with a significant number of parties who were interested in either investing in the DIP Lender to provide financing to the Applicants, purchasing the assets of the Applicants, or buying PCAS. During the SISP PCAS, with the assistance of PwCCF and the Monitor, (i) ran an electronic due diligence data-room, (ii) identified 184 potential bidders from around the globe and contacted 164 of them, (iii) developed a "teaser" which was circulated to 121 of the identified parties, as well as a confidential information memorandum which was posted to the data room and sent to the all of the 18 interested parties who had executed a non-disclosure agreement, (iv) conducted site tours at its Premises, with the Monitor in attendance, for seven potential bidders, (v) developed a non-reliance letter for Qualified Bidders to sign in order to be able to review third-party review of the PCAS technology prepared for the Board and facilitated meetings with the authors of the Technology Review at the request of two potential bidders.

[41] In its Sixth Report dated May 28, 2012 the Monitor described in detail the steps taken up until that point of time in conducting the SISP. The Monitor provided updated information in its Seventh Report dated June 1, 2012. In its Confidential Appendix to the Seventh Report the Monitor presented detailed, un-redacted information about the bids which were tendered, the resulting communications with the bidders, and its comparative evaluation of the bids.

[42] I am satisfied that the SISP run by the Applicants, with the extensive involvement of the Monitor, complied with the terms of the SISP approved in my May 14 Order.

[43] As mentioned, on the continuation of the approval hearing on June 6 counsel appeared for a potential bidder, Merge, seeking to submit an offer on behalf of his client. In *Royal Bank of Canada v. Soundair*, in the context of an approval motion for a sale by a court-appointed receiver, Galligan J. considered the approach which a court should take where a second offer was made after a receiver had entered into an agreement of purchase and sale. He cited two judgments by Saunders J. which had held that the court should consider the second offer, if constituting a "substantially higher bid",[5] and Galligan J.A. continued:

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[4] 2012 ONSC 2840, para. 19.

[5] *Re Selkirk* (1986), 58 C.B.R. (N.S.) 245 (Ont. Bkcy.); *Re Beauty Counsellors of Canada Ltd.* (1986), 58 C.B.R. (N.S.) 237 (Ont. Bkcy.)

> What those cases show is that the prices in other offers have relevance only if they show that the price contained in the offer accepted by the receiver was so unreasonably low as to demonstrate that the receiver was improvident in accepting it. I am of the opinion, therefore, that if they do not tend to show that the receiver was improvident, they should not be considered upon a motion to confirm a sale recommended by a court-appointed receiver. If they were, the process would be changed from a sale by a receiver, subject to court approval, into an auction conducted by the court at the time approval is sought. In my opinion, the latter course is unfair to the person who has entered bona fide into an agreement with the receiver, can only lead to chaos, and must be discouraged.
>
> If, however, the subsequent offer is so substantially higher than the sale recommended by the receiver, then it may be that the receiver has not conducted the sale properly. In such circumstances, the court would be justified itself in entering into the sale process by considering competitive bids. However, I think that that process should be entered into only if the court is satisfied that the receiver has not properly conducted the sale which it has recommended to the court.[6]

[44] In the present case I departed from the process described in the *Soundair* case and declined to accept Merge's offer for consideration. The facts in *Soundair* are quite distinguishable. In the *Soundair* case the second bidder had secured a court order permitting it to make an offer. By contrast, in the present case the court had approved a SISP which set a May 24, 2012 bid deadline. All other bids complied, or came very close to complying, with that court-approved deadline. Merge contended that it did not learn of the bidding process until May 30, a week after the bid deadline. The prompt posting of all court orders on the Monitor's website, when combined with Merge's delays in pursuing an offer after learning of this proceeding make it completely unreasonable for Merge to expect that a court would grant it leave to submit an offer for consideration. The court-approved SISP would be stood on its head were that allowed.

[45] Moreover, as was apparent from the Monitor's detailed narration of the consideration given to the bids which were filed on or just after the court-approved bid deadline, time was spent during the SISP process for discussions amongst the Applicants, the Monitor and the bidders to ascertain whether their bids constituted Qualified Bids. The stay of proceedings in this case was set to expire on June 6, the date Merge came forth in court with its offer. The only cash available for Applicants' operations through to June 6 was the advance of $250,000 by the Purchaser to the Applicants on May 31. The Applicants stated that they would be out of funds by day's end on June 6 or early on June 7. Consequently, there was no realistic prospect that any offer tendered on June 6 could receive a measured consideration while the companies continued to operate.

[46] Finally, Merge did not tender its offer at the commencement of the approval motion on June 5. Its counsel made no submissions that day nor signed the counsel sheet. The only reason

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[6] *Soundair, supra*., pp. 9h-10c.

I adjourned the hearing to June 6 was to afford some shareholders a brief opportunity to consult with counsel. I made it clear on the record on June 5 that hearing from those shareholders was the only order of business for June 6. Merge did not come forth until the resumption of the hearing on June 6. In those circumstances it was difficult to treat Merge's proffer of a bid as a serious one.

[47] In sum, the compliance of the Applicants with the court-approved SISP and the unreasonableness of the timing of Merge's offer led me to conclude that the process leading to the proposed sale was reasonable.

Did the Monitor approve the process leading to the proposed sale or disposition?

[48] In its Fifth Report dated May 11, 2012 the Monitor recommended approving the SISP.

Did the Monitor file with the court a report stating that in its opinion the sale or disposition would be more beneficial to the creditors than a sale or disposition under a bankruptcy?

[49] In its Seventh Report the Monitor set out at some length its views about the proposed sale transaction:

> The Monitor is of the view that the transaction contemplated by the APA meets the factors set out in section 36(3) of the *CCAA*. As previously described in the Fifth Report and the Sixth Report, the Monitor is of the view that an expedited SISP was likely the only viable process to maximize the value of the Company for the benefit of its stakeholders given the Company's dire liquidity situation.
>
> The APA provides for a going concern sale of the Company's business that maintains some Canadian operations and should allow for some continued employment.
>
> The Company and the DIP Lender developed the SISP in consultation with Monitor and, in the Monitor's view, the Company implemented a fair, transparent and efficient SISP in the circumstances in accordance with the Orders of this Court and the Court's reasons for decision dated May 14, 2012. Given the Company's liquidity situation, the necessity of implementing an expedited SISP and the bids received, it is the Monitor's view that the price obtained for the Company's assets is fair and reasonable in the circumstances. In addition, as reported in the Second Report, the Monitor is of the view that it is unlikely that a Trustee would have been able to appropriately take possession, market and sell the technology, intellectual property and other assets of the Company as a result of the Company having effectively no cash, limited accounts receivable and few unencumbered assets available to be monetized quickly in liquidation.

The Monitor recommended approving the Successful Bid.

To what extent were the creditors consulted?

[50] The record disclosed that discussions had taken place with the secured creditors. Appropriate notice was given by the Applicants of all steps taken to seek approval of the DIP Lending Facility, the various extensions of the stay and approval of the SISP. As noted, only one

unsecured creditor appeared at the approval hearing and its information questions were answered.

What are the effects of the proposed sale or disposition on the creditors and other interested parties?

[51] As summarized by the Monitor in its Seventh Report:

> The APA does not provide for any recovery for the Company's shareholders. The APA provides as follows:
>
> a) statutory priority claims are paid in full in cash.
>
> b) The beneficiaries of the KERP are to be paid in full and in cash.
>
> c) The claim of the DIP Lender will be partially satisfied through a combination of cash and interest bearing secured notes convertible at maturity into cash or common shares of the Purchaser.
>
> d) The Company's unsecured creditors will receive their pro rata share of a pool of interest bearing unsecured notes convertible at maturity into cash or common shares of the Purchaser.
>
> e) The Company will assume the Assumed Liability [IBM].
>
> In addition, the APA also provides funding for a bankruptcy of the Company or a continuation of the CCAA Proceedings in respect of the Company. As described in further detail below, it is anticipated that the Company will be assigned into bankruptcy and that the entitlement of the unsecured creditors to the unsecured convertible notes will be determined through the statutory claims process provided under the *Bankruptcy and Insolvency Act* ... It is anticipated that one unsecured note will be provided to a trustee in bankruptcy to be appointed in respect of the Company**.**

Is the consideration to be received for the assets reasonable and fair, taking into account their market value?

[52] In its Seventh Report the Monitor expressed its view that "the price obtained for the Company's assets is fair and reasonable in the circumstances". In the *Soundair* case Galligan J.A. stated:

> At the outset, I think that the fact that the OEL offer was the only acceptable one available to the receiver on March 8, 1991, after ten months of trying to sell the airline, is strong evidence that the price in it was reasonable.[7]

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[7] *Soundair, supra.*, p. 8g.

So, too, in this case. Although no valuation was filed in respect of the companies' assets, the evidence filed on previous motions disclosed that the applicants had made efforts for many months prior to initiating *CCAA* proceedings to secure further investment in or the sale of the companies. The state of the companies, and the potential business opportunity they offered, were extensively known. Notwithstanding the short SISP, the Monitor reported that contact was made with a large number of potentially interested parties. Only three bids resulted. Of those three, two were not treated as Qualified Bids. The record, especially the Monitor's Confidential Appendix, supported the selection of the DashRx offer as the Successful Bid. Against the backdrop of those efforts, I concluded that the proposed purchase price was fair and reasonable.

Does the proposed transaction satisfy the requirements of section 36(7) of the *CCCA*?

[53] The applicants did not sponsor a pension plan for its employees. With the payment of the statutory priority claims from the proceeds of sale, obligations under section 6(5)(a) of the *CCAA* will be satisfied.

C. Conclusion

[54] In sum, the proposed Purchase Agreement met the specific factors enumerated in section 36(3) of the *CCAA* and, when looked at as a whole in the particular circumstances of this case, represented a fair and reasonable transaction.[8] For those reasons I authorized the proposed Purchase Agreement and granted the vesting order which was sought.

VI. Analysis of the proposed distribution

[55] The distribution of the sale proceeds proposed by the Applicants, and supported by the Monitor, was straight-forward, save for one issue – the validity of Castcan's security in respect of HST Refunds.

A. The Castcan security issue described

[56] In its Seventh Report the Monitor described the Pari Passu Agreement which the DIP Lender had negotiated with two secured creditors, RBC and Castcan, at the time of putting in place the DIP Lending Facility:

> The Monitor has been advised that the DIP Lender entered into an agreement with Castcan and others, whereby the DIP Lender agreed that its claims against the Company would be subordinate to the claims of Castcan (the "Pari Passu Agreement"). Pursuant to the Pari Passu Agreement, Castcan has the right to be repaid in full before the DIP Lender receives any consideration for the amounts it advanced under the DIP Facility… The Monitor has been advised that the DIP Lender has agreed that its position will also be subordinate to RBC, as provided for in the Initial Order.

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[8] *White Birch Paper Holding Company*, 2010 QCCS 4915, paras. 48 and 49.

> Although the Purchaser was willing to assume the liabilities owed to RBC and Castcan, they both advised that they were not willing to become creditors of the Purchaser and wanted to be paid in cash in full on closing. In order to accommodate the secured creditors' requests, the DIP Lender has agreed to pay RBC and Castcan in full in cash from the amount payable to the DIP Lender pursuant to the terms of the APA. As a result of that payment, the DIP Lender will be subrogated to or take an assignment of the positions of RBC and Castcan in respect of their validly perfected and secured positions, subject to the lack of clarity in the law in respect of the Castcan Loan and Security discussed below.

[57] The lack of clarity in the law in respect of the Castcan Loan stemmed from the assignment of Crown debts, on a full recourse basis, made in the March 6, 2012 Factor Agreement between Castcan and the Applicants. The Crown debts assigned to Castcan included certain Scientific Research and Experimental Development ("SR&ED") refundable tax credit entitlements, Ontario Innovation Tax Credit ("OITC") refunds and harmonized sales tax ("HST") refunds. The Applicants executed a GSA in favour of Castcan to secure the obligations owing to Castcan, including those under the Factor Agreement.

[58] Counsel to the Monitor provided an opinion that the assignment of the SR&ED Tax Credits and the OITC Tax Credits under the Factor Agreement was valid and the security granted in each GSA in respect of such assignments was valid and enforceable.

[59] Section 67 of the *Financial Administration Act (Canada)*, R.S.C. 1985, c. F-11 (the "*FAA*") provides as follows:

> Except as provided in this Act or any other Act of Parliament,
>
> (a) a Crown debt is not assignable; and
>
> (b) no transaction purporting to be an assignment of a Crown debt is effective so as to confer on any person any rights or remedies in respect of that debt.

In light of that section, counsel to the Monitor advised that the HST Refunds might not be assignable and that the security granted in respect of the HST Refunds might not be valid and enforceable because no provision in the *Excise Tax Act* (Canada) or the *FAA* exempted the HST Refunds from section 67 of the *FAA*.

[60] Castcan took the position that certain provisions in the Factor Agreement entitled it, in any event, to receive the HST Refunds. The Monitor commented on part of the argument advanced by Castcan:

> Section 12 of the Factor Agreement provides that if any right or entitlement that, as a matter of law is not assignable, the Company will: (a) co-operate with Castan to provide the benefits of these Non-Assignable Rights to Castcan, including, holding them in trust; (b) enforce any rights of Castcan arising from these Non-Assignable Rights; (c) take all actions to ensure that the value of these Non-Assignable Rights are preserved; and (d) pay over to Castcan all monies collected in respect of these Non-Assignable Rights. One interpretation is that the obligations set out in Section 12 of the Factor

> Agreement with respect to the HST Refunds are enforceable and are secured by the GSAs. Another interpretation is that Section 12 simply gives rise to a claim in equity against the Company and that such an equitable claim may not be secured by the GSAs.
>
> The Monitor is of the view that there is strong argument that Castcan has a claim against the Company for unjust enrichment and, to the extent of such unjust enrichment, a Court may order that a constructive trust applies to the monies advanced by Castcan in respect of the HST Refunds.
>
> Given the provisions of the FAA and existing case law, counsel to the Monitor has advised that it cannot conclude with certainty that the obligations in the Factor Agreement in favour of Castcan with respect to the HST Refunds are secured by the GSAs. Accordingly, the Monitor is of the view that it is unclear whether any payment by the Company to Castcan in respect of the HST Refunds should be made in priority to other creditors.
>
> The Monitor is of the view that the equities clearly favour paying Castcan the full amount owed to it under the Factor Agreement, including the amounts in respect of the HST Refunds. The Monitor notes that Castcan paid $1,000,000 to the Company in good faith on a full recourse basis at a time when the Company was in dire need of liquidity. The vast majority of the amounts paid by Castcan were used to fund the Company's payroll. In the Monitor's view, it would be inequitable for the Company or any of its creditors to get a windfall at the expense of a creditor that provided value to the Company as a result of lack of clarity in the existing law and the wording of the Factor Agreement.

[61] The Applicants proposed that upon paying out the claims of the Senior Secured Creditors from the cash proceeds received on closing, the DIP Lender would be subrogated to and/or take an assignment of the Senior Secured Creditor's claims. The Applicants also sought an order which provided, in part, that they, or the proposed Trustee, pay to the DIP Lender any tax credit entitlements received in respect of the HST Refund, notwithstanding section 67 of the *FAA*. The Monitor explained the rationale for this request:

> The DIP Lender is of the view that since there is likely no secondary market for the secured convertible notes, the net present value of the secured convertible notes is less than the face value of such notes. As a result, the DIP Lender is taking the position that the consideration it is receiving is insufficient to satisfy the full amount of the DIP Lender's claim against the Company. The DIP Lender is also of the view that the DIP Lender's Charge should continue to secure the obligations owing to the DIP Lender as a result of its shortfall after distribution of the proceeds to it on closing of the transaction contemplated by the APA. The Monitor supports the DIP Lender's views.
>
> The DIP Lender is also of the view that the value of the notes should be discounted by an amount that is at least as great as the amount of the HST Refunds in order to permit the proceeds of the HST Refunds once received by the estate to be paid to the DIP Lender on account of its DIP Charge. The Monitor supports the DIP Lender's views with respect to the DIP Lender's Charge. Accordingly, the Monitor is of the view that

the DIP Lender's Charge should remain effective over all of the Excluded Assets until such time as such refunds are received and become proceeds of the estate and the DIP Lender is repaid in full.

The parties with an economic interest in the proceeds of the transaction and the Tax Credit Entitlements have agreed to the arrangement with the DIP Lender described above with respect to the HST Refunds. Such an arrangement will permit the DIP Lender to satisfy its obligations under the Pari Passu Agreement while still receiving the consideration that was agreed to be paid to it pursuant to the APA.

B. Legal analysis

[62] Section 67 of the *FAA* provides that "no transaction purporting to be an assignment of a Crown debt is effective" except as provided in that Act or any other federal Act. In *Mazetti v. Marzetti* the Supreme Court of Canada held that under section 67 "a purported assignment of a Crown debt is rendered absolutely ineffective, as between debtor and creditor, and as between assignor and assignee."[9] The Court of Appeal, in *Profitt v. A.D. Productions Ltd. (Trustee of)*, held that purported assignments of federal sales tax refunds were invalid.[10]

[63] In their factum the Applicants pointed to several cases which they contended might limit the application of the decisions in *Mazetti* and *Profitt*.[11] Castcan had submitted to the Monitor that several provisions of the Factor Agreement operated to give it priority to the HST Refund notwithstanding the *Mazetti* and *Profitt* decisions. I did not need to address those points to decide the motion. Assuming, for purposes of argument, the ineffectiveness of Castcan's security as it related to the HST Refund, that refund would constitute property of the Applicants. Pursuant to the Initial Order the DIP Lender was granted a charge on the "Property" of the Applicants which was defined as the Applicants' "current and future assets, undertakings and properties of every nature and kind whatsoever, and wherever situate including all proceeds thereof". The "Property" of the applicants included their entitlement to the HST Refund. Accordingly, in the event of a failure of Castcan's security, the DIP Lender would be entitled to the HST Refund.

[64] Section 67 of the *FAA* does not prevent such a result since it only renders ineffective any "*transaction* purporting to be an assignment of a Crown debt". The DIP Lender's Charge created by the Initial Order was not such a "transaction". As the Supreme Court of Canada pointed out in *Bank of Montreal v. i Trade Finance Inc.*, rights which result from a court order are not rights stemming from a "transaction".[12] Section 67 of the *FAA* does not apply to rights

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[9] [1994] 2 S.C.R. 765, para. 99.
[10] (2002), 32 C.B.R. (4th) 94 (O.C.A.), para. 28.
[11] *Cargill Ltd. v. Ronald (Trustee of)* (2007), 32 C.B.R. (5th) 169 (Man. C.A.); *McKay & Maxwell, Ltd., Re* (1927), 8 C.B.R. 534 (N.S.S.C.); *Christensen, Re* (1961), 2 C.B.R. (N.S.) 324 (Ont. S.C.); *Front Iron & Metal Co., Re* (1980), 38 C.B.R. (N.S.) 317 (Ont. S.C.).
[12] [2011] 2 S.C.R. 360, para. 30. See also, *Torstar Corp. v. ITI Information Technology Institute Inc.* (2002), 36 C.B.R. (4th) 114 (N.S.S.C.), paras. 29 and 32.

created by a court order, including a DIP lending charge granted over all of a company's property pursuant to section 11.2(1) of the *CCAA*.

[65] Since the DIP Lender would be entitled to the HST Refund in the event of a defect in Castcan's security, it was open to the DIP Lender to agree, with Castcan, as a matter of contract, that Castcan should receive full payout as contemplated by the Pari Passu Agreement.

[66] As to the Applicants' request for an order that they, or the proposed Trustee, pay to the DIP Lender any tax credit entitlements received in respect of the HST Refund, I was satisfied that it was appropriate to exercise my discretion under section 11 of the *CCAA* to make such an order. I accepted the Monitor's view that the DIP Lender was entitled to be repaid in full upon the conclusion of the *CCAA* proceedings and that its charge should continue to secure the obligations to it as a result of the shortfall after distribution of the transaction proceeds. The use of the Secured Note to repay the DIP Lender entails a risk that the DIP Lender might not receive full repayment of its DIP Lending Facility. Consequently, I accepted the Monitor's view that it would be appropriate to discount the value of the note by an amount equal to the HST Refund. Such a result promotes, in part, the remedial purposes of the *CCAA* by ensuring that DIP lenders, whose role often is critical to the successful completion of a re-organization, can advance interim financing with the reasonable assurance of receiving repayment of their DIP loans.

[67] As to the distribution of $100,000 of the sales proceeds to fund bankruptcy proceedings involving the Applicants, I accepted the Monitor's view that since no further funds existed to continue the *CCAA* proceedings, a bankruptcy would serve as the most cost effective and efficient way in which to complete the winding-up of the companies' affairs, including establishing a mechanism to determine the quantum for unsecured claims.

[68] For those reasons I approved the distribution of the sale proceeds proposed by the Applicants, as well as the related orders terminating the *CCAA* proceedings upon the Monitor filing its discharge certificate and approving the Monitor's Seventh Report and the activities described therein.

VII. Sealing order

[69] The information contained in the Confidential Appendix to the Monitor's Seventh Report clearly met the criteria for a sealing order set out in *Sierra Club of Canada v. Canada (Minister of Finance)*.[13] In order to protect the integrity of the SISP and the proposed sales transaction, I granted an order that the appendix be sealed until the completion of the Purchase Agreement transaction.

(original signed by)

D. M. Brown J.

Date: June 9, 2012

[13] [2002] 2 S.C.R. 522.